



# Chong Hing Bank Limited

(incorporated with limited liability in Hong Kong)

## U.S.\$225,000,000 6.000% Subordinated Notes due 2020

**Issue Price: 99.488%**

The 6.000% Subordinated Notes due 2020 (the “Notes”) will be issued in an initial aggregate principal amount of U.S.\$225,000,000 by Chong Hing Bank Limited (the “Issuer” or the “Bank”). Subject as provided below, the Notes will bear interest at the rate of 6.000% per annum from and including 4 November 2010 to, but excluding, 4 November 2020, payable semi-annually in arrear on 4 May and 4 November of each year (each an “Interest Payment Date”), provided however, that from and including the Interest Payment Date on which a Change in Status Notice (as defined in Condition 3(4) of the Notes) becomes effective pursuant to Condition 3(4) of the Notes, the rate of interest on the Notes shall be reduced by 0.500% per annum. For the avoidance of doubt, the rate of interest on the Notes upon a Change in Status Notice becoming effective shall be 5.500% per annum.

The Notes will mature on 4 November 2020, if not redeemed or purchased and cancelled earlier. Subject to satisfaction of certain regulatory approval requirements (if applicable), the Notes will be redeemable at the option of the Issuer in whole but not in part, at a redemption price equal to their principal amount together with accrued and unpaid interest to the date fixed for redemption, upon the occurrence of certain changes in taxation in Hong Kong requiring the payment of additional amounts. See “*Terms and Conditions of the Notes — Redemption and Purchase*”.

Subject as provided below, the Notes will constitute direct, unsecured and subordinated obligations of the Issuer and will rank *pari passu* without any preference among themselves and at least equally with all other outstanding unsecured and subordinated obligations of the Issuer. Upon a Change in Status Notice becoming effective, the Notes shall cease to constitute subordinated obligations of the Issuer and shall thereafter constitute direct, unconditional, unsubordinated and (subject to Condition 4 of the Notes) unsecured obligations of the Issuer and shall at all times thereafter rank *pari passu* and without any preference among themselves. The payment obligations of the Issuer under the Notes shall, save for such exceptions as may be provided by applicable legislation and subject to Condition 4 of the Notes, at all times thereafter rank at least equally with all its other present and future unsecured and unsubordinated obligations including liabilities in respect of deposits. See “*Terms and Conditions of the Notes — Status*”.

The Notes are expected to be rated “Baa3” by Moody’s Investors Service, Inc. (“Moody’s”) and “BBB” by Fitch Ratings Ltd. (“Fitch”). A rating is not a recommendation to buy, sell or hold Notes and maybe subject to revision, suspension or withdrawal at any time by the assigning rating organisation.

See “*Investment Considerations*” beginning on page 13 for a discussion of certain considerations to be taken into account in connection with an investment in the Notes.

Application has been made to The Stock Exchange of Hong Kong Limited (the “HKSE”) for the listing of, and permission to deal in, the Notes by way of selectively marketed securities (as defined in the Rules Governing the Listing of Securities on the HKSE (the “Listing Rules”)) and such permission is expected to become effective on 5 November 2010.

Hong Kong Exchanges and Clearing Limited and the HKSE takes no responsibility for the contents of this Offering Circular, makes no representation as to its accuracy or completeness and expressly disclaims any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this Offering Circular.

The Notes have not been and will not be registered under the United States Securities Act of 1933, as amended (the “Securities Act”) and, subject to certain exceptions, may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons (as defined in Regulation S under the Securities Act (“Regulation S”)). The Notes are being offered and sold only outside the United States in accordance with Regulation S.

The Notes will be initially evidenced by a global certificate (the “Global Certificate”) in registered form, which will be registered in the name of a nominee of, and deposited with a common depositary for, Euroclear Bank SA/NV (“Euroclear”) and Clearstream Banking, société anonyme (“Clearstream, Luxembourg”) on or about 4 November 2010 (the “Closing Date”). Beneficial interests in the Global Certificate will be shown on, and transfers thereof will be effected only through, the records maintained by Euroclear and Clearstream, Luxembourg and their respective accountholders. Except in the limited circumstances set out herein, individual certificates for Notes will not be issued in exchange for beneficial interests in the Global Certificate. See “*The Global Certificate*”.

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*Joint Bookrunners and Joint Lead Managers*

**Goldman Sachs (Asia)  
L.L.C.**

**HSBC**

**UBS**

Offering Circular dated 28 October 2010

## IMPORTANT NOTICE

The contents of this document have not been reviewed by any regulatory authority in Hong Kong. You are advised to exercise caution in relation to the offer of Notes. If you are in any doubt about any of the contents of this document, you should obtain independent professional advice.

This Offering Circular includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Issuer and the Notes. The Issuer, having made all reasonable enquiries, confirms that (i) this Offering Circular contains all information with respect to the Issuer and the Issuer's subsidiaries (collectively, the "**Group**"), and the issue of the Notes, which is material in the context of the issue and offering of the Notes; (ii) the statements contained herein relating to the Issuer and the Group are in every material respect true and accurate and not misleading; (iii) the opinions and intentions expressed in this Offering Circular with regard to the Issuer and the Group are honestly held, have been reached after considering all relevant circumstances and are based on reasonable assumptions; (iv) there are no other facts in relation to the Issuer, the Group or the Notes, the omission of which would, in the context of the issue and offering of the Notes (the "**Offering**"), make any statement in this Offering Circular misleading in any material respect; and (v) all reasonable enquiries have been made by the Issuer to ascertain such facts and to verify the accuracy of all such information and statements. In addition, the Issuer accepts full responsibility for the accuracy of the information contained in this Offering Circular.

This Offering Circular has been prepared by the Issuer solely for use in connection with the proposed offering of the Notes described in this Offering Circular. The distribution of this Offering Circular and the offering of the Notes in certain jurisdictions may be restricted by law. Persons into whose possession this Offering Circular comes are required by the Issuer and the joint lead managers as set forth in "Subscription and Sale" (the "**Joint Lead Managers**") to inform themselves about and to observe any such restrictions. No action is being taken to permit a public offering of the Notes or the distribution of this Offering Circular in any jurisdiction where action would be required for such purposes. There are restrictions on the offer, sale and resale of the Notes, and the circulation of documents relating thereto, in certain jurisdictions including, without limitation, the United States, the United Kingdom, Hong Kong, Singapore, Japan and Italy, and to persons connected therewith. For a description of certain further restrictions on offers, sales and resales of the Notes and distribution of this Offering Circular, see "*Subscription and Sale*".

No person has been or is authorised to give any information or to make any representation concerning the Issuer, the Group or the Notes other than as contained herein and, if given or made, any such other information or representation should not be relied upon as having been authorised by the Issuer, the Joint Lead Managers, the Trustee or the Agents (each as defined in the Terms and Conditions of the Notes). Neither the delivery of this Offering Circular nor any offering, sale or delivery made in connection with the issue of the Notes shall, under any circumstances, constitute a representation that there has been no change or development reasonably likely to involve a change in the affairs of the Issuer, the Group or any member of the Group since the date hereof or create any implication that the information contained herein is correct as at any date subsequent to the date hereof. This Offering Circular does not constitute an offer of, or an invitation by or on behalf of the Issuer, the Joint Lead Managers, the Trustee or the Agents to subscribe for or purchase any of the Notes and may not be used for the purpose of an offer to, or a solicitation by, anyone in any jurisdiction or in any circumstances in which such offer or solicitation is not authorised or is unlawful.

No representation or warranty, express or implied, is made or given by the Joint Lead Managers, the Trustee, the Agents or their affiliates or advisers as to the accuracy, completeness or sufficiency of the information contained in this Offering Circular. To the fullest extent permitted by law, none of the Joint Lead Managers, the Trustee or the Agents accept any responsibility for the contents of the Offering Circular or for any other statement, made or purported to be made by the Joint Lead Managers, the Trustee or the Agents or on its behalf in connection with the Issuer or the issue and offering of the Notes. Each of the Joint Lead Managers, the Trustee and the Agents accordingly

disclaims all and any liability whether arising in tort or contract or otherwise (save as referred to above) which it might otherwise have in respect of the Offering Circular or any such statement. Neither the Offering Circular nor any other financial statements are intended to provide the basis of any credit or other evaluation and should not be considered as a recommendation by any of the Issuer, the Joint Lead Managers, the Trustee, the Agents or their affiliates or advisers that any recipient of the Offering Circular or any other financial statements should purchase the Notes. Each potential purchaser of Notes should determine for itself the relevance of the information contained in the Offering Circular and its purchase of Notes should be based upon such investigation as it deems necessary. None of the Joint Lead Managers, the Trustee or the Agents undertakes to review the financial condition or affairs of the Issuer during the life of the arrangements contemplated by the Offering Circular nor to advise any investor or potential investor in the Notes of any information coming to the attention of any of the Joint Lead Managers, the Trustee or the Agents.

**IN CONNECTION WITH THIS ISSUE, THE HONGKONG AND SHANGHAI BANKING CORPORATION LIMITED (OR ANY PERSON ACTING ON ITS BEHALF) MAY OVERALLOT OR EFFECT TRANSACTIONS WITH A VIEW TO SUPPORTING THE MARKET PRICE OF THE NOTES AT A LEVEL HIGHER THAN THAT WHICH MIGHT OTHERWISE PREVAIL. HOWEVER, THE HONGKONG AND SHANGHAI BANKING CORPORATION LIMITED (OR ANY PERSON ACTING ON ITS BEHALF) IS NOT OBLIGED TO UNDERTAKE STABILISATION ACTION. ANY STABILISATION ACTION MAY BEGIN ON OR AFTER THE DATE ON WHICH ADEQUATE PUBLIC DISCLOSURE OF THE TERMS OF THE OFFER OF THE NOTES IS MADE AND, IF BEGUN, MAY BE ENDED AT ANY TIME, BUT IT MUST END NO LATER THAN THE EARLIER OF 30 DAYS AFTER THE CLOSING DATE AND 60 DAYS AFTER THE DATE OF THE ALLOTMENT OF THE NOTES. ANY STABILISATION ACTION OR OVER-ALLOTMENT SHALL BE CONDUCTED IN ACCORDANCE WITH ALL APPLICABLE LAWS AND RULES.**

Any purchase or acquisition of the Notes is in all respects conditional on the satisfaction of certain conditions set out in the Subscription Agreement (as defined in “*Subscription and Sale*”) and the issue of the Notes by the Issuer to the Joint Lead Managers pursuant to the Subscription Agreement. Any offer, invitation to offer or agreement made in connection with the purchase or acquisition of the Notes pursuant to this Offering Circular shall (without liability or responsibility on the part of the Issuer or the Joint Lead Managers) lapse and cease to have any effect if (for any reason whatsoever) the Notes are not issued by the Issuer to the Joint Lead Managers pursuant to the Subscription Agreement.

In making an investment decision, investors must rely on their own examination of the Issuer, the Group and the terms of the offering of the Notes, including the merits and risks involved. See “*Investment Considerations*” for a discussion of certain considerations to be taken into account in connection with an investment in the Notes.

Each person receiving this Offering Circular acknowledges that such person has not relied on the Joint Lead Managers, the Trustee or the Agents or any person affiliated with the Joint Lead Managers, the Trustee or the Agents in connection with its investigation of the accuracy of such information or its investment decision.

## CERTAIN DEFINED TERMS AND CONVENTIONS

Unless otherwise specified or the context requires otherwise, references herein to the “**Issuer**” or the “**Bank**” are to Chong Hing Bank Limited and its consolidated subsidiaries.

Unless otherwise specified or the context requires, references herein to “**Hong Kong dollars**”, “**HK dollars**” and “**HK\$**” are to the lawful currency of the Hong Kong Special Administrative Region of the People’s Republic of China (“**Hong Kong**”), references herein to “**U.S. dollars**” or “**U.S.\$**” are to the lawful currency of the United States of America, references herein to “**Renminbi**” or “**RMB**” are to the lawful currency of the People’s Republic of China, references to “**Mainland China**” and the “**PRC**” are to the People’s Republic of China excluding Hong Kong, Macau and Taiwan, references to “**HKFRSs**” are to Hong Kong Financial Reporting Standards and references to “**IFRS**” are to International Financial Reporting Standards.

Unless otherwise specified, where financial information as at and for the six months ended 30 June 2010 has been translated into U.S. dollars, it has been so translated for information purposes only at the rate of HK\$7.7853 equal to U.S.\$1.00 (being the average of the buying and selling rates of the opening indicative counter exchange rate published by the Hong Kong Association of Banks as at 30 June 2010), and for financial information as at and for the year ended 31 December 2009, it has been so translated for information purposes only at the rate of HK\$7.755 equal to U.S.\$1.00 (being the average of the buying and selling rates of the opening indicative counter exchange rate published by the Hong Kong Association of Banks as at 31 December 2009). No representation is made that the Hong Kong dollar or U.S. dollar amounts referred herein could have been or could be converted into Hong Kong dollars or U.S. dollars, as the case may be, at any particular rate or at all.

## PRESENTATION OF FINANCIAL INFORMATION

The Bank has prepared audited consolidated financial statements for the years ended 31 December 2007, 2008 and 2009 and unaudited consolidated interim financial statements for the six months ended 30 June 2009 and 2010 in accordance with HKFRSs. Unless otherwise specified, the financial information set out in this Offering Circular is presented on a consolidated basis for the Bank and its subsidiaries.

In this Offering Circular, where information has been presented in thousands or millions of units, amounts may have been rounded up or down. Accordingly, totals of columns or rows of numbers in tables may not be equal to the apparent total of the individual items and actual numbers may differ from those contained herein due to rounding. References to information in billions of units are to the equivalent of a thousand million units.

## FORWARD-LOOKING STATEMENTS

This Offering Circular contains forward-looking statements regarding the intent, belief or current expectations of the Bank held reasonably with respect to its financial condition and future results of operations. In many cases, but not all, words such as “anticipate”, “believe”, “estimate”, “expect”, “intend”, “may”, “plan”, “probability”, “project”, “risk”, “seek”, “should”, “target” and similar expressions are used in relation to the Bank to identify forward-looking statements. Investors can also identify forward-looking statements in discussions of strategy, plans or intentions. These statements reflect the current views of the Bank with respect to future events and are subject to risks, uncertainties and assumptions. Should one or more of these risks or uncertainties materialise, or should underlying assumptions prove incorrect, the Bank’s actual results may vary materially from those it currently anticipates. Given these risks and uncertainties, prospective investors are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date of this Offering Circular. The Bank disclaims any obligation to update, or to announce publicly any revision to, any of the forward-looking statements contained in this Offering Circular to reflect future actual events or developments. The information contained in this Offering Circular, including without limitation the information under “*Investment Considerations*” and “*Business of the Bank*”, identifies important factors that might cause the forward-looking statements not to be realised.

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## SUMMARY

*The following summary is qualified in its entirety by, and is subject to, the detailed information contained or referred to elsewhere in this Offering Circular. For a discussion of certain considerations that should be made in connection with an investment in the Notes, see “Investment Considerations”.*

The Bank is a full service bank which operates primarily in Hong Kong. As at the date of this Offering Circular, the Bank had an established network comprising a head office and a total of 54 branches, including 51 branches in Hong Kong, 3 overseas branches located in Shantou, Macau and San Francisco, and 2 representative offices located in Guangzhou and Shanghai.

The Bank provides a wide range of corporate and retail banking services and other related financial services. Corporate and retail banking services provided by the Bank include lending and trade finance facilities, consumer financing, overdraft facilities, mandatory provident fund services, provision of fixed deposits, current and savings accounts, credit card services and personal wealth management services. Other related financial services offered by the Bank include remittance and money exchange, safe deposit boxes, auto pay and direct debit services. The Bank is also engaged in treasury activities and securities dealing activities, which include inter-bank placement and deposit transactions, the management of overall interest rate risk and liquidity of the Bank and centralised cash management as well as other business activities such as investment holding and property investment. The Bank also offers futures and securities trading and insurance services through certain of its wholly-owned subsidiaries.

Since its inception in 1948, the Bank has expanded steadily and believes that it has successfully established itself as a reliable and prudent bank in Hong Kong as well as the other jurisdictions in which it operates. Despite its relatively small size, the Bank enjoys long-standing relationships with many of its key customers and believes that it possesses a strong and stable deposit base. As at 30 June 2010, the Bank's total assets, shareholders' funds, advances to customers and customer deposits amounted to HK\$70,728 million (U.S.\$9,085 million), HK\$6,287 million (U.S.\$808 million), HK\$35,553 million (U.S.\$4,567 million) and HK\$60,515 million (U.S.\$7,773 million), respectively.

For the year ended 31 December 2009 and the six months ended 30 June 2010, the Bank recorded a net profit of HK\$232 million (U.S.\$30 million) and HK\$193 million (U.S.\$25 million), respectively. As at 30 June 2010, the Bank's capital adequacy ratio, loan-to-deposit ratio and average liquidity ratio were 15.24%, 53.81% and 45.01%, respectively. For the six months ended 30 June 2010, the Bank achieved an annualised return on average assets of 0.59% and a return on average shareholders' funds of 6.23%. See “Summary Financial and Other Information — Other Selected Financial Data”.

The Bank maintains correspondent banking relationships with approximately 300 foreign banks and provides services such as Hong Kong dollar clearing services for foreign banks that maintain Hong Kong dollar and/or U.S. dollar accounts with the Bank, negotiation and advisory services in relation to letters of credit as well as trade enquiries, transfers and remittances.

The Bank has been listed on the HKSE since July 1994. As at 30 June 2010, the authorised share capital of the Bank was 600 million ordinary shares of HK\$0.50 each, of which 435 million ordinary shares have been issued and are outstanding and fully paid. Based on the closing price of its shares on the HKSE on 30 June 2010, the Bank had a market capitalisation of approximately HK\$6,473 million.

The Bank's long-term strategy is to continue to strengthen its foundation, enhance its overall competitiveness, expand its operations both locally and overseas and provide its customers with quality financial and banking products and services. The Bank has formulated a strategic plan for the years 2009 to 2013 governing the direction and strategies for the Bank's future business development and growth.

The major components of the strategic plan are as follows:

- position the Bank as a community bank in retail banking sector and seek opportunities to open branches in areas where the customers are underserved by the large banks;
- expand the Bank's deposits base by introducing new deposit products and enhancing its services;
- improve and diversify the Bank's customer mix and income sources;
- prudently increase the Bank's credit portfolios by leveraging the Bank's close relationship with Hong Kong corporations and residents by serving their financial needs through various stages of economic cycle; and
- increase non-interest income by enhancing the Bank's existing services.



## THE OFFERING

The following is a brief summary of certain terms of this Offering. For a more detailed description of the terms of the Notes, see “Terms and Conditions of the Notes”. Capitalised terms used herein and not defined have the meanings given to them in “Terms and Conditions of the Notes”.

<b>The Issuer</b> .....	Chong Hing Bank Limited, a company incorporated with limited liability in Hong Kong.
<b>The Notes</b> .....	U.S.\$225,000,000 6.000% Subordinated Notes due 2020.
<b>Issue Price</b> .....	99.488%
<b>Interest</b> .....	The Notes will bear interest at the rate of 6.000% per annum, provided however, that from and including the Interest Payment Date immediately on which a Change in Status Notice becomes effective pursuant to Condition 3(4) of the Notes, the rate of interest on the Notes shall be reduced by 0.500% per annum. For the avoidance of doubt, the rate of interest on the Notes upon a Change in Status Notice becoming effective shall be 5.500% per annum. Interest on the Notes is payable semi-annually in arrear on 4 May and 4 November in each year, commencing on the Interest Payment Date falling in May 2011.
<b>Interest Payment Dates</b> .....	The 4th day of May and November of each year up to and including 4 November 2020 (each an “ <b>Interest Payment Date</b> ”).
<b>Maturity Date</b> .....	The Interest Payment Date falling on 4 November 2020.
<b>Final Redemption</b> .....	Unless previously redeemed or purchased and cancelled, the Notes will mature and become payable at their principal amount on the Maturity Date.
<b>Use of Proceeds</b> .....	The Notes are intended to qualify as “Category II Supplementary Capital” of the Bank for purpose of capital adequacy under Part XVII of the Hong Kong Banking Ordinance (Cap. 155). The issuance of the Notes will strengthen the Bank’s capital base and fund the growth of the Bank’s operations. See “ <i>Use of Proceeds</i> ” .
<b>Status of the Notes</b> .....	Subject as provided below, the Notes constitute direct, unsecured and subordinated obligations of the Issuer, ranking pari passu without any preference among themselves.



The claims of the holders of the Notes will, in the event of the winding up of the Issuer, be subordinated in right of payment in the manner provided in the Trust Deed to the claims of depositors and all other unsubordinated creditors of the Issuer and will rank, in the event of the winding up of the Issuer, at least equally in right of payment with all other Subordinated Indebtedness, present and future, of the Issuer. Claims in respect of the Notes will rank in priority to the rights and claims of holders of subordinated liabilities which by their terms rank in right of payment junior to the Notes and all classes of equity securities of the Issuer, including holders of preference shares, if any.

If at any time (on or) after 1 January 2013, the HKMA decides (having regard to the applicable regulatory framework) that the Notes no longer fully qualify as term subordinated debt for inclusion in Category II — Supplementary Capital of the Issuer, the Issuer may (in accordance with Condition 3(4) of the Notes) at its option and subject to the prior written approval of the HKMA, provide notice to such effect to Noteholders (in accordance with Condition 13), such notice a “**Change in Status Notice**”. Upon a Change in Status Notice becoming effective, the Notes shall cease to constitute subordinated obligations of the Issuer and shall thereafter constitute direct, unconditional, unsubordinated and (subject to Condition 4 of the Notes) unsecured obligations of the Issuer and shall at all times thereafter rank *pari passu* and without any preference among themselves. The payment obligations of the Issuer under the Notes shall, save for such exceptions as may be provided by applicable legislation and subject to Condition 4 of the Notes, at all times thereafter rank at least equally with all its other present and future unsecured and unsubordinated obligations including liabilities in respect of deposits.

**Events of Default and  
Enforcement . . . . .**

The following will constitute events of default (each a “**Subordinated Note Event of Default**”) with respect to the Notes until (but excluding) the date on which a Change in Status Notice becomes effective pursuant to Condition 3(4):

- (a) if default is made in the payment of principal or interest due in respect of the Notes or any of them and the default continues for a period of five Business Days in Hong Kong (in the case of principal) or ten Business Days in Hong Kong (in the case of interest), then the Trustee at its discretion may, subject as provided in Condition 11(2), in order to enforce payment without further notice, institute proceedings for the winding up of the Issuer in Hong Kong, but may take no further action in respect of such default (but without prejudice to Condition 11(2)); or

- (b) if an order is made or an effective resolution is passed for the winding up, liquidation or dissolution of the Issuer in Hong Kong (except for the purposes of a reconstruction, amalgamation or reorganisation the terms of which have previously been approved by an Extraordinary Resolution (as defined in the Trust Deed) of the Noteholders), then the Trustee at its discretion may give written notice to the Issuer that the Notes are, and they shall forthwith thereupon become, immediately due and repayable at their principal amount together with accrued interest as provided in the Trust Deed.

From and including the date on which a Change in Status Notice becomes effective pursuant to Condition 3(4), the Notes will contain certain events of default (each a “**Senior Note Event of Default**”), including a cross default provision as further described in Condition 10(2) of the Notes.

The Trustee may, subject as provided below, at its discretion and without further notice, institute such proceedings against the Issuer as it may think fit to enforce any obligation, condition or provision binding on the Issuer under the Notes or the Trust Deed (other than any obligation for the payment of any principal or interest in respect of the Notes), provided that the Issuer shall not as a consequence of such proceedings be obliged to pay any sum or sums representing or measured by reference to principal or interest in respect of the Notes sooner than the same would otherwise have been payable by it.

The Trustee shall not be bound to take action upon any Subordinated Note Event of Default or Senior Note Event of Default or as referred to in Condition 10 or in the preceding paragraph unless (i) it shall have been so requested in writing by Noteholders holding at least one-quarter of the principal amount of the Notes then outstanding or if so directed by an Extraordinary Resolution of the Noteholders and (ii) it shall have been indemnified and/or secured to its satisfaction by the Noteholders.

No Noteholder shall be entitled to proceed directly against the Issuer unless the Trustee having become bound so to proceed, fails to do so within a reasonable period and such failure is continuing.

**Redemption for Taxation****Reasons** .....

Upon obtaining the approval of the HKMA (if required) and satisfying the Trustee immediately before the giving of the notice referred to below that (a) as a result of any change in, or amendment to, the laws or regulations in Hong Kong, or any change in the official interpretation of the laws or regulations in Hong Kong, which change or amendment becomes effective after 28 October 2010, on the occasion of the next payment due in respect of the Notes the Issuer would be required to pay additional amounts, and (b) the requirement cannot be avoided by the Issuer taking reasonable measures available to it, the Issuer may at its option, having given not less than 30 nor more than 60 days' notice to the Noteholders, redeem all the Notes, but not some only, at any time at their principal amount together with interest accrued to but excluding the date of redemption, provided that, prior to the Optional Redemption Date, no such notice of redemption shall be given earlier than 90 days before the earliest date on which the Issuer would be required to pay the additional amounts were a payment in respect of the Notes then due. See "*Terms and Conditions of the Notes — Redemption and Purchase — Redemption for Taxation Reasons*".

**Trustee** .....

DB Trustees (Hong Kong) Limited

**Trust Deed** .....

The Notes will be constituted by a Trust Deed to be dated 4 November 2010 between the Issuer and the Trustee.

**Form and Denomination** .....

The Notes will be issued in registered form in denominations of U.S.\$100,000 each and integral multiples of U.S.\$1,000 in excess thereof. The Notes will initially be represented by the Global Certificate, in registered form, deposited on or about the Closing Date with, and registered in the name of a nominee of, a common depositary for Euroclear and Clearstream, Luxembourg.

Beneficial interests in the Global Certificate will be shown on, and transfer thereof will be effected only through, the records maintained by Euroclear and Clearstream, Luxembourg and their respective accountholders. Except as described herein, definitive certificates of Notes will not be issued in exchange for beneficial interests in the Global Certificate. See "*The Global Certificate — Change of Registration of Title*".

<b>Payments</b> .....	All payments of principal and interest by the Issuer will be made without withholding or deduction for, or on account of, any present or future taxes or duties of whatever nature imposed by or on behalf of Hong Kong or any political subdivision or taxing authority thereof or therein, unless the withholding or deduction of such taxes or duties is required by law. In that event, the Issuer will pay such additional amounts as may be necessary in order that the net amounts received by the holder of a Note, after such withholding or deduction, shall be equal to the respective amounts of principal or interest that would have been received in respect of such Note in the absence of such withholding or deduction, subject to certain exceptions.
<b>Ratings</b> .....	The Notes are expected to be rated “Baa3” by Moody’s and “BBB” by Fitch. A rating is not a recommendation to buy, sell or hold the Notes and may be subject to revision, suspension or withdrawal at any time by the assigning rating organisation.
<b>Governing Law</b> .....	The Notes and the Trust Deed and any non-contractual obligations arising out of or in connection with them are governed by, and shall be construed in accordance with, English law, except that the provisions of the Notes and the Trust Deed relating to subordination shall be governed by the Laws of Hong Kong.
<b>Listing</b> .....	Application has been made to list the Notes as selectively marketed securities on the HKSE.
<b>Selling Restrictions</b> .....	There are restrictions on the distribution of this Offering Circular and the making of solicitations pursuant thereto in certain jurisdictions, including, among others, the United States, the United Kingdom, Hong Kong, Singapore, Japan and Italy. See “ <i>Subscription and Sale</i> ” .

## SUMMARY FINANCIAL AND OTHER INFORMATION

### Summary Consolidated Financial and Other Information Relating to the Bank

The following tables set forth the summary consolidated financial information relating to the Bank as at and for the years ended 31 December 2007, 2008 and 2009 and the six months ended 30 June 2009 and 2010, which have been extracted from and restated as appropriate, and should be read in conjunction with, the Bank's audited consolidated financial statements for the years ended 31 December 2007, 2008 and 2009 and the Bank's unaudited consolidated interim financial statements for the six months ended 30 June 2009 and 2010, respectively. The Bank has prepared and presented its audited consolidated financial statements for the years ended 31 December 2007, 2008 and 2009 in accordance with HKFRSs applicable, respectively, as at 31 December 2007, 2008 and 2009. The Bank's financial results for any past period are not and should not be taken as an indication of the Bank's performance, financial position and results of operations in future years.

### CONSOLIDATED INCOME STATEMENTS

	Years ended 31 December			Six months ended 30 June	
	2007	2008	2009	2009	2010
	<i>(HK\$ thousands, except for earnings per share)</i>			<i>(HK\$ thousands, except for earnings per share)</i>	
Interest income .....	3,310,484	2,171,336	1,184,922	607,759	558,193
Interest expense .....	(2,339,871)	(1,307,010)	(361,591)	(211,229)	(146,725)
Net interest income .....	970,613	864,326	823,331	396,530	411,468
Fees and commission income .....	326,641	265,220	307,299	137,657	133,915
Fees and commission expense .....	(43,229)	(48,419)	(43,670)	(20,667)	(24,182)
Net fee and commission income ....	283,412	216,801	263,629	116,990	109,733
Net gain (losses) on financial assets at fair value through profit or loss .....	10,372	(48,299)	76,760	41,961	(5,270)
Other operating income .....	156,297	146,566	146,222	73,813	73,342
Operating expenses .....	(642,894)	(772,431)	(978,415)	(360,869)	(348,977)
	777,800	406,963	331,527	268,425	240,296
Impairment allowances on loans and advances .....	(82,922)	(91,334)	(102,289)	(54,131)	(19,736)
Net gain on disposal of prepaid lease payments for land.....	2,591	—	362	—	—
Net gain (loss) on disposal of property and equipment .....	(64)	294	(14)	(4)	82
Net gain on disposal of available-for-sale securities .....	177,351	108,706	24,810	20,133	—
Net gain on disposal of and on fair value adjustments on investment properties .....	28,811	39,560	31,148	1,374	6,630

	Years ended 31 December			Six months ended 30 June	
	2007	2008	2009	2009	2010
	<i>(HK\$ thousands, except for earnings per share)</i>			<i>(HK\$ thousands, except for earnings per share)</i>	
Impairment loss on available-for-sale securities .....	(369,627)	(264,654)	(43,571)	(44,292)	(1,818)
Impairment loss on goodwill .....	<u>(30,000)</u>	<u>(20,000)</u>	<u>(10,000)</u>	<u>(10,000)</u>	<u>—</u>
Profit from operations .....	503,940	179,535	231,973	181,505	225,454
Share of profit (loss) of jointly controlled entities .....	<u>66,074</u>	<u>(90,240)</u>	<u>32,410</u>	<u>7,257</u>	<u>2,883</u>
Profit before taxation .....	570,014	89,295	264,383	188,762	228,337
Taxation .....	<u>(64,982)</u>	<u>(28,675)</u>	<u>(32,635)</u>	<u>(28,133)</u>	<u>(34,945)</u>
Profit for the year/period .....	<u>505,032</u>	<u>60,620</u>	<u>231,748</u>	<u>160,629</u>	<u>193,392</u>
Earnings per share, basic and diluted .....	<u>HK\$1.16</u>	<u>HK\$0.14</u>	<u>HK\$0.53</u>	<u>HK\$0.37</u>	<u>HK\$0.44</u>

# **CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**

	As at 31 December			As at 30 June
	2007	2008	2009	2010
				(Unaudited)
	(HK\$ thousands)			
<b>ASSETS</b>				
Cash and short-term funds .....	14,763,977	17,659,927	15,048,680	12,515,314
Placements with banks and other financial institutions maturing between one and twelve months .....	3,084,147	5,367,858	2,814,566	3,707,638
Derivative financial instruments .....	60	429	331	6,108
Financial assets at fair value through profit or loss..	1,134,422	680,680	576,730	847,604
Available-for-sale securities .....	876,661	196,527	272,649	433,789
Held-to-maturity securities .....	15,607,980	9,727,685	16,954,466	15,934,387
Advances and other accounts .....	32,495,890	33,634,842	33,267,735	36,253,832
Tax recoverable.....	19,816	38,113	31,925	4,462
Interests in jointly controlled entities .....	142,230	82,999	119,418	120,747
Loan to a jointly controlled entity .....	5,267	—	—	—
Investment properties .....	60,241	129,801	103,199	105,970
Property and equipment (restated, except as at 30 June 2010) <sup>(1)</sup> .....	777,875	794,704	762,657	745,446
Prepaid lease payments for land (restated, except as at 30 June 2010) <sup>(1)</sup> .....	3,229	3,147	2,564	2,532
Goodwill .....	80,606	60,606	50,606	50,606
<b>Total assets</b> .....	<u>69,052,401</u>	<u>68,377,318</u>	<u>70,005,526</u>	<u>70,728,435</u>
<b>LIABILITIES</b>				
Deposits and balances of banks and other financial institutions .....	456,858	1,525,509	1,447,718	2,332,547
Deposits from customers .....	60,327,437	59,401,660	60,788,415	60,515,020
Other accounts and accruals .....	861,619	477,381	556,016	537,826
Derivative financial instruments .....	114,546	39,303	44,413	53,643
Current tax liabilities .....	35,008	5,104	15,671	17,151
Deferred tax liabilities .....	15,274	6,283	11,772	13,390
Loan capital .....	970,871	965,454	967,199	971,546
<b>Total liabilities</b> .....	<u>62,781,613</u>	<u>62,420,694</u>	<u>63,831,204</u>	<u>64,441,123</u>
<b>SHAREHOLDERS' EQUITY</b>				
Share capital .....	217,500	217,500	217,500	217,500
Reserves .....	6,053,288	5,739,124	5,956,822	6,069,812
Shareholders' funds .....	6,270,788	5,956,624	6,174,322	6,287,312
<b>Total liabilities and shareholders' equity</b> .....	69,052,401	68,377,318	70,005,526	70,728,435



## OTHER SELECTED FINANCIAL DATA

	As at/for the year ended 31 December			As at/for the six months ended 30 June <sup>(2)</sup>	
	2007	2008	2009	2009	2010
	(percentage)			(percentage)	
<b>Profitability Indicators</b>					
Return on total assets <sup>(3)</sup> .....	0.73	0.09	0.33	0.23	0.27
Return on average total assets <sup>(4)</sup> .....	0.75	0.09	0.35	0.49	0.59
Return on equity <sup>(5)</sup> .....	8.13	0.98	3.80	5.35	6.23
Net interest margin <sup>(6)</sup> .....	1.44	1.28	1.23	1.20	1.25
Net fee and commission income to operating income .....	19.95	18.38	20.13	18.59	18.62
Cost to income ratio <sup>(7)</sup> .....	45.25	65.49	74.69	57.35	59.22
<b>Capital Adequacy Ratio</b>					
Core capital adequacy <sup>(8)</sup> .....	11.52	12.55	12.72	12.85	12.11
Capital adequacy ratio (unadjusted) .....	14.22	15.64	15.95	16.05	15.24
Total equity to total assets.....	9.08	8.71	8.82	8.79	8.89
<b>Asset Quality Indicator</b>					
Impaired loans.....	0.68	0.30	0.16	0.18	0.12
Allowance on impaired loans.....	62.36	114.13	249.50	204.31	345.60
Allowance to total loans.....	0.42	0.35	0.41	0.37	0.42
<b>Other indicators</b>					
Loan to deposit ratio .....	48.15	51.52	49.57	50.73	53.81

Notes:

(1) Amendment to Hong Kong Accounting Standard (“HKAS”) 17 Leases

As part of Improvements to HKFRSs issued in 2009, HKAS 17 Leases has been amended in relation to the classification of leasehold land. Before the amendment to HKAS 17, lessees were required to classify leasehold land as operating leases and to present leasehold land as prepaid lease payments in the consolidated statement of financial position. The amendment has removed such a requirement. Instead, the amendment requires the classification of leasehold land to be based on the general principles set out in HKAS 17, that is, whether or not the risks and rewards incidental to ownership of a leased asset have been transferred substantially to the lessee.

In accordance with the transitional provisions set out in the amendment to HKAS 17 Leases, the Bank reassessed the classification of unexpired leasehold land based on information which existed at the inception of these leases. Leasehold land which met finance lease classification have been reclassified from prepaid lease payments for land to property and equipment retrospectively, resulting in a reclassification of prepaid lease payments for land with carrying amount of HK\$331,002,000, HK\$324,980,000 and HK\$318,969,000 as at 31 December 2007, 2008 and 2009, respectively, as property and equipment that are measured at cost model. The application of the amendment has had no significant financial impact to profit or loss for current or prior accounting periods.

The effect of changes in accounting policies described above on the financial position of the Bank as at 31 December 2007, 2008 and 2009 is as follows:

	<b>As at 31 December 2007</b>	<b>Adjustments</b>	<b>As at 31 December 2007</b>
	<i>(HK\$ thousands) (originally stated)</i>	<i>(HK\$ thousands)</i>	<i>(HK\$ thousands) (restated)</i>
Property and equipment.....	446,873	331,002	777,875
Prepaid lease payments for land .....	334,231	(331,002)	3,229

	<b>As at 31 December 2008</b>	<b>Adjustments</b>	<b>As at 31 December 2008</b>
	<i>(HK\$ thousands) (originally stated)</i>	<i>(HK\$ thousands)</i>	<i>(HK\$ thousands) (restated)</i>
Property and equipment.....	469,724	324,980	794,704
Prepaid lease payments for land .....	328,127	(324,980)	3,147

	<b>As at 31 December 2009</b>	<b>Adjustments</b>	<b>As at 31 December 2009</b>
	<i>(HK\$ thousands) (originally stated)</i>	<i>(HK\$ thousands)</i>	<i>(HK\$ thousands) (restated)</i>
Property and equipment.....	443,688	318,969	762,657
Prepaid lease payments for land .....	321,533	(318,969)	2,564

- (2) Figures as at/for the six months ended 30 June 2009 and 2010 are annualised.
- (3) Calculated as profit after taxation divided by total assets.
- (4) Calculated as profit after taxation divided by the average balance of total assets at each month end falling within the relevant year or period.
- (5) Calculated as profit after taxation divided by the average balance of the total equity at each month end falling within the relevant year or period.
- (6) Calculated as net interest income divided by average balance of total assets at each month end falling within the relevant year or period.
- (7) Calculated as the ratio of general and administrative expenses to the sum of net interest income and net non-interest income (excluding general and administrative expenses.)
- (8) “Core capital adequacy” means the ratio of core capital (Tier 1) to risk-weighted assets. For details, see “*Regulation and Supervision — Principal Obligations of License Banks — Capital Adequacy*”.

## INVESTMENT CONSIDERATIONS

*Prospective investors should carefully take into account the investment considerations described below, in addition to the other information contained herein, before investing in the Notes. The occurrence of one or more events described below could have an adverse effect on the Bank's business, financial condition, or results of operations, and could affect its ability to make payments of principal and interest under the Notes. Additional considerations and uncertainties not presently known to the Bank, or which the Bank currently deems immaterial, may also have an adverse effect on an investment in the Notes.*

### Considerations Relating to the Bank

#### **Competition**

The Bank is subject to significant competition from many other banks and financial institutions, including competitors which have significantly greater financial and other capital resources, greater market share, and greater name recognition than the Bank. In particular, the banking and financial services industry in Hong Kong is a mature market and, as at 31 December 2009, supported 23 Hong Kong incorporated licensed banks and 122 banks incorporated outside Hong Kong competing for a customer population of approximately 7 million people. Therefore, many of the international and local banks and niche players operating in Hong Kong compete for substantially the same customers as the Bank. There is a limited market, especially for retail banking products such as investment and insurance products, home mortgage loans, credit cards, personal loans and transport lending businesses. The strength of competition in the past few years has had an adverse impact on the Bank's pricing of certain products.

In recent years, competition among banks in Hong Kong for investment and insurance products, home mortgage loans, credit cards, personal loans and transport lending business has become very aggressive. There can be no assurance that increased competition will not have a material adverse effect on the Bank's business, financial condition or results of operations.

Since 2000, many banks in Hong Kong, including the Bank, have lowered interest rates charged on new-home mortgage loans not guaranteed by the Hong Kong government. Despite a slight increase in such interest rates in 2008, competition in the mortgage loans market remains intense. In 2009, with interest rates at an extremely low level, a significant portion of new-home mortgage loan rates charged by banks in Hong Kong was HIBOR based. As at 30 June 2010, the standard rate the Bank charged on its new-home mortgage loans was 3% below the prime lending rate or 70 basis points above HIBOR. Competition among banks in Hong Kong for home mortgage loans could result in further reductions in home mortgage interest rates. Such reductions could have an adverse effect on the Bank's business, financial condition or results of operations.

Following the PRC's accession to the World Trade Organisation ("**WTO**"), a number of foreign banks have received authorisation from the PRC government to, from five years after accession, provide RMB-denominated banking and financial services ("**RMB services**") to PRC domestic enterprises and individuals. The Closer Economic Partnership Agreement with the PRC ("**CEPA**"), which allows Hong Kong banks to operate in the PRC, has also increased competition in the Mainland China market. Since April 2007, the PRC government has begun granting approvals for locally incorporated banking licences for a number of foreign banks which allow them to compete with PRC domestic banks on equal footing, thereby effectively removing regulatory restrictions on the geographical presence, customer base and operating licences of foreign banks. Accordingly, the Bank is likely to face competition in the Mainland China market from both existing local Chinese banks and foreign banks entering the Mainland China market. There can be no assurance that the Bank will maintain its current position or continue to develop its business successfully in Mainland China if, as expected, competition in the banking sector in Mainland China intensifies as a result of these latest changes in the regulatory environment in the PRC.

The introduction of CEPA has also enabled Mainland China banks to relocate certain operations, for example, the handling of international securities and bonds, as well as foreign exchange trading centres, to Hong Kong. Under CEPA, Mainland China banks are encouraged to expand their business through merger and acquisition (“M&A”) activities. The entry of Mainland China banks into the Hong Kong market via M&A activities is likely to result in increased competition in the banking sector and there can be no assurance that the Bank’s business will not be affected by such increased competition.

### ***Expansion of the Bank’s Business in Hong Kong and Mainland China***

The Bank intends to continue its focus on growing its business operations in Hong Kong. In particular, due to the maturity of the Hong Kong banking sector, increasing competition and downward market pressure on profit margins, the Bank intends to expand its range of products and services to diversify its business portfolio in order to maintain its competitive edge. Specifically, the Bank intends to target the younger age demographic in its development of new products and services. The Bank also intends to expand its operations in Mainland China by expanding the range of products and services offered by its branch in Shantou and by establishing more branches in China. Expansion of the Bank’s business activities exposes the Bank to certain risks and challenges, including the following:

- the Bank may not have sufficient experience or expertise in certain new products and services and may not be able to compete effectively in these areas;
- the Bank’s new products and services may not be well-received by its customers or meet the Bank’s expectations for profitability;
- the Bank may need to hire additional qualified personnel which may not be available;
- the Bank may fail to obtain regulatory approval for its new products or services where necessary; and
- the Bank may not be successful in enhancing its risk management capabilities and information technology systems to support a broader range of products and services.

If the Bank is not able to achieve the intended results with respect to the expansion of its business activities, the Bank’s business, financial condition and results of operations may be adversely affected.

### ***Advance Concentration: Exposure to the Hong Kong Property Market***

The Bank has a significant exposure to the Hong Kong property market due to its portfolio of home mortgage advances. As at 30 June 2010, home mortgage advances (excluding Government Home Ownership Scheme mortgages), and advances for property development and investment in Hong Kong accounted for 17.1% and 26.8%, respectively, of the Bank’s total advances to customers. The Hong Kong property market is highly cyclical and property prices in general have been volatile. During the period from 1997 to the first half of 2003, property prices and transaction volumes in the Hong Kong property market experienced significant declines although both have risen significantly since the end of 2003. In addition, while the Hong Kong property market showed improvement during the period from 2004 to the first half of 2008, property prices in Hong Kong declined in the second half of 2008 and early 2009, before increasing significantly since the second half of 2009. Property prices are further affected by a number of factors, including, among other things, the supply of, and demand for, comparable properties, the rate of economic growth in Hong Kong, political and economic developments in the PRC and the relationship between the PRC, Hong Kong and other countries. The Bank’s relatively high loan-to-value ratio with respect to home mortgage advances, the 60% collateralisation of its loan portfolio and its emphasis on tangible securities cover may partially offset

any future decreases in property values in the Hong Kong property market. However these measures provide no assurance that the Bank's business, financial condition or results of operations will not be adversely affected by such developments. Any such future decreases could adversely affect the Bank's business, financial condition or results of operations.

In addition, the property market in Mainland China is subject to policies implemented by the PRC government from time to time. In recent years, the PRC government has introduced measures designed to discourage excessive growth of PRC's high-end residential property sector and encourage the development of mass market residential property projects with a higher degree of affordability. These policies and measures may have a material impact on property prices in the PRC which could adversely affect the Bank's business, financial condition and results of operation.

### ***Quality of the Bank's Credit Portfolio***

Any lending activity is exposed to credit risk arising from the risk of default by borrowers. The sustainability of the Bank's growth depends largely on its ability to effectively manage its credit risk and maintain the quality of its loan portfolio. A number of factors will affect the Bank's ability to control and reduce impaired and restructured loans. Some of these, including developments in the Hong Kong economy, movements in the global economy, global competition, interest rates and exchange rates are not within the Bank's control.

Although the Bank has in place credit risk management policies, procedures and systems and the Bank is constantly focusing its efforts on tightening its credit appraisal systems, credit risk monitoring and management systems and improving collections on existing impaired assets, there can be no assurance that such growth will continue, that the Bank will continue to be successful in its efforts to reduce its level of impaired assets, that the overall quality of its loan portfolio will not deteriorate in the future or that the business of the Bank's borrowers will grow in line with the economy. If the Bank is not able to control and reduce its impaired loans, or if there is a further significant increase in its restructured loans, the Bank's business, future financial performance and the price of the Notes could be adversely affected.

The Bank's gross impaired loans on a consolidated basis as at 30 June 2010 were HK\$44 million (US\$5.7 million), which represented 0.12% of the Bank's gross advances to customers and against which provisions totalling HK\$34 million (US\$4.3 million) have been made on the unsecured portion of these loans. Whilst the Bank continues to pursue recovery of these impaired loans, there is no assurance that the Bank will ultimately recover any amount of the impaired loans.

There is also no assurance that there will be no deterioration in provisions for loan losses as a percentage of impaired loans or otherwise, that the percentage of impaired loans that the Bank will be able to recover will be similar to the Bank's past experience of recoveries of impaired loans or that upon enforcement, the value of any collateral or guarantee securing the Bank's advances will be sufficient. In the event of any deterioration in the Bank's asset portfolio, there could be an adverse impact on the Bank's business, future financial performance, shareholders' funds and the price of the Notes.

In addition, the Bank may decide to restructure certain of its impaired loans. In such restructuring, the Bank usually agrees to set payments of principal and/or interest at a relatively low level for a certain time frame followed by larger payments in later periods to match the Bank's expectation of the borrowers' ability to service the debt. The relatively low payments improve the likelihood that a restructured loan will be categorised as performing during the period of such payments. However, future higher payments may cause the loan to again become impaired if the borrower is unable to make such larger payments in the later periods. If a significant number of the Bank's customers are unable to make larger payments for their respective restructured loans, such restructured loans may become impaired, thereby requiring additional provisions and could have a material adverse effect on the Bank's ability to make payments under the Notes.

### ***Recent market conditions and the risk of continued market deterioration***

The U.S. credit markets and the sub-prime residential mortgage market have recently experienced substantial dislocations, liquidity disruptions and market corrections. In particular, sub-prime mortgage loans have experienced increased rates of delinquency, foreclosure and loss. These and other related events have had a significant impact on the global credit and financial markets as a whole.

The Bank has not invested directly in any assets or securities linked to, or the value of which is derived from, assets that could be classified as sub-prime residential mortgages. As such, the Bank currently does not have direct exposure to the sub-prime residential lending market. However, as at 30 June 2010, less than 0.1% of the Bank's investment securities comprised structured investment vehicles which hold and invest in assets that are classified as sub-prime residential mortgages. As such, the Bank has indirect exposure to the sub-prime residential lending market. To date, the Bank is not aware of any significant deterioration in the performance of or any significant revaluation of such investments. However, the values of many of the investment securities that the Bank holds are sensitive to the volatility of the credit markets and accordingly, such investment securities may be adversely affected by future developments in the credit markets. To the extent that turmoil in the credit market continues and/or intensifies, it may have the potential to materially affect the value of the Bank's investment portfolio. In the event that the Bank is forced to liquidate all or part of its investment portfolio in the current market, the Bank could experience significant losses on these investments. However, the Bank's current intention is to hold such investment securities to maturity, although from time to time, the Bank may sell any of these assets as part of our overall management of the investment portfolio.

In addition, to the extent that any of the Bank's borrowers have been adversely affected by the recent deterioration of conditions in the sub-prime residential mortgage market, the ability of such borrowers to service their debt obligations to the Bank may also be affected. If the loans to these borrowers were to become impaired, this could adversely affect the Bank's business and results of operations.

The recent market volatility has also made the valuation of certain of the Bank's securities assets more difficult as the Bank's estimates of the value of these investments incorporates a combination of independent pricing agency and third-party dealer valuations as well as comparable sales transactions. The fair values of such investments as reflected in the Bank's results of operations may not reflect the prices that can be obtained by the Bank if such investments were actually sold due to uncertainty in the credit markets in the valuation of, or in the stability of the value of, certain investment assets.

Furthermore, due to the recent market events, the Bank's investments may be subject to rapid changes in value caused by sudden developments which could have a material adverse affect on the value of these investments.

### ***Classification of Advances: Adequacy of Allowance for Advance Losses***

In accordance with guidelines set by the HKMA, the Bank divides its classified advances into one of the following three categories corresponding to levels of risk: "Sub-standard", "Doubtful" and "Loss". See "*Selected Statistical and Other Information*". The classification of advances into one of these categories depends on various quantitative and qualitative factors, including the number of months payment is in arrears, the type of advance, the tenor of the advance and the level of collateral coverage. In accordance with HKAS 39, advances are designated as "impaired" where there is objective evidence of impairment as a result of one or more of the loss events that will impact the estimated future cash flows of the loans. Interest will continue to accrue on impaired advances based on the original terms of the loans but will be discounted to arrive at the net present value of the impaired loans.



The laws, regulations and guidelines governing the banking industry in Hong Kong differ from those applicable in various other countries in certain respects and may result in particular advances being classified at a different time or being classified in a category reflecting a different degree of risk than would be required in other countries. While the Bank believes that its credit policies are more prudent than those that are required under Hong Kong laws and regulations, the Bank is not required to maintain such policies at levels above those generally applicable to banks in Hong Kong. For a description of the banking regulations that apply to banks in Hong Kong, see “*Regulation and Supervision*”.

### ***Liquidity; Short-Term Funding***

Most of the Bank’s funding requirements are met through short-term funding sources, primarily in the form of customer deposits, including savings, current, short-term and structured term deposits and, to a much smaller extent, interbank deposits. As at 30 June 2010, substantially all of the Bank’s total customer deposits had remaining maturities of one year or less or were payable on demand. Accordingly, the maturity profile of the Bank’s assets and liabilities shows a negative gap in the short term. The negative gap has arisen mainly because the Bank’s deposits, which are met through short-term funding sources (primarily in the form of deposits) and other liabilities, are of shorter average maturity than its loans and investments, which have medium- or long-term maturities, thereby creating a potential for funding mismatches. Historically, savings, current and a substantial portion of term deposits which used to roll over upon maturity have been a stable source of long-term funding. However, no assurance can be given that this pattern will continue. If a substantial number of depositors fail to roll over deposited funds upon maturity, the Bank’s liquidity position would be adversely affected and the Bank may need to seek alternative sources of short-term or long-term funding to finance its operations, which may be more expensive than existing deposits.

The HKMA acts as a lender of last resort to all authorised institutions in Hong Kong to provide support for liquidity needs in the banking system generally as well as to specific institutions. Although the Hong Kong Government has in the past taken measures on a case-by-case basis to maintain or restore public confidence in individual banks with an isolated liquidity crisis, there can be no assurance that the HKMA will provide such assistance in the future or that it would elect to provide such assistance in the event of a liquidity crisis in respect of the Bank.

### ***Currency Risks***

The majority of the Bank’s revenues are generated in Hong Kong dollars. Although the Hong Kong dollar has been linked to the U.S. dollar since 1983, there can be no assurance that such linkage will be maintained in the future. In order to ensure continued liquidity of the Hong Kong dollar, the HKMA has entered into bilateral repurchase agreements with the central banks or monetary authorities of Australia, the PRC, Indonesia, Japan, Korea, Malaysia, New Zealand, the Philippines, Singapore and Thailand. In addition, the Hong Kong Government has in the past expressed its commitment to maintaining exchange rate stability under the Linked Exchange Rate System, an automatic interest rate adjustment mechanism. However, there can be no assurance that the Hong Kong dollar will continue to be linked to the U.S. dollar or that, in the event of a liquidity problem affecting the Hong Kong dollar, such bilateral repurchase agreements or the automatic interest rate adjustment mechanism will help to maintain adequate liquidity for the Hong Kong dollar. The Bank’s business, financial condition and results of operations could be adversely affected by the impact on the Hong Kong economy of the discontinuation of the link of the Hong Kong dollar to the U.S. dollar or any revaluation of the Hong Kong dollar or Renminbi.



### ***Interest rate risk***

As with other banks, net interest income is a significant factor in determining the Bank's overall financial performance. For the years ended 31 December 2007, 2008 and 2009 and the six months ended 30 June 2010, net interest income represented approximately 68.3%, 73.3%, 62.9% and 69.8%, respectively, of the Bank's operating income. Changes in market interest rates affect the interest received on the Bank's interest-earning assets and the interest paid on the Bank's interest-bearing liabilities. The differences in timing and levels of changes in interest rates can result in an increase in interest expense relative to its interest income, which may lead to a reduction in the Bank's net interest income. Interest rates in Hong Kong are sensitive to factors over which the Bank has no control, including, among others:

- interest rates in the United States;
- liquidity of the domestic inter-bank market and the international capital markets;
- domestic and international economic and political conditions; and
- competition for loan demand.

In the event that interest rates move against the Bank's position, it may adversely affect the Bank's business, financial condition or results of operations. The bankruptcy of Lehman Brothers in September 2008 and its aftermath impacted the global economy. In spite of global concerted efforts in the implementation of fiscal and monetary stimulating policies to revive economic growth and the financial markets, the interest rate environment in 2009 and the first half of 2010 remained low and, as a result, the Bank's net interest margin also remained at a low level. For the six months ended 30 June 2010, the Bank's net interest margin was 1.25%.

An increase in interest rates could lead to a decline in the value of securities in the Bank's portfolio even though most of such decline in value would not affect the Bank's operating income because most of the securities are in the held-to-maturity portfolio. A sustained increase in interest rates could also raise the Bank's funding costs without a proportionate increase in loan demand (if at all). Rising interest rates would therefore require the Bank to re-balance its assets and liabilities in order to minimise the risk of potential mismatches and maintain its profitability. In addition, rising interest rate levels may adversely affect the economy in Hong Kong or Mainland China and the financial condition and repayment ability of its corporate and retail borrowers, including holders of credit cards, which in turn may lead to a deterioration in the Bank's credit portfolio.

### ***Exposure to the PRC and Macau market***

As at the date of this Offering Circular, the Bank has three overseas branches located in Shantou, Macau and San Francisco, and two representative offices located in Guangzhou and Shanghai. As at 30 June 2010, the Bank's loan portfolio in Mainland China and Macau amounted to approximately HK\$347 million (U.S.\$45 million) and HK\$158 million (U.S.\$20 million), which accounted for 1.0% and 0.4% of the Bank's overall loan portfolio, respectively. Currently, the Bank's exposure to the PRC and Macau markets is limited. However, the Bank has targeted Mainland China and Macau as potential markets for future development and may decide to expand its business or branch network in Mainland China and Macau in the future. In addition, the Bank's banking activities in Mainland China and Macau are conducted mainly with its existing customers based in Hong Kong who are engaged in business in Mainland China and Macau and the Bank may increase such banking activities to cater to the needs of its customers as they increase the size and scope of their business operations in Mainland China or, as the case may be, Macau. There is no assurance that the Bank's exposure to the PRC and Macau markets, including the general economic and business conditions, the banking industry, the political and social environment and the legal system of Mainland China and Macau, will not increase in the future.

## ***Different Corporate Disclosure, Accounting and Regulatory Requirements***

The Bank's issued shares are listed on the HKSE and, as such, the Bank is required to publish annual audited and semi-annual unaudited financial information. The amount of information publicly available for issuers in Hong Kong is less than that publicly available for comparable banks in certain other countries. In addition, the Bank prepares its financial statements in accordance with HKFRSs, which are in all material aspects fully converged with IFRS effective for accounting periods beginning on or after 1 January 2008. Thus, the accounting presentation of historical reported earnings of the Bank for accounting periods before 1 January 2008 may differ from those of companies in certain other countries. Certain changes in HKFRSs, which became effective on or from 1 January 2010, have since been adopted by the Bank. This Offering Circular does not include a reconciliation of the Bank's historical financial statements to IFRS and, as applicable, HKFRSs, and there can be no assurance that any such reconciliation would not identify material qualitative or quantitative differences.

Under the Hong Kong Banking Ordinance, the HKMA regulates the business activities and operations of commercial banks and has the ability to influence banking and financial markets generally. Potential investors should be aware that regulatory requirements in Hong Kong may differ from that which prevails in other countries. See "*Regulation and Supervision*". Since the Bank operates in the highly regulated banking and securities industries in Hong Kong, potential investors should also be aware that the regulatory authorities have been consistently imposing higher standards and developing new guidelines and regulatory requirements. In December 2009, the Basel Committee on Banking Supervision issued a consultative document with proposals to reform the capital adequacy standards of the banking sector. There is no certainty as to the final framework for capital and adequacy standards which will be developed and implemented, which may require increased capital requirements and impact existing business models, or the timing of the implementation. If such final recommended measures are adopted by the HKMA, the Bank may incur substantial costs in monitoring and complying with the new requirements.

## ***Change in Accounting Standards***

The Bank's financial statements included elsewhere in this Offering Circular have been prepared in accordance with all applicable Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants ("**HKICPA**") and accounting principles generally accepted in Hong Kong. The HKICPA has issued a number of new and revised HKFRSs, which are effective for accounting periods beginning on or after 1 January 2009. The effect of the changes brought about by the new HKFRSs are disclosed in Note 2 to the unaudited interim financial statements of the Bank as of and for the six months ended 30 June 2010.

## ***Internet Banking Services***

The Bank relies on its internet banking services as a means of providing customers with greater access to its products and services. Usage of the Bank's internet banking services may be adversely affected for a number of reasons, such as unavailability of high-speed access to the internet. To the extent that the Bank's internet banking activities involve the storage and transmission of confidential information, security breaches could expose the Bank to possible liability and damage the Bank's reputation. The Bank's networks may be vulnerable to unauthorised access, computer viruses and other disruptive problems. Costs incurred in rectifying any of such disruptive problems may be high and may adversely affect the Bank's financial condition and results of operations. Concerns regarding security risks may deter the Bank's existing and potential customers from using its internet banking products and services. Eliminating computer viruses and alleviating other security problems may result in interruptions, delays or termination of service to users accessing the Bank's internet banking services. Undetected defects in software products that the Bank uses in its products and the Bank's inability to sustain a high volume of traffic may materially and adversely affect the Bank's internet banking business.

### ***Dependence on Key Personnel***

The Bank's business and operations are substantially dependent upon key members of its management. Although the Bank has succeeded in maintaining the core of its senior management team over the recent past, the loss of the services of members of the Bank's senior management could have an adverse effect on the Bank's financial condition and results of operations.

### ***The Ability of Shareholders and Related Parties to Exercise Influence over Certain of the Bank's Affairs***

As at 30 June 2010, Liu Chong Hing Estate Company, Limited was the Bank's largest shareholder, holding a 48.52% shareholding interest. In addition, pursuant to an agreement dated 20 May 1994, The Bank of Tokyo-Mitsubishi UFJ, Ltd has granted an option to Liu Chong Hing Estate Company, Limited, which is exercisable at any time during the term of that agreement to purchase 40 million shares of the Bank from The Bank of Tokyo-Mitsubishi UFJ, Ltd in certain circumstances. Liu Chong Hing Estate Company, Limited is a wholly-owned subsidiary of Liu Chong Hing Investment Limited, a public company listed on the HKSE which is, in turn, approximately 45% owned by Liu's Holdings Limited. Liu's Holdings Limited is wholly-owned by members of the Liu family, including Messrs. Liu Lit Mo and Liu Lit Chi who are Directors of the Bank. Four out of the seven Executive Directors, together with two out of the seven Non-executive Directors, on the Bank's Board of Directors, also comprise members of the Liu family and four of these individuals also hold shareholding interests in the Bank. See "*Principal Shareholders and Directors' Interests*". Members of the Liu family also serve on the board of directors of Liu Chong Hing Investment Limited. Accordingly, the Liu family has the ability to exert significant influence over the Bank's affairs subject to the Listing Rules and the Laws of Hong Kong.

The Bank has, from time to time, entered into a number of transactions with members of the Liu family or companies controlled or significantly influenced by them. The transactions include, among others, lending, deposit-taking, loan syndications, provision of cheque clearing services, stockbroking and nominee services, remittances and foreign exchange services, acceptance of property consultancy and property management services, and leasing of office premises. The Bank conducts all transactions with its related parties, including but not limited to members of the Liu family, on an arm's length basis and believes that such transactions were as beneficial, and on terms as favourable to it, as similar transactions with unrelated third parties would have been. In addition, the Bank has four directors who are independent non-executive directors in accordance with the criteria set out in the Listing Rules and maintains internal policies and procedures to prevent possible conflicts of interest. However, the interests of the Liu family may differ significantly from the interests of the Bank and the Bank's other shareholders and creditors, including the holders of the Notes, and there can be no assurances that the Liu family will exercise influence over the Bank in a manner that is in the best interests of the Bank and the Bank's other shareholders and creditors.

### ***Further Issuance of Securities***

To ensure that it remains in compliance with applicable capital requirements under Hong Kong law, rules and regulations (including guidelines issued by the HKMA), the Bank may from time to time raise additional capital through such means and in such manner as it may consider appropriate including, without limitation, the issue of further subordinated notes (whether on terms similar to the Notes or otherwise) or other hybrid capital instruments, subject to any regulatory approval that may be required. There can be no assurance that such future capital raising activities will not adversely affect the market price of the Notes in the secondary market.

## Considerations Relating to Hong Kong, Mainland China and Elsewhere

### *Hong Kong Economy*

On 1 July 1997, Hong Kong ceased to be a Crown Colony of the United Kingdom and became a Special Administrative Region of the PRC. Although Hong Kong has thus far enjoyed a high degree of legislative, judicial and economic autonomy since the handover, there can be no assurance that there will not be a change in regulatory oversight as a consequence of the exercise of PRC sovereignty over Hong Kong or that, should such change occur, that the Bank's business, financial condition and results of operations will not be adversely affected.

Most of the Bank's revenues are derived from its operations conducted in Hong Kong. As a result, the Bank's financial condition and results of operations are influenced by the general state of the Hong Kong economy (including the level of unemployment) and the political environment in Hong Kong. The economic and political environment in Hong Kong is, in turn, significantly affected by a variety of external factors, including the economic and political environment in the PRC and throughout Asia and the rest of the world.

In 1997, the Asian financial crisis and the subsequent economic downturn in Hong Kong and the Severe Acute Respiratory Syndrome ("SARS") epidemic in 2003 necessitated among other things, increased provisions which negatively affected the Bank's profitability. Although the Hong Kong economy has, to a large extent, recovered from the impact of the Asian financial crisis and SARS in subsequent years, the global credit markets have experienced, and may continue to experience, significant dislocation and turbulence which originated from the liquidity disruptions in the United States credit and sub-prime residential mortgage markets in the second half of 2007. Sub-prime mortgage loans in the United States have experienced increased rates of delinquency, foreclosure and loss. These and other related events, such as the collapse of a number of financial institutions, have resulted in an economic slowdown in the United States and most economies around the world, substantial volatility in equity securities markets globally, fluctuations in foreign currency exchange rates and volatility and tightening of liquidity in global credit markets. Although there has been evidence of economic recovery mounting since the second half of 2009, recent economic downturns and sovereign debt concerns in certain European countries have led to renewed doubts regarding the sustainability of the global economic recovery. If there is any renewed economic downturn or slowdown in global economic recovery, there can be no assurance that the Hong Kong economy or the Bank's business, financial condition and results of operations will not be adversely affected.

The Bank expects the recovery of, and the continued growth in, the Hong Kong economy to depend in part upon the economic performance of the United States and the PRC, as well as certain other developed countries. There can be no assurance that future global events will not have an adverse effect on the Hong Kong economy and the Bank.

### *Mainland China Economy*

Many of the Bank's commercial customers are dependent on varying degrees on trade with Mainland China. The value of the Bank's advances in Mainland China, as well as its advances to companies that have business interests in Mainland China, may be influenced by the general state of the PRC economy and may be affected by significant political, social or legal uncertainties or changes in Mainland China (including changes in political leadership, the rate of inflation, exchange controls and the exchange rate and the impact on the economy of the PRC's accession to the WTO). There can be no assurance that the economic and political environment in Mainland China will remain favourable to the Bank's business in Mainland China in the future irrespective of the likelihood of whether the PRC Government would reverse its open-door economic policy which has been adopted for more than two decades and which contributed to the country's economic well being over the years.

In November 2008, in response to the deepening of the global economic crisis, the PRC government announced a RMB4 trillion (US\$583 billion) stimulus plan in a bid to reduce the adverse

impact of the global economic crisis on the PRC and to increase spending and employment in the subsequent two years. Such liquidity injections in the last quarter of 2008 contributed to a significant increase in bank lending in 2009. However, due to the PRC government's growing concerns that rapidly rising bank lending could fuel asset bubbles and increase the risk of inflation, in January, February and May 2010, the People's Bank of China raised the Renminbi deposit reserve requirement ratio for banks by 50 basis points for each of the three months. If the PRC's economy experiences a slowdown in growth or a downturn in the future, or the PRC government continues to tighten its monetary policies, the Bank's PRC business and its ability to implement its growth strategies in the PRC could be materially and adversely affected.

With the increased integration of the PRC and Hong Kong economies, PRC policies will have an impact on Hong Kong and Hong Kong companies conducting business in the PRC. The Bank and its customers may also be affected accordingly.

### ***Recurrence of SARS, Avian Influenza or Other Highly Contagious Diseases in Asia and Elsewhere***

During the first half of 2003, the outbreak of SARS caused an adverse effect on the economies of the affected regions in Asia, including Hong Kong and the PRC, which affected the Bank's operations in these affected regions. In the last few years, there have also been outbreaks of avian influenza in parts of Asia, including Hong Kong. In 2009, there were outbreaks among humans of the Human Swine Influenza A ("H1N1") virus globally. On 11 June 2009, the World Health Organization ("WHO") raised its pandemic alert level to Phase 6, its highest level, after considering data confirming the H1N1 outbreak. To date, there has been a significant number of confirmed cases of H1N1 in the Asia Pacific region and a number of deaths worldwide.

No assurance can be given that there will not be a recurrence of the outbreak of SARS or other epidemics, or that incidents of avian influenza or H1N1 will not increase. As such, there can be no assurance that the Bank's business, financial condition and results of operations would not be adversely affected if another outbreak of SARS, H1N1 virus or another highly contagious disease occurs.

### **Considerations Relating to the Notes**

#### ***Subordination of the Notes***

Prior to the date on which a Change in Status Notice becomes effective pursuant to Condition 3(4) of the Notes, the Notes will constitute direct, unsecured and subordinated obligations of the Bank, ranking *pari passu* without any preference among themselves. In the event of a winding-up of the Bank, the claims of the holders of the Notes will be subordinated in right of payment to the claims of all unsubordinated creditors of the Bank and will rank *pari passu* in right of payment with all other subordinated indebtedness present and future of the Bank, except that claims in respect of the Notes will rank in priority to the rights and claims of holders of subordinated liabilities which by their terms rank in right of payment junior to the Notes and all classes of equity securities of the Bank, including holders of preference shares, if any. See "*Terms and Conditions of the Notes — Status*".

As a consequence of these subordination provisions, in the event of a liquidation, winding-up or other similar proceeding of the Bank, the holders of the Notes may recover less rateably than the holders of deposit liabilities and/or the holders of other unsubordinated liabilities of the Bank. The rights of the holders of the Notes will also be effectively subordinated to the rights of holders of all liabilities, including deposit liabilities, of the Bank's subsidiaries. The Notes and the Trust Deed do not limit the amount of the liabilities ranking senior to the Notes that may be hereafter incurred or assumed by the Bank.



It is intended that the Notes should constitute Category II Supplementary Capital of the Bank and, accordingly, under statutory requirements prevailing at the date of this Offering Circular relating to Category II Supplementary Capital, and by virtue of the above provisions, any redemption of such Notes prior to the stated maturity is subject to the prior approval of the HKMA at the relevant time.

### ***The rate of interest on the Notes***

The Basel Committee on Banking Supervision (the “BCBS”) is in a process of consultation on a package of proposals to strengthen global capital and liquidity regulations with the goal of promoting a more resilient banking sector. The BCBS’ programme may lead to changes in the requirements for bank capital and certain term subordinated debt may not qualify as regulatory capital beyond a certain time frame. Such changes may be correspondingly adopted by the HKMA and in particular, the HKMA may decide that the Notes do not qualify as term subordinated debt for inclusion in Category II — Supplementary Capital of the Issuer. If the Notes do not qualify as Category II — Supplementary Capital of the Issuer, the Issuer may, on or after 1 January 2013, at its option, and subject to the prior approval of the HKMA, provide a Change in Status Notice (as defined in Condition 3(4) of the Notes) in accordance with Condition 3(4) of the Notes, which will become effective on the Interest Payment Date specified therein. Upon a Change in Status Notice becoming effective, the Notes shall thereafter constitute unsubordinated obligations of the Issuer pursuant to Condition 3(4) of the Notes and the rate of interest on the Notes shall be reduced from 6.000% per annum to 5.500% per annum.

### ***Certain Considerations Relating to Enforcement***

To the extent that the Trustee or the holders of the Notes are entitled to any recovery with respect to the Notes in any Hong Kong proceedings, the Trustee and such holders of the Notes might not be entitled in such proceedings to a recovery in U.S. dollars and might be entitled only to a recovery in Hong Kong dollars.

In Hong Kong proceedings, if the Bank’s assets become subject to the control of a court-appointed receiver, interest on the Notes would cease to accrue on the date of the court order and the relevant U.S. dollar amounts would be converted to Hong Kong dollars as at such date for purpose of claims.

### ***Credit Ratings of the Notes***

The Notes are expected to be rated “Baa3” by Moody’s and “BBB” by Fitch. These ratings reflect the Bank’s ability to make timely payments of principal and interest on the Notes. A rating is not a recommendation to buy, sell or hold any security, does not address the likelihood or timing of payment of the Notes and may be subject to revision, suspension or withdrawal at any time by the assigning rating organisation. There is no assurance that the ratings assigned to the Notes will remain in effect for any given period or that the ratings will not be revised by the assigning rating organisation in the future if, in its judgment, circumstances so warrant. A downgrade in ratings may affect the secondary market price of the Notes.

### ***Liquidity of the Notes***

There can be no assurance as to the liquidity of the Notes or that an active trading market will develop. If such a market were to develop, the Notes could trade at prices that may be higher or lower than the initial issue price depending on many factors, including prevailing interest rates, the Bank’s operations and the market for similar securities. The Joint Lead Managers are not obliged to make a market for the Notes and any such market-making, if commenced, may be discontinued at any time at the sole discretion of the Joint Lead Managers, acting together. No assurance can be given as to the liquidity of, or trading market for, the Notes upon their listing on the HKSE. Lack of a liquid, active trading market for the Notes may adversely affect the price of the Notes or may otherwise impede a holder’s ability to dispose of the Notes.

***The Trustee may decline to take actions requested by the Noteholders***

In certain circumstances (including the giving of notice to the Issuer pursuant to Condition 10 (Events of Default)), the Trustee may (at its sole discretion) request the Noteholders to provide an indemnity and/or security to its satisfaction before it takes actions on behalf of the Noteholders and shall not be obliged to take any such actions until it is indemnified and/or secured to its satisfaction.

The Trustee may decline to take action requested by the Noteholders, notwithstanding the provision of an indemnity or security to it, where it is not satisfied that the action is permitted by applicable law.



## **USE OF PROCEEDS**

The Notes are intended to qualify as “Category II Supplementary Capital” of the Bank for purposes of capital adequacy under Part XVII of the Hong Kong Banking Ordinance. The issuance of the Notes will strengthen the Bank’s capital base and fund the growth of the Bank’s operations and are freely available to absorb the losses of the Bank, if any, in accordance with the requirements of the Hong Kong Banking (Capital) Rules (Cap. 155L). The net proceeds from the issue of the Notes will be approximately U.S.\$223,341,750, after deducting the commissions and expenses incurred in connection with the issue of the Notes.

## CAPITALISATION AND INDEBTEDNESS

### Capitalisation and Indebtedness of the Bank

As at the date of this Offering Circular, the Bank has an authorised share capital of HK\$300,000,000 consisting of 600,000,000 ordinary shares of HK\$0.50 each, and issued and fully paid up share capital of HK\$217,500,000 consisting of 435,000,000 ordinary shares of HK\$0.50 each.

The following table sets forth the Bank's unaudited consolidated capitalisation and indebtedness as at 30 June 2010 and as adjusted for the issue of the Notes.

	As at 30 June 2010	
	Actual	As adjusted
	(HK\$ thousands)	
<b>Short-term borrowings</b>		
Deposits from customers .....	60,503,732	60,503,732
Cash and balances with banks and other financial institutions .....	2,332,547	2,332,547
<b>Total short-term borrowings .....</b>	<b>62,836,279</b>	<b>62,836,279</b>
<b>Medium-term borrowings</b>		
Deposits from customers .....	11,288	11,288
Cash and balances with banks and other financial institutions .....	—	—
<b>Total medium-term borrowings .....</b>	<b>11,288</b>	<b>11,288</b>
<b>Long-term borrowings</b>		
Deposits from customers .....	—	—
Cash and balances with banks and other financial institutions .....	—	—
Loan capital .....	971,546	971,546
Notes to be issued .....	—	1,744,875
<b>Total long-term borrowings .....</b>	<b>971,546</b>	<b>2,716,421</b>
<b>Capital resources</b>		
Share capital .....	217,500	217,500
Reserves .....	6,069,812	6,069,812
<b>Total capital resources .....</b>	<b>6,287,312</b>	<b>6,287,312</b>
<b>Total capitalisation .....</b>	<b>70,106,425</b>	<b>71,851,300</b>

The Bank may repurchase a portion of its lower tier 2 debt on the open market.

There has been no material change in the Bank's total consolidated capitalisation or indebtedness since 30 June 2010.

## BUSINESS OF THE BANK

### Introduction

The Bank is a full service bank which operates primarily in Hong Kong. As at the date of this Offering Circular, the Bank had an established network comprising a head office and a total of 54 branches, including 51 branches in Hong Kong, 3 overseas branches located in Shantou, Macau and San Francisco, and 2 representative offices located in Guangzhou and Shanghai.

The Bank provides a wide range of corporate and retail banking services and other related financial services. Corporate and retail banking services provided by the Bank include lending and trade finance facilities, consumer financing, overdraft facilities, mandatory provident fund services, provision of fixed deposits, current and savings accounts, credit card services and personal wealth management services. Other related financial services offered by the Bank include remittance and money exchange, safe deposit boxes, auto pay and direct debit services. The Bank is also engaged in treasury activities and securities dealing activities, which include inter-bank placement and deposit transactions, the management of overall interest rate risk and liquidity of the Bank and centralised cash management as well as other business activities such as investment holding and property investment. The Bank also offers futures and securities trading and insurance services through certain of its wholly-owned subsidiaries.

Since its inception in 1948, the Bank has expanded steadily and believes that it has successfully established itself as a reliable and prudent bank in Hong Kong as well as the other jurisdictions in which it operates. Despite its relatively small size, the Bank enjoys long-standing relationships with many of its key customers and believes that it possesses a strong and stable deposit base. As at 30 June 2010, the Bank's total assets, shareholders' funds, advances to customers and customer deposits amounted to HK\$70,728 million (U.S.\$9,085 million), HK\$6,287 million (U.S.\$808 million), HK\$35,553 million (U.S.\$4,567 million) and HK\$60,515 million (U.S.\$7,773 million), respectively.

For the year ended 31 December 2009 and the six months ended 30 June 2010, the Bank recorded a net profit of HK\$232 million (U.S.\$30 million) and HK\$193 million (U.S.\$25 million), respectively. As at 30 June 2010, the Bank's capital adequacy ratio, loan-to-deposit ratio and average liquidity ratio were 15.24%, 53.81% and 45.01%, respectively. For the six months ended 30 June 2010, the Bank achieved an annualised return on average assets of 0.59% and a return on average shareholders' funds of 6.23%. See "*Summary Financial and Other Information — Other Selected Financial Data*".

The Bank maintains correspondent banking relationships with approximately 300 foreign banks and provides services such as Hong Kong dollar clearing services for foreign banks that maintain Hong Kong dollar and/or U.S. dollar accounts with the Bank, negotiation and advisory services in relation to letters of credit as well as trade enquiries, transfers and remittances.

The Bank has been listed on the HKSE since July 1994. As at 30 June 2010, the authorised share capital of the Bank was 600 million ordinary shares of HK\$0.50 each, of which 435 million ordinary shares have been issued and are outstanding and fully paid. Based on the closing price of its shares on the HKSE on 30 June 2010 the Bank had a market capitalisation of approximately HK\$6,473 million.

### History

The Bank was founded in 1948 in Hong Kong under the name "Liu Chong Hing Savings Bank" with the objectives of promoting savings, assisting industry and commerce and providing banking services to the public. In 1955, it was granted a banking licence by the HKMA and in the same year, it was formally incorporated.

In 1973, The Bank of Tokyo-Mitsubishi UFJ, Ltd (formerly known as "The Mitsubishi Bank, Limited" and "The Bank of Tokyo-Mitsubishi, Ltd") acquired a 25% interest in the Bank. Through this

affiliation, the Bank enjoyed an increase in Japanese and correspondent banking services. In the same year, Liu Chong Hing Investment Limited acquired a majority interest in the Bank of 57.67%, through its wholly-owned subsidiary, Liu Chong Hing Estate Company, Limited. Liu Chong Hing Investment Limited is a public company which has been listed on the HKSE since 1972 and is principally engaged in property development, investment and insurance activities. As at 30 June 2010, it held a 48.52% indirect interest in the Bank.

In 1975, the Bank introduced online computerised services for all of its deposit accounts, which were subsequently upgraded in 1980 and 1987. The Bank believes that it is one of the first locally incorporated banks to provide such services.

In 1977, the Bank established a depositary agency in San Francisco to provide services to its existing customers who were engaged in business in San Francisco as well as to foster the Bank's trade finance business between Hong Kong and the United States. In September 1995, the Bank was granted a full wholesale banking branch licence in the United States, which allowed it to accept deposits from United States residents, subject to certain conditions.

In June 1982, the Bank introduced through-the-wall automated teller machines ("ATMs") to its operations and in January 1986, the Bank's ATM network was linked to the Joint Electronic Teller Services Limited ("JETCO") network comprising a central data processing system connected to ATMs belonging to 44 banks in Hong Kong, which enabled the Bank to use ATMs of other banks in the system. In October 1984, the Bank became a founding member of the Easy Pay System, an electronic retail point of sale payment system.

As part of its continuing drive to capitalise on opportunities created by the further liberalisation of the financial markets in Mainland China and the increased business activity between the PRC and Hong Kong, the Bank set up a representative office in Shanghai in 1988. In April 1993, the Bank established a full service foreign bank branch in Shantou in the Guangdong province of the PRC.

In October 1993, the Bank introduced fully automated telephone banking services for its retail customers.

In 1994, Liu Chong Hing Estate Company, Limited and The Bank of Tokyo-Mitsubishi UFJ, Ltd entered into a shareholders' agreement, which enabled the Bank to gain access to updated technology, expertise in international banking, management know-how, market development and a firm foundation for future growth, through mutual co-operation with and support from The Bank of Tokyo-Mitsubishi UFJ, Ltd. On 11 July 1994, the Bank was publicly listed on the HKSE. Its listed shares were selected as a constituent stock of the Hang Seng MidCap 50 Index in 1996 and, subsequently, a constituent stock of the Hang Seng Composite Index.

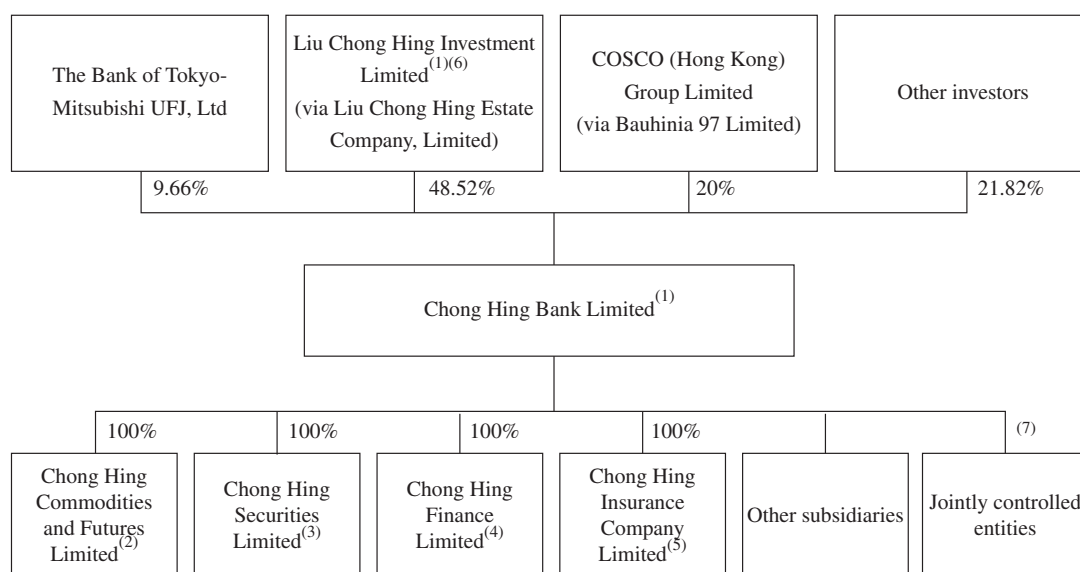
In 1997, the Bank established a branch in Macau.

In 1999, the Bank formed the Bank Consortium Holding Limited (the "**Bank Consortium**") with nine other local banks in Hong Kong with the objective of providing quality Mandatory Provident Fund ("**MPF**") services (with both the Master Trust Scheme and the Industry Scheme) through the Bank Consortium Trust Company Limited, a wholly-owned subsidiary of the Bank Consortium. In the same year, the Bank established a representative office in Guangzhou, PRC.

In December 2006, the Bank changed its name from "Liu Chong Hing Bank Limited" to "Chong Hing Bank Limited". On 27 December 2006, the Bank relocated its head office operations to a newly redeveloped building along 24 Des Voeux Road Central, which has been named "Chong Hing Bank Centre".

## Corporate Structure

The chart below illustrates the corporate structure of the Bank as at 30 June 2010:



- (1) Listed on the HKSE.
- (2) Registered with The Hong Kong Futures Exchange Limited as a participant.
- (3) Registered with the HKSE as a participant.
- (4) Licensed under the Banking Ordinance (Cap. 155 of the Laws of Hong Kong) as a deposit-taking company.
- (5) Licensed under the Insurance Companies Ordinance (Cap. 41 of the Laws of Hong Kong) as an insurance company.
- (6) As at 30 June 2010, Liu Chong Hing Investment Limited is approximately 45% owned by Liu's Holdings Limited, which is, in turn, owned by members of the Liu family.
- (7) The Bank also holds strategic investments in a number of jointly controlled entities which include the Bank Consortium, BC Reinsurance Limited, Hong Kong Life Insurance Limited and Net Alliance Co., Limited. The Bank Consortium, a 13.3% jointly controlled entity, offers a wide range of services for retirement schemes, which facilitates the Bank to offer MPF services. BC Reinsurance Limited and Hong Kong Life Insurance Limited, a 21.0% and 16.7% jointly controlled entity, respectively, offer reinsurance and life insurance underwriting services, which enhance the insurance services offered by the Bank. Net Alliance Co., Limited, a 17.6% jointly controlled entity, provides a wide range of internet services.

The Bank is the holding company and the principal operating company of the Group. Through its shareholding relationships and mutual co-operation with Liu Chong Hing Investment Limited, COSCO (Hong Kong) Group Limited and The Bank of Tokyo-Mitsubishi UFJ, Ltd, the Bank benefits from cross-referrals, both locally and internationally, business promotion and market development of financial products and services as well as access to management know-how and updated technology.

The Bank's key subsidiaries are Chong Hing Commodities and Futures Limited, Chong Hing Securities Limited, Chong Hing Finance Limited and Chong Hing Insurance Company Limited. The Bank offers futures and securities trading and insurance services through its wholly-owned subsidiaries, Chong Hing Commodities and Futures Limited, Chong Hing Securities Limited and Chong Hing Insurance Company Limited whereas Chong Hing Finance Limited is principally engaged in deposit-taking. In addition, the Bank has a number of other wholly-owned subsidiaries whose business activities include property investment, credit card management, general merchant banking, and the provision of nominee services and electronic data processing services.

The Bank also holds strategic investments in a number of jointly controlled entities which include the Bank Consortium, BC Reinsurance Limited, Hong Kong Life Insurance Limited and Net Alliance Co., Limited. The Bank Consortium, a 13.3% jointly controlled entity, offers a wide range of services for retirement schemes, which facilitates the Bank to offer MPF services. BC Reinsurance Limited and Hong Kong Life Insurance Limited, a 21.0% and 16.7% jointly controlled entity, respectively, offer reinsurance and life insurance underwriting services, which enhance the insurance services offered by the Bank. Net Alliance Co., Limited, a 17.6% jointly controlled entity, provides a wide range of internet services. The Bank will continue to selectively consider suitable opportunities for strategic investments as they arise in the future.

## **Strategy**

The Bank's long-term strategy is to continue to strengthen its foundation, enhance its overall competitiveness, expand its operations both locally and overseas and provide its customers with quality and comprehensive financial and banking products and services. The Bank has formulated a strategic plan for the years 2009 to 2013 governing the direction and strategies for the Bank's future business development and growth.

The major components of the strategic plan are as follows:

### ***Position the Bank as a community bank in retail banking sector and seek opportunities to open branches in areas where the customers are underserved by large banks***

The Bank currently operates a network comprising a head office and 51 branches in Hong Kong. The Bank plans to widen its customer coverage by increasing the number of branches in Hong Kong up to 57 by 2013. The Bank expects to establish these branches in strategic locations across Hong Kong where the Bank currently does not have presence so as to tap into new customer bases. In particular, the Bank intends to explore establishing a presence in newly developed commercial and residential areas where there is a higher proportion of younger customers so as to diversify its customer base demographically. In addition, the Bank is also planning to establish a number of branches in selected shopping malls operated under The Link Management Limited. The Bank believes that it is able to operate on a cost-effective basis in such areas where the target customer base is much larger and underserved by large banks. To minimise the capital requirements for bank premises for these new branches, the Bank plans to establish the new branches mainly under long-term operating leases.

The Bank is also continually considering other suitable key locations in Hong Kong in which to set up more ATMs in order to expand the Bank's ATM network. The Bank currently operates a network of 54 ATMs, which are situated at the Bank's head office and branches in Hong Kong.

### ***Expand the Bank's deposits base by introducing new deposit products and enhancing its services***

The Bank derives a large proportion of its funding from customer deposits. In addition to expanding its branch network to increase its customer base, the Bank has implemented, and intends to continue to grow its deposit base steadily through, the following initiatives:

- focusing on building its foreign currency deposits and exchange capability to meet with growing customer need;
- focusing on middle/lower segments with customised sales, pricing and promotion strategy;
- building cross-selling capability to leverage on existing customer base of other retail products;
- offering attractive deposit rates to core and loyal customers with multiple relationships;

- enhancing internet banking and telephone banking services, which will enable its customers to perform more off-counter transactions;
- installing automatic banking facilities (such as automatic passbook printing) at its branches to upgrade and enhance banking services;
- increasing the number of promotional and marketing activities to attract new deposit customers;
- enhancing customer services by fostering a culture of courtesy among its customer service staff; and
- providing value-added services to its existing customers in order to cultivate their loyalty and retain their business.

Partly as a result of the Bank's increased promotional activities and marketing campaigns conducted in relation to its new deposit products, the Bank has recorded increased growth in its customer deposits. As at 30 June 2010, the Bank's customer deposits amounted to HK\$60,515 million (U.S.\$7,773 million), which represented a 1.3% increase from HK\$59,738 million as at 30 June 2009. The level of customer deposit has remained steady during the recent financial crisis, demonstrating the Bank's strength in having a diversified and stable customer deposit base. The Bank believes that its expanded and upgraded coverage network, coupled with a wider variety of deposit products offered to customers, will enable it to maintain its existing business as well as increase its customer base by attracting new customers.

***Improve and diversify the Bank's customer mix and income sources***

To compensate for the effects of decreasing interest rate margins and increased competition, the Bank intends to focus on diversifying its sources of income. In addition to introducing more tailored deposit products, the Bank is also in the process of (i) developing new banking products especially in RMB related areas to cater to existing and potential customers, (ii) expanding its credit card business to RMB/HK dollar dual currency credit card, (iii) increasing cross-selling opportunities, in particular, for mortgage, retail brokerage and insurance services, (iv) expanding its securities business by enhancing and improving its personal brokerage services, (v) extending its existing share financing business to its retail customers and (vi) increasing efforts to derive higher profit margins from its investment activities, (vii) developing new customer segments of auto loan dealers and customers in the private vehicle and licensed transport market; and (viii) growing foreign exchange income through the foreign currency deposit and exchange capability. The Bank has continued to enhance its sales capability through on-going trainings and the development of cross-selling programmes targeted at the existing customer base. Furthermore, the Bank has continuously enhanced its internet banking platform to encourage internet banking and securities dealing. The Bank believes that these initiatives, together with the expansion of its branch network, will diversify its income portfolio, enlarge its income base and reduce the Bank's reliance on any one source of income.

***Prudently increase the Bank's credit portfolios by leveraging the Bank's close relationship with Hong Kong corporations and residents by serving their financial needs through various stages of economic cycle***

The Bank aims to achieve steady growth in its corporate loan and retail loan portfolio. In addition to diversifying its overall income sources, the Bank believes that the development of additional loan products and services and the expansion of its overall loan portfolio will enable it to capitalise on growing opportunities in Hong Kong and Mainland China. As at 30 June 2010, local corporate loans (including trade finance loans) represented 66.1% of the Bank's total loan portfolio, local retail loans represented 22.6% and loans advanced for overseas uses represented 11.3%.



### *Corporate loan portfolio*

Corporate lending represents a major portion of the Bank's credit activities and the Bank intends to continue to strengthen its corporate credit portfolio and improve its risk-adjusted return by actively managing the sector, geographical, customer and product composition of its corporate credit portfolio. The intended growth and expansion in the Bank's corporate loan portfolio will be focused on certain key areas such as:

- lending to mid-sized corporates and companies listed in Hong Kong;
- trade finance and services to import and export companies;
- supporting small and medium-sized enterprises ("SMEs"), major industries in Hong Kong and PRC companies engaged in business in Hong Kong;
- lending to the hotel industry and other infrastructure development;
- lending to high net-worth individuals;
- share financing to medium to large-sized customers;
- placing more focus on cash flow lending in addition to secured lending for increased flexibility and to better cater to the changing needs of customers;
- participating in syndicated loans; and
- granting credit facilities to large corporations with business activities in Hong Kong and Asia (particularly in Mainland China).

The Bank plans to and is in the process of (i) establishing corporate and commercial banking centres in both Hong Kong Island and Kowloon, (ii) strengthening marketing efforts to solicit business from large corporations and high net-worth individuals, (iii) increasing flexibility in its facility structuring and service offerings, (iv) synchronising the Bank's internal risk assessment and credit policy with the Bank's target market positioning, (v) enhancing tailor-made services and products to corporate customers and (vi) reducing credit turnaround time to enhance speed and time to market. With these initiatives, the Bank aims to establish a boutique "Community Bank" image in the market as a relationship-oriented bank and to become the preferred banking partner and operating bank for corporate customers, particularly mid-sized corporates.

### *Retail loan portfolio*

Currently, the majority of the Bank's deposit customers comprise retail customers, out of which a large portion comprises middle-aged established individuals above 40 years of age. The Bank intends to leverage on its existing network of retail deposit customers to grow its retail credit portfolio in a prudent manner. In addition to improving its customer services at branches by upgrading and enhancing information technology systems and services as well as operation support systems to increase efficiency, reduce costs and turnaround time, the Bank intends to focus on growing certain components of its retail banking business, especially in high margin business such as consumer financing and auto-financing.

Furthermore, the Bank plans to build its residential mortgage loans business by increasing cross-selling of mortgage services as well as other retail banking products, offering competitive pricing and terms and conditions for its mortgages, soliciting co-operation with developers or property agencies to capitalise on business opportunities and offering its mortgage loan plans at more of its branches so as to shorten its loan application processing time. As at 30 June 2010, residential mortgages comprised approximately 17.1% of the Bank's total loan portfolio, which the Bank estimates to be low compared

to the proportion of most other locally incorporated banks and, accordingly, the Bank is of the view that there is still potential for growth in this business segment. The Bank is also in the process of developing more personal loan products such as unsecured overdrafts to attract young professionals. In addition, the Bank intends to focus on growing its share financing business on a retail level by offering share financing to its retail customers, which is currently offered mainly to corporate and institutional customers.

***Increase non-interest income by enhancing the Bank's existing services***

In addition to fees arising from credit businesses, the Bank aims to continue to increase non-interest income through existing services. The Bank's wholly-owned subsidiary, Chong Hing Securities Limited, has a proven securities dealing platform which allows customers to place orders through branches, telephone, dealing centres, internet and mobile electronic devices, and the Bank plans to continue to use this platform to build its customer base and commission income. The Bank has actively developed its foreign exchange income and insurance fee income through the growth of foreign currency deposits and insurance sales. The Bank aims to also increase its fees and charges on its safe deposit box and other general banking services in order to provide additional sources of fee income to the Bank.

**Business Overview**

The principal business segments of the Bank are corporate banking and retail banking. Other business activities include treasury activities, securities dealing activities, insurance, MPF services and other asset management and trustee services. The following table sets forth the contribution of each segment to the Bank's total operating income for the periods indicated.

	For the six months ended 30 June			
	2009		2010	
	(HK\$ thousands)	(percentage)	(HK\$ thousands)	(percentage)
Corporate and retail banking .....	291,213	46.2%	304,374	51.6%
Treasury activities .....	212,675	33.8%	184,338	31.3%
Securities dealing .....	92,834	14.8%	83,715	14.2%
Others .....	32,572	5.2%	16,846	2.9%
Total operating income .....	<u>629,294</u>	<u>100.0%</u>	<u>589,273</u>	<u>100.0%</u>

***Corporate banking***

The corporate banking business of the Bank comprises mainly lending activities to large corporate and institutional customers both in Hong Kong and Mainland China, which include the financing and refinancing of property developments, property investments and infrastructure projects, trade financing, commercial mortgages for purposes of purchasing retail, office and industrial space, and funding for general corporate requirements. The Bank also offers financial services such as remittance and money exchange services, safe deposit boxes, autopay and direct debit services on a corporate level.

The majority of the Bank's borrowers are Hong Kong companies that typically use the funds for projects and investments in Hong Kong and, to a lesser degree, in Macau and Mainland China. The Bank's lending activities in Mainland China are conducted mainly with its existing customers based in Hong Kong or referrals arising from its existing customer relationships who are engaged in business in Mainland China.

### *Commercial advances*

As at 30 June 2010, the amount of outstanding corporate advances (including trade finance loans) amounted to HK\$23,498 million (U.S.\$3,018 million), which represented 66.1% of the Bank's total outstanding advances.

Substantially all of the Bank's corporate advances are extended on a recourse basis and/or are secured by underlying projects. In the case of property financing, all advances are secured by a first registered charge over the underlying property and in most cases, together with a charge over all the sale and rental proceeds derived from the property. In some circumstances, the Bank may require additional collateral such as time deposits, listed securities and other financial instruments that the Bank deems acceptable. All overdrafts and term loans are renewed on an annual basis. The Bank's corporate advances range from relatively small amounts to that of several hundred million Hong Kong dollars and the average original maturity for instalment loans is approximately 16 years. Loan-to-value ratios for project financing are determined on a case-by-case basis. The maximum loan-to-value ratios for construction projects and commercial mortgages are approximately 60% and 70% of the total estimated completion value of the project and the prevailing market value of the commercial properties, respectively.

### *Trade finance*

The trade finance business of the Bank comprises mainly advances and credits to commercial, corporate and institutional customers, which include overdraft facilities, letter of credits, trust receipt financing, short-term advances, packing credits and export financing for the purpose of accommodating customer's working capital requirements. The Bank also provides other trade finance related services to its customers, including advising and transfer of export documentary credits, shipping guarantee, negotiation of bills under documentary credits and collection of bills. The majority of trade finance advances are secured by a mortgage of property or cash collateral, although advances may be made on a partially secured or on an unsecured basis. Trade finance advances typically have a relatively shorter maturity and most of the Bank's trade finance advances have a maturity period ranging from 60 to 150 days. As at 30 June 2010, the Bank's total outstanding trade finance advances amounted to HK\$767 million (U.S.\$99 million), which represented 2.2% of the Bank's total outstanding advances.

The Bank's trade finance customers comprise mainly manufacturing companies, SMEs, large trading companies and multinational corporations. The Bank intends to continue to increase income contribution from trade finance as its existing customers increase the size and scope of their operations and by providing its customers with customised service through its experienced trade finance staff. The trade finance sector in Hong Kong is well developed and, consequently, the Bank is also seeking to capitalise on its overall reputation and existing network in the PRC to deliver trade finance services to its increasing number of HK-based customers with operations in the PRC. The Bank also intends to increase trade financing provided to import and export companies.

### *Syndicated Lending*

The Bank is also engaged in the Hong Kong syndicated lending market. The majority of the Bank's syndicated advances are extended to local companies engaging in property development or investment in completed developments, large local conglomerates and large Mainland China private or state-owned enterprises. The Bank's typical commitment per advance is between HK\$50 million and HK\$400 million.

The syndicated corporate lending market has remained active as both large and medium-sized enterprises took advantage of the high level of bank liquidity in Hong Kong to finance their expansion projects and/or refinance their existing debt. In addition, large PRC corporations continued to tap the local syndicated lending market to finance their overseas acquisitions. Despite this increase in activity, interest margins on syndicated loan transactions continued to decline as the credit market

stabilised and due to keen competition. In order to improve its yield return and broaden its customer base, the Bank intends to continue to focus on increasing its lending activities to high quality companies in the middle market as the Bank believes that the margins associated with borrowers from this sector are typically more attractive than margins on unsecured syndicated advances to the larger property developers in the market.

### *Retail banking*

Retail banking comprises personal banking (including deposits, residential mortgage financing and other consumer financing) and wealth management services (including insurance and investment) to individual customers and small companies. The Bank also offers financial services such as remittance and money exchange services, safe deposit boxes, autopay and direct debit services on a retail level and provides phone banking and internet banking services to its customers.

### *Residential and commercial mortgages*

Residential mortgages represent the largest segment of the Bank's total advances to retail customers, accounting for 83.1% of the Bank's total retail loan portfolio and 18.8% of the Bank's total loan portfolio as at 30 June 2010, and includes advances guaranteed by the Hong Kong Government under GHOS, Private Sector Participation Scheme ("PSPS") and Tenants Purchase Scheme ("TPS") to assist lower income families in purchasing homes. Advances under GHOS, PSPS and TPS accounted for an aggregate of HK\$595 million (U.S.\$76 million), which represented 1.7% of the Bank's total loan portfolio as at 30 June 2010. The Bank has established a strong retail and corporate customer base that provides an ongoing source of residential and commercial mortgage business. Property developers, solicitors and real estate agencies are also sources of referrals. The majority of the residential mortgages are owner-occupied properties. The Bank has also taken on investment properties, both residential and commercial, largely from existing customers with significant net-worth.

All home mortgage advances are secured by a first registered charge over the property and, in certain circumstances, the Bank may also require personal guarantees as additional security. Home mortgages typically include floating interest rates and are repayable by instalments. The contractual tenor of mortgage loans has been capped at 30 years though the actual tenor is much shorter. Competitive pricing and buoyancy of the property markets are common causes of refinancing and early redemptions. The Bank offers mortgage loan advances within the loan-to-value ratio limits as specified by the HKMA from time to time. Amount in excess of these limits are covered by insurance providers through approved Mortgage Insurance Schemes.

### *Consumer financing*

Consumer advances are generally higher yield loans and include overdrafts, secured and unsecured advances to individuals for a variety of purposes such as tax payments, general investment purposes, travel, hospitalisation, educations and home improvements.

Applications for consumer advances are processed by qualified underwriters based on established guidelines approved by the Loans Committee and are subject to regular credit reviews.

As at 30 June 2010, the Bank's total outstanding consumer advances (including credit card advances) amounted to HK\$1,352 million (U.S.\$174 million), which represented 16.9% of the Bank's retail loan portfolio and 3.8% of the Bank's total loan portfolio.

The Bank has gradually built up its consumer finance portfolio through gradual growth of its personal loan and tax loan business. The Bank has a prudent credit policy and delinquency and

write-offs are below market averages. The Bank has, over the past years, launched frequent campaigns with attractive pricing, simplified procedures and fast approval turnaround in capturing a growing number of new customers. The Bank will focus on growing overdraft business through existing customers.

### *Credit cards*

The Bank became a principal member of VISA in 1998 and a principal member of Master Card International in 2000. Apart from issuing a variety of regular, gold and platinum credit cards as its core products, the Bank also offers co-brand cards and corporate cards to business partners and affinity cards with various professional, educational and commercial institutions and association in Hong Kong.

As of 30 June 2010, the Bank has issued over 100,000 credit cards.

The Bank had taken active steps in to add value to its credit cards. In 2010, the Bank is planning to launch (RMB/HK dollar) dual currency credit cards to tap into the frequent PRC travellers market. In face of thinning margins and saturation of the market, the Bank has worked with a number of business partners in offering co-branded cards with exclusive benefits and privileges. Both the MSN and LINK co-brand cards are generating a reasonable number of cardholders in the portfolio. The former focused on the younger generation, while the latter targets at the middle income group within shopping malls operated under The Link Management Limited where the Bank has a strong presence.

Credit cards rely heavily on interest income from the rollover customer segment which has diminished gradually over the past years. The thinning of margins had prompted card issuers, including the Bank, to take on a slower pace in card growth. The Bank has engaged in cross-selling activities at its existing branch network to offer new cards to existing customers.

The Bank has a merchant business which has experienced growth in terms of number of customers and profitability over the last three years.

### *Treasury activities*

The Bank's treasury activities primarily consist of money market transactions, investment portfolio management and proprietary and other interbank and capital market activities conducted on behalf of the Bank. Both the Bank and its wholly-owned subsidiary, Chong Hing Securities Limited, engaged in limited proprietary trading activities. Treasury operations are also responsible for managing the funding and liquidity positions of the Bank and other market risk positions arising from banking activities. The Bank generally maintains an insignificant open foreign exchange position.

The Bank is also engaged in foreign exchange trading activities as well as equity and futures stock broking on behalf of its customers. Income derived from foreign exchange activities is generated mainly from services provided to customers in the form of foreign exchange trading and forward contracts. As at 30 June 2010, the Bank had a limited exposure to structured credit products, which comprised single reference entity credit linked notes arranged directly with banks.

As a matter of policy, the Bank generally discourages aggressive trading activities and foreign exchange trading activities are typically engaged on behalf of its customers as part of the Bank's overall banking business. Historically, treasury activities on a proprietary basis constitute a minor proportion of the Bank's business activities. Off-balance sheet derivatives are used only for hedging customers and the Bank's positions. However, in order to increase the rate of return derived from its total asset portfolio, the Bank intends to expand prudently its treasury operations and is currently in the process of establishing specialised corporate dealing desks and upgrading its systems to improve and diversify its services. The Bank is also hiring more personnel, such as dealers to manage surplus funds and arbitrage opportunities and professionals to develop new structured products.

## *Securities dealing*

Stock broking activities and dealings in Hang Seng Index futures, options and other derivative products are conducted through the Bank's wholly-owned subsidiaries, Chong Hing Securities Limited and Chong Hing Commodities and Futures Limited, on an agency basis. This has grown to provide a stable source of additional income for the Bank even during the last few years where there has been volatility in the Hong Kong stock market.

Chong Hing Securities Limited was admitted as the first batch of brokers adopting the AMS/3 (OG/BSS) system of the HKSE and provides a range of securities related services through the Bank's branches as well as its own branches and dealing platform. During 2009, the number of users of and transactions conducted through "Chong Hing i-Web Stock Trading Service" increased substantially, reflecting the wide acceptance of the securities service by customers.

As part of business development, Chong Hing Securities Limited continued to expand its electronic securities trading services. In January 2010, "Chong Hing Mobile Securities Service" was launched, enabling customers to conveniently conduct stock transactions online anywhere using their smartphones or personal digital assistant devices. The platform enables customers to deal with their securities investments anytime, anywhere. With the launch of a marketing campaign, the service was positively received by customers. Compared with that of the same period last year, the number of users of electronic securities trading services rose by more than 20% for the first half of 2010.

## *Others*

### *Insurance*

The Bank conducts its main insurance business through its wholly-owned subsidiary, Chong Hing Insurance Company Limited, which was acquired in June 2005 to serve as a division for the Bank's insurance business. Chong Hing Insurance Company Limited provides a diversified range of insurance services, including fire insurance, marine insurance, motor vehicle insurance, employee's compensation insurance, public liability insurance and property insurance. Insurance products offered by Chong Hing Insurance Company Limited are distributed through the Bank's branch network, insurance agents, brokers, allied partners and internet websites of both the Bank and Chong Hing Insurance Company Limited.

The Bank also offers a comprehensive range of both individual and group life and medical insurance, general and travel insurance through its 16.7% owned jointly-controlled entity, Hong Kong Life Insurance Limited.

For the year ended 31 December 2009, Chong Hing Insurance Company Limited's premium income derived from its insurance business amounted to HK\$34 million (U.S.\$4 million), which represented a decrease of 5.5% as compared to the year ended 31 December 2008. For the six months ended 30 June 2010, Chong Hing Insurance Company Limited's premium income was HK\$16 million (U.S.\$2 million), which represented an increase of 3.9% as compared to the six months ended 30 June 2009.



The Bank offers a comprehensive range of MPF services, including trustee, scheme administration, investment management and custody services to employers, employees and the self-employed through its 13.3% owned jointly-controlled entity, the Bank Consortium. The Bank Consortium is currently collectively owned by the Bank, Asia Financial Holdings, Dah Sing Bank, Shanghai Commercial Bank, Wing Hang Bank, Wing Lung Bank, Fubon Bank, and Industrial and Commercial Bank of China (Asia). The Bank Consortium also offers a full range of pension products which include the Bank Consortium MPF Plan (a master trust scheme), the Bank Consortium Industry Plan (an industry scheme), BCT Premier Pooled ORSO Retirement Plan (an ORSO scheme) for Employer Sponsored Scheme and scheme administration for other registered MPF schemes. Customers can choose from the BCT MPF plans a wide range of funds to meet their individual investment and retirement needs.

### ***Internet Banking Services***

As part of its general banking business, the Bank offers internet banking services to its customers which allow them to manage their accounts on the internet. The Bank's internet banking services comprise a wide variety of banking functions, including balance enquiries, rate enquiries, funds transfers, time deposit, bill payment, credit card transactions and MPF account enquiries and contributions.

As at 30 June 2010, the Bank had over 31,000 registered internet banking users, which represented an increase of 13% as compared to as at 30 June 2009, and the average daily transaction volume for the six months ended 30 June 2010 exceeded 6,000 transactions.

The Bank also offers internet-based brokerage service (including real-time internet stock price quote service) through its wholly-owned subsidiary, Chong Hing Securities Limited, which allows customers to trade securities on the internet. Chong Hing Securities Limited was admitted as part of the first batch of brokers adopting the Broker Supplied System under the AMS/3 system, which allowed its dealing operations to run under a fully automated straight-through processing environment. Over the past few years, Chong Hing Securities Limited has instituted various incentive schemes to encourage clients to execute trades via its user-friendly electronic trading platform and the Bank believes that these schemes have been well-received by its customers. As at 30 June 2010, more than 42% of Chong Hing Securities Limited's trading customers had registered internet-based securities client accounts with its internet-based brokerage service, and the volume of transactions executed via the internet-based brokerage system accounted for approximately 29% of the total number of trades and approximately 25% of Chong Hing Securities Limited's total turnover.

### **Information Technology**

The Bank's management information system is currently operated based on a cost-effective "open system" based core banking system composing UNIX and Oracle Database. The Bank's strategy is to increase the use of information technology in its business, including its front-office and back-office operations, in order to enhance its business capabilities, products and services, and the Bank intends to continue upgrading its information technology capabilities in order to meet its growth objectives. The Bank is also dedicated to ensuring security and regulatory compliance in its information technology systems.



## International Operations

The Bank's international operations were commenced to meet the requirements of its existing core customers as their interests expand overseas from Hong Kong. The table below sets forth the Bank's branches and representative offices outside Hong Kong.

Operations	Country	Year of Establishment
Representative office in Guangzhou .....	PRC	1999
Branch in Macau .....	PRC	1997
Branch in San Francisco .....	USA	1977
Representative office in Shanghai .....	PRC	1988
Branch in Shantou .....	PRC	1993

The Bank's Shantou branch began its cross-border Renminbi trade settlement business with the Bank's Head Office on 19 July 2010. In October 2009, the Bank's Shantou branch received approval to accept fixed deposits from PRC citizens with a minimum of RMB1 million for each transaction. The Bank also intends to upgrade its representative offices in Shanghai and Guangzhou to full-service foreign branches at an appropriate time to further exploit the business opportunity in the PRC.

## Group Structure

As at the date of this Offering Circular, the Bank has a total of 8 principal subsidiaries and 4 jointly controlled entities. The Bank is the holding company and the principal operating company of the Group. The Bank has a number of significant subsidiaries through which the Bank conducts various operations such as stockbroking, insurance, property investment and certain fee-based activities. As at the date of this Offering Circular, save for Chong Hing Securities Limited, none of the Bank's subsidiaries account for 2% or more of the consolidated net profit and loss of the Bank or has a book value of 0.4% or more of the Bank's consolidated total assets.

The table below sets forth a summary of the Bank's principal subsidiaries as at the date of this Offering Circular:

Name of subsidiary	Place of incorporation/ operation	Issued and fully paid ordinary share capital	% of issued share capital held by the Bank	Nature of business
Chong Hing (Nominees) Limited	Hong Kong	HK\$100,000	100%	Provision of nominee services
Chong Hing Finance Limited	Hong Kong	HK\$25,000,000	100%	Deposit-taking and lending
Chong Hing Information Technology Limited	Hong Kong	HK\$100,000	100%	Provision of electronic data processing services

<b>Name of subsidiary</b>	<b>Place of incorporation/ operation</b>	<b>Issued and fully paid ordinary share capital</b>	<b>% of issued share capital held by the Bank</b>	<b>Nature of business</b>
Chong Hing Securities Limited	Hong Kong	HK\$10,000,000	100%	Stockbroking
Chong Hing Commodities and Futures Limited	Hong Kong	HK\$5,000,000	100%	Investment holding and commodities and futures broking
Gallbraith Limited	Hong Kong	HK\$16,550,000	100%	Property investment
Card Alliance Company Limited	Hong Kong	HK\$18,000,000	100%	Credit card management
Chong Hing Insurance Company Limited	Hong Kong	HK\$85,000,000	100%	Insurance underwriting

The table below sets forth a summary of the Bank's jointly controlled entities as at the date of this Offering Circular:

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


## Properties

The Bank currently owns properties with an aggregate floor area of approximately 340,000 square feet in Hong Kong, which include the newly redeveloped building in which the Bank's headquarters is located. Most of the Bank's properties are used as banking offices, as branches or for back office operations. The remainder are currently leased to third parties. In addition, the Bank also leases properties with an aggregate floor area of approximately 134,000 square feet in Hong Kong. These leased properties are used as banking offices, as branches and for back office operations.

The Bank intends to obtain office space held on long-term operating leases for all of its new branches which it expects to set up in the next three years.

## Intellectual Property

The Bank relies on domain name registrations to establish and protect its internet domain names. The Bank has registered a number of internet domain names, including "www.chbank.com" and "www.chbank.com.hk".

The Bank has registered "  創興銀行 " as a trade mark with the Trade Marks Registry, Intellectual Property Department of the Government of the Hong Kong Special Administrative Region.

## Insurance

The Bank maintains various types of insurance coverage, including property insurance to cover the loss of or damage to building structure and content, electronic equipment and motor vehicles; insurance to cover loss of property due to burglary, theft and robbery; public liability insurance to cover legal liability as a result of physical bodily injury and/or property damage caused to third parties; bankers blanket bonds insurance to cover the loss resulting from fraudulent acts (including computer-related crimes) by employees, loss of money on premises and in transit and forgery of bank instruments; directors' and officers' liability insurance to cover the personal liability of the Bank's officers against any claims resulting from any wrongful act committed in connection with carrying out their duties as officers of the Bank; employees' liability insurance as required by the Employees' Compensation Ordinance (Cap. 282 of the Laws of Hong Kong); and group medical insurance for its workforce. The Bank also requires borrowers to obtain appropriate insurance coverage for security provided by them.

## Competition

The Hong Kong banking industry is mature and the Bank faces intense competition from a number of Hong Kong incorporated banks and branches of international banks, particularly in the home mortgage lending sector and deposit-taking business. In addition, the Bank faces keen competition from local finance companies in certain areas of its business, such as credit cards and hire purchase.

Given the increasing competition among the local banks in Hong Kong, the Bank has decided to focus on diversifying its revenue sources and increasing its fee based income, particularly from its wealth management and retail investment businesses. In addition, like many of the local banks in Hong Kong, the Bank is now focusing on expanding its presence in Mainland China and Macau. However, in view of the fact that certain restrictions previously imposed on foreign banks in Mainland China have recently been lifted, the Bank expects competition to continue to increase in the region.

For a further discussion of the risks of competition faced by the Bank in Hong Kong, see "*Investment Considerations*".

## Litigation

Save as otherwise disclosed in this Offering Circular, neither the Bank nor any of its subsidiaries is currently involved in any litigation, arbitration or similar proceedings and the Bank is not aware of any such proceedings pending or threatened against it or any of its subsidiaries which are or might be material in the context of the issue of the Notes.

## Employees

As at the date of this Offering Circular, the Bank had a total of 1,475 employees as set forth in the following table:

	<u>No. of employees</u>
Head office .....	1,296
Overseas (including Mainland China).....	45
Subsidiaries .....	<u>134</u>
Total .....	<u><u>1,475</u></u>

Approximately 18% of the Bank's employees as at 30 June 2010 performed managerial and management functions.

The Bank views its employees as an asset and believes that investment in human resources is critical to its growth. The Bank has training programmes, both internal and external, aimed at management development and team building. The Bank's training curriculum includes courses on banking operations, product knowledge, marketing, management skills and customer service.

The Bank believes that it enjoys a good relationship with its employees. None of the Bank's employees are members of a trade union. The Bank provides subsidised mortgage, low-interest housing advances, life and medical insurance benefits and maintains a pension fund scheme for its employees. The Bank also operates employee share option schemes under which options to purchase shares in the Bank can be granted to eligible employees and Executive Directors. As at the date of this Offering Circular, no options to purchase shares under any of its employee share option schemes had been granted by the Bank.

## SELECTED STATISTICAL AND OTHER INFORMATION

The selected statistical and other information set forth below relates only to the Bank and has, except where otherwise indicated, been compiled as at and for each of the three years ended 31 December 2007, 2008 and 2009 and each of the six month periods ended 30 June 2009 and 2010, respectively, and should be read in conjunction with the information contained elsewhere in this Offering Circular, including “*Business of the Bank*”.

### Advance Portfolio

#### Overview

As at 30 June 2010, the Bank’s total outstanding gross advances to customers were HK\$35,553 million (U.S.\$4,567 million), which represented 50.3% of its total assets. The majority of the Bank’s advances are in respect of home mortgages and advances for property investment and development, which together represented 43.9% (excluding advances under GHOS, PSPS and TPS) of the Bank’s total advances to customers as at 30 June 2010.

The table below sets forth a summary of the Bank’s gross advances by sector as the dates indicated.

	As at 31 December						As at 30 June	
	2007	Percentage of total	2008	Percentage of total	2009	Percentage of total	2010	Percentage of total
(HK\$ millions, except percentages)								
Loans for use in Hong Kong								
Industrial, commercial and financial								
— Property development .....	2,135	6.7%	1,449	4.4%	1,516	4.6%	1,599	4.5%
— Property investment .....	6,507	20.5%	7,561	22.7%	7,712	23.5%	7,917	23.3%
— Financial concerns .....	2,524	8.0%	3,031	9.1%	1,990	6.1%	2,237	6.3%
— Stockbrokers .....	347	1.1%	158	0.5%	311	0.9%	455	1.3%
— Wholesale and retail trade ..	834	2.6%	977	2.9%	1,019	3.1%	1,108	3.1%
— Manufacturing .....	2,225	7.0%	2,051	6.2%	1,414	4.3%	1,209	3.4%
— Transport and transport equipment .....	630	2.1%	933	2.8%	642	2.0%	787	2.2%
— Recreational Activities .....	45	0.1%	3	0.0%	2	0.0%	1	0.0%
— Information Technology .....	—	0.0%	—	0.0%	—	0.0%	—	0.0%
— Others <sup>(1)</sup> .....	4,830	15.3%	5,297	16.0%	6,319	19.3%	7,418	20.8%
Individuals								
— Loans for the purchase of flats under the Government Home Ownership Scheme, the Private Sector Participation Scheme and the Tenant Purchase Scheme	680	2.1%	694	2.1%	618	1.9%	595	1.7%
— Loans for the purchase of other residential properties ..	4,705	14.8%	5,457	16.4%	5,918	18.0%	6,076	17.1%
— Credit card advances .....	134	0.4%	116	0.3%	97	0.3%	80	0.2%
— Others <sup>(2)</sup> .....	1,677	5.3%	1,558	4.7%	1,498	4.6%	1,272	3.6%
— Sub-total .....	27,273	86.0%	29,285	88.1%	29,056	88.6%	30,754	86.5%
Trade finance .....	918	2.9%	804	2.4%	692	2.1%	767	2.2%
Loans for use outside Hong Kong <sup>(3)</sup> .....	3,531	11.1%	3,156	9.5%	3,046	9.3%	4,032	11.3%
Total advances to customers .....	31,722	100.0%	33,245	100.0%	32,794	100.0%	35,553	100.0%

Notes:

(1) “Others” includes the civil engineering, utilities, telecommunications and hotel industries.

(2) “Others” includes professional and private individuals for other private purposes.

(3) This refers to loans to customers the proceeds of which are not used in Hong Kong

## Geographical Concentration

The table below sets forth a summary of the Bank’s gross advances to customers by geographical location as at the dates indicated.

	As at 31 December						As at 30 June	
	2007	Percentage of total	2008	Percentage of total	2009	Percentage of total	2010	Percentage of total
<i>(HK\$ millions, except percentage)</i>								
Hong Kong .....	29,035	91.6%	31,322	94.2%	31,089	94.8%	34,024	95.7%
PRC .....	186	0.6%	383	1.2%	396	1.2%	347	1.0%
Macau .....	1,184	3.7%	466	1.4%	143	0.4%	158	0.4%
United States of America .....	327	1.0%	332	1.0%	389	1.2%	394	1.1%
Others .....	990	3.1%	742	2.2%	777	2.4%	630	1.8%
Total .....	<u>31,722</u>	<u>100.0%</u>	<u>33,245</u>	<u>100.0%</u>	<u>32,794</u>	<u>100.0%</u>	<u>35,553</u>	<u>100.0%</u>

## Customer Advance Concentrations

The Hong Kong Banking Ordinance generally prohibits any bank incorporated in Hong Kong from maintaining a financial exposure to any single person or group of connected persons in excess of 25% of its capital base. For a discussion of “financial exposure”, see “*Regulation and Supervision — Principal Obligations of Banks — Financial Exposure to Any One Customer*”. As at 30 June 2010, the Bank’s 20 largest borrowers (including groups of individuals and companies) accounted for approximately HK\$7,478 million (U.S.\$961 million), or 21% of the Bank’s gross advances, with the largest accounting for HK\$500 million (U.S.\$64 million), or 1.4% of the Bank’s gross advances.

## Advance Analysis

Approximately 28.5% of advances had a remaining maturity of more than five years as at 30 June 2010. The following table sets forth a summary of the Bank’s gross advances by remaining maturity as at the dates indicated.

	As at 31 December						As at 30 June	
	2007	Percentage of total	2008	Percentage of total	2009	Percentage of total	2010	Percentage of total
<i>(HK\$ millions, except percentage)</i>								
Repayable on demand <sup>(1)</sup> .....	2,511	8.0%	2,507	7.6%	1,456	4.3%	1,386	3.9%
3 months or less .....	4,105	12.9%	4,472	13.5%	3,736	11.4%	5,302	14.9%
1 year or less but over 3 months ..	4,790	15.1%	4,868	14.6%	4,774	14.6%	6,711	18.9%
5 years or less but over 1 year ....	10,605	33.4%	11,572	34.8%	13,015	39.7%	12,025	33.8%
After 5 years .....	9,496	29.9%	9,550	28.7%	9,629	29.4%	10,049	28.3%
Undated .....	215	0.7%	276	0.8%	184	0.6%	80	0.2%
Total gross advances to customers.	<u>31,722</u>	<u>100.0%</u>	<u>33,245</u>	<u>100.0%</u>	<u>32,794</u>	<u>100.0%</u>	<u>35,553</u>	<u>100.0%</u>

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*Note:*

(1) Includes overdrafts

As at 30 June 2010, approximately 93% of advances made by the Bank were at floating rates of interest (see “*Asset and Liability Management*”), with the balance being made at fixed interest rates. The rates for home mortgage advances and commercial mortgage advances in Hong Kong typically range from 3% below the prime rate to the prime rate. The effective annualised interest rate for Hong Kong dollar consumer finance advances (other than overdrafts) ranges from 3.76% to 7.93%. The interest rate for Hong Kong dollar trade finance advances made by the Bank is typically a margin over the prime rate. The interest rate for project finance lending and syndicated lending is typically a margin over the HIBOR. As at 30 June 2010, 96% of advances made by the Bank were denominated in Hong Kong dollars and 3% were denominated in U.S. dollars. Rates which are lower than the above rates may be offered by the Bank under appropriate circumstances.

Home mortgages are secured by a first registered charge over the underlying property. Working capital advances for businesses are typically secured by fixed and floating charges over land, buildings, machinery, inventory and receivables. Term advances for specific projects or developments are typically secured against the underlying project’s assets and its receivables, while additional guarantees are typically provided by the sponsors or shareholders. The Bank also receives guarantees in relation to certain of its other advances to cover, in the case of trade finance, any shortfall in security or, in the case of consumer advances to younger or less financially mature customers, to guarantee in what are otherwise unsecured advances.

All forms of security taken as collateral against credit facilities are monitored by the respective departments which extend the advances. In general, the collateral is periodically valued by an independent valuer to determine whether any additional collateral is required.

### **Credit Policies and Approval Procedures**

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

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

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

Credit approval on loans to individual customers and corporations is performed by the Loans Committee in accordance with the delegated lending authority from the Lending Policy of the Bank



with reference to a customer's objective of borrowing, financial strength, repayment ability, past account performance and collateral being offered as security, as appropriate. Approval from the Executive Loans Committee is required as and when the requested amount of the advance exceeds the delegated authority of the Loans Committee.

Credit approval on unadvised limits to bank counterparties is performed by the Bank's Asset and Liability Management Committee ("ALCO") with reference to the credit standing of the institutions. Endorsement by the Executive Management Committee is required for any increase in limit.

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

The exposure to any one borrower including banks and brokers is further restricted by sub-limits covering on and off-balance sheet exposures, and daily delivery risk limits in relation to trading items such as forward foreign exchange contracts. Actual exposures against limits are monitored daily.

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.

## **Asset Quality**

### ***Overview***

The performance of the Hong Kong economy is heavily dependent on the property sector, and property lending (excluding advances under GHOS, PSTS and TPS) accounted for 43.9% of the Bank's total advances to customers as at 30 June 2010. As a result, the Bank's asset quality is vulnerable to a decline in property prices. The ability of borrowers, including homeowners, to make timely repayment of their indebtedness may be adversely affected by rising interest rates or a slowdown in economic recovery. As at 30 June 2010, home mortgage advances (including advances under GHOS, PSPS and TPS) accounted for HK\$6,671 million (U.S.\$857 million) or 18.8% of the Bank's total advances to customers and accounted for one of the largest segments of the Bank's total advances to customers. See *"Investment Considerations — Considerations Relating to the Bank — Advance Concentration; Exposure to the Hong Kong Property Market"*.

Appropriate precautionary measures are taken to minimise credit loss arising from impaired loans and such measures include the monitoring of key indicators, such as account conduct, business performance, financial data, industry prospect, etc., and selecting an appropriate strategy, such as exit, request for additional collateral or suspension of limit for high risk customers. Precautionary measures against exposure to bank counterparties include the daily monitoring of movements in share price and prices of credit default swaps and the escalation to watch-list for further monitoring and actions, such as the suspension of unadvised limits, as considered appropriate by ALCO.

The Bank's preference for lending secured by security interests over chattels and real property and its conservative policy on loan to value ratios have helped to enable effective recovery actions on impaired loans.

The Bank conducts regular stress tests on customer loan portfolios, secured property values and exposure to bank counterparties to ensure that the level of risk assumed by the Bank is appropriate for the Bank.

Impaired loans are individually assessed loans with objective evidence of impairment.

The Bank believes that its advance classification policy is in compliance with the Hong Kong Banking Ordinance and the applicable guidelines of the HKMA.

### **Classification of Impaired Loans**

The Bank's impaired loans are sub-divided into three categories: sub-standard, doubtful and loss. When the repayment of an advance is uncertain (for example, there is a past-due record of 90 days or more and there would be a loss of an amount of principal or interest after taking into consideration the net realisable value of any collateral), the Bank downgrades the advance to sub-standard. If full recovery of the advance is in doubt and the Bank expects to sustain a loss of principal or interest, taking into account the net realisable value of any available secured property, the Bank classifies the advance as doubtful. Loss advances are those which are considered non-collectible after exhausting all collection efforts, such as the realisation of collateral and the institution of legal proceedings and the liquidator or official receiver has ascertained the relevant recovery ratio.

### **Impairment allowance under Hong Kong Financial Reporting Standards**

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.

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

The table below summarises the changes in the Bank's provisions for bad and doubtful debts/impairment allowance for the periods indicated.

	Years ended 31 December			Six months ended 30 June	
	2007	2008	2009	2009	2010
<i>(HK\$ millions, except percentages)</i>					
<b>Impairment allowance:</b>					
Beginning balance .....	137	135	115	115	134
Increase in impairment allowances .....	112	145	117	58	26
Amounts reversed .....	(29)	(54)	(15)	(4)	(6)
Amounts written off .....	(87)	(142)	(92)	(47)	(3)
Recoveries of advances written off in previous years .....	21	35	13	2	—
Unwinding effect of discount rate .....	(19)	(4)	(4)	(2)	—
Exchange Difference .....	—	—	—	—	—
Closing balance.....	<u>135</u>	<u>115</u>	<u>134</u>	<u>122</u>	<u>151</u>

	Years ended 31 December			Six months ended 30 June	
	2007	2008	2009	2009	2010
<i>(HK\$ millions, except percentages)</i>					

**Impairment allowance as a  
percentage of:**

Total gross loans and advances to customers at year/period end .....	0.4%	0.3%	0.4%	0.4%	0.4%
Total gross impaired loans and advances to customers at year/period end .....	62%	114%	250%	204%	346%

	Years ended 31 December			Six months ended 30 June	
	2007	2008	2009	2009	2010
<i>(HK\$ millions, except percentages)</i>					

**Write-offs as a percentage of:**

Average total loans during year/ period <sup>(1)</sup> .....	0.3%	0.4%	0.3%	0.1%	0.0%
Total gross loans and advances to customers at year/period-end .....	0.3%	0.4%	0.3%	0.1%	0.0%
Total gross impaired loans and advances to customers at year/period end .....	40.3%	140.6%	170.4%	78.3%	6.8%

*Note:*

- (1) Average balance of total gross loans and advances to customers is the average of the total gross loans and advances to customers at the beginning of the relevant year or period and the total loans at the end of the relevant year or period.

### ***Top Five Impaired Loans***

As at 30 June 2010, the Bank's five largest impaired loans accounted for 0.1% of its total advances. Approximately 61% of the value of the Bank's five largest impaired loans is attributable to a loan advanced by the Bank to a Hong Kong listed customer engaged in electronic manufacturing. As at 30 June 2010, the Bank's exposure under its five largest impaired loans (represented 88% of the total impaired loans) ranged from approximately HK\$23.5 million (US\$3 million) to approximately HK\$1.9 million (US\$0.24 million), amounted to approximately HK\$38.4 million (US\$4.9 million) in the aggregate.

### ***Impaired Loans Which Have Been Restructured***

The Bank's impaired loans are restructured on a case-by-case basis, subject to the approval of the appropriate lending parties for both the restructured limits and recovery measures. The Bank maintains a prudent reclassification policy. For example, if payments under an advance are rescheduled, that advance will not be reclassified and will remain under adverse classification (either as a sub-standard or doubtful advance) and may only be upgraded to a pass advance if the revised payment terms are honoured for a period of 6 months, in the case of monthly payments, and 12 months, in the case of quarterly or semi-annual repayments.

The following table sets forth, as at the dates indicated, the Bank's impaired loans including those that have been restructured through the rescheduling or principal repayments and deferral or waiver of interest.

	As at 31 December			As at 30 June
	2007	2008	2009	2010
<i>(HK\$ millions, except percentages)</i>				
Gross impaired loans .....	216	101	54	44
Impairment loss allowance, individual assessed.....	(18)	(6)	(26)	(34)
Net impaired loans.....	<u>198</u>	<u>95</u>	<u>28</u>	<u>10</u>
Gross impaired loans as a percentage of total gross loans and advances to customers .....	0.68%	0.30%	0.16%	0.12%
Net impaired loans as a percentage of total gross loans and advances to customers .....	0.62%	0.29%	0.09%	0.03%

### ***Held-to-maturity Debt Securities***

The Bank's held-to-maturity debt securities comprise both listed and unlisted debt securities, which included Hong Kong dollar and U.S. dollar denominated bonds and notes. None of the Bank's held-to-maturity debt securities have undergone significant revaluation for the years ended 31 December 2007, 2008 and 2009 and the six months ended 30 June 2010. As at 30 June 2010, the carrying value of these securities was HK\$15,934 million (U.S.\$2,047 million), which represented 92.6% of the Bank's total investments in securities. See "Asset and Liability Management" below.

The Bank carries out quarterly stress testing on its debt securities based on various scenarios on their credit standing.

The following table sets forth, as at the dates indicated, carrying values of the Bank's held-to-maturity debt securities, categorised by the types of issuers:

	As at 31 December						As at 30 June	
	2007		2008		2009		2010	
	Amount	Percentage	Amount	Percentage	Amount	Percentage	Amount	Percentage
<i>(HK\$ millions, except percentages)</i>								
Held-to-maturity securities issued by:								
Central government and central banks.....	535	3.4%	289	3.0%	182	1.1%	180	1.1%
Public sector entities .....	11	0.1%	68	0.7%	56	0.3%	57	0.4%
Banks and other financial institutions .....	15,060	96.5%	8,034	82.6%	14,767	87.1%	13,921	87.4%
Corporate entities .....	2	0.0%	1,337	13.7%	1,949	11.5%	1,776	11.1%
Total.....	<u>15,608</u>	<u>100.0%</u>	<u>9,728</u>	<u>100.0%</u>	<u>16,954</u>	<u>100.0%</u>	<u>15,934</u>	<u>100.0%</u>

## Asset and Liability Management

The Bank's asset and liability management is steered by the ALCO. The ALCO establishes policies and guidelines in respect of the maturity, pricing and volume of non-capital funding such that the Bank obtains funds in the most efficient and effective manner. Capital planning also comes under the supervision and review of the ALCO. The deployment of funds into various asset classes is reviewed regularly by the ALCO, having regard to the policies laid down for the management of the credit risk, the liquidity risk, the interest rate risk and the market risk. The ALCO consists of the senior staff members representing major divisions of the Bank.

Two key aspects of the Bank's asset and liability policy are liquidity risk management and interest rate risk management.

### Liquidity Risk Management

Liquidity risk is the risk that the Bank cannot meet its current obligations. The ALCO is responsible for monitoring the Bank's liquidity position, and does so through the periodic review of the statutory liquidity ratio, the maturity profile of assets and liabilities, loan-to-deposit ratio and inter-bank transactions. Liquidity policy is monitored by the ALCO and reviewed regularly by the Board of Directors of the Bank. The Bank's policy is to maintain a conservative level of liquid funds on a daily basis so that the Bank is prepared to meet its obligations when they fall due in the normal course of business and to satisfy statutory liquidity ratio requirements, and also to deal with any funding crises that may arise. Limits are set on the minimum proportion of maturing funds available to meet all the calls on cash resources such as overnight deposits, current accounts, maturing deposits, loan draw-downs and guarantees, and from margin and other calls on cash-settled derivatives and on the minimum level of inter-bank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand.

The Bank's average consolidated liquidity ratio and consolidated loan-to-deposit ratio were 45.01% (which was above the statutory minimum of 25%) and 53.81%, respectively, as at 30 June 2010.

The ALCO recommends internal target levels in respect of the monthly average liquidity ratio, monthly average Tier 1 liquidity ratio, and lowest daily liquidity ratio, and the weekly computation of liquidity ratio and Tier 1 liquidity ratio. The Bank's Finance and Treasury Management Division is responsible for monitoring these ratios and, where a tight liquidity position remains for a prolonged period, the Finance and Treasury Management Division reports the findings to the ALCO who, after

consultation with members of the Executive Committee decide the appropriate corrective actions to be taken. The liquidity positions of the Bank's overseas branches in Shantou, San Francisco and Macau are monitored through the submission of monthly management accounts and daily cash flow positions to the Bank's head office.

In managing liquidity risk the Bank measures, monitors and controls cash flow and maturity mismatch positions under different operating conditions. Under this cash flow approach the Bank believes that it has in place appropriate systems for:

- monitoring on a daily basis net funding requirements under normal business conditions;
- conducting regular cash flow analyses based on stress scenarios; and
- developing reasonable assumptions for making the above cash flow projections.

The Bank constructs a maturity profile that projects future cash flows arising from assets, liabilities and off-balance sheet transactions. All cash flows are allocated into a series of time bands according to their expected maturity dates for which the Bank is able to estimate the prospective net funding requirement. The profile enables the Bank to monitor short-term liquidity requirements as a priority and to review mismatch positions for medium to longer-term bands. Time bands within one month are monitored daily whilst longer bands are reviewed on a monthly basis. In calculating maturity mismatches, the Bank analyses historical experience and observations to determine cash flow patterns and derive behavioural assumptions applicable to the cash flows and takes into account not only contractual maturities but also adopts realistic assumptions underlying the behaviour of assets, liabilities and off-balance sheet activities. The Finance and Treasury Management Division is responsible for analysing the magnitude of the mismatches and discuss the findings with the ALCO and Executive Committee as appropriate.

The Bank conducts a programme of stress testing to assess the Bank's ability to meet obligations under institution-specific or general market funding crises and submits the results of such testing to the ALCO and the Risk Management and Compliance Committee for review on a regular basis. These systems and procedures are designed to enable the Bank to ensure that either a positive cash flow position is maintained or otherwise sufficient cash can be generated to satisfy the funding requirements on a daily basis.

The Bank's liabilities in foreign currencies other than U.S. dollars are incurred virtually exclusively from customer deposits, the majority of which are placed on deposits with other authorised institutions, and therefore the Bank's policy in respect of such currencies is to monitor liquidity on a matched basis. The Bank has a policy of taking deposits and holding assets denominated in only those hard currencies tradable in the interbank money market or currency forward market.

Although the Bank has generally been a net inter-bank lender in the market, it regards the ability to obtain funds in the inter-bank market as an important source of liquidity in both normal and crisis situations, and therefore regularly borrows in the inter-bank market as a means of testing the availability of credit lines. The Bank's borrowing capacity, however, is restricted by statutory limits, the Bank's ability to pledge collateral acceptable to prospective lenders, the general liquidity position in the market, the price of such borrowings and the circumstances leading to the Bank's need to borrow rather rely on deposits.

As the Bank considers a stable deposit base as critical to its liquidity position, it conducts statistical and behavioural analyses of its deposit base with the objective of accumulating funding sources which are likely to remain with the Bank on a longer-term basis. The Bank is focused on building its relationships with depositors to achieve this objective.

## ***Interest Rate Risk Management***

Interest rate risk is the risk that arises when the movement of interest rates affects adversely the net interest margin of the Bank and thus its operating results. Net interest margin is defined as the net interest income (total interest income less total interest expenses) expressed as a percentage of total assets or total liabilities plus shareholders' funds. The Bank does not carry interest rate positions on its trading book. Interest rate risk arises primarily from several sources, including the timing differences in the re-pricing of, and the different bases of pricing, interest-bearing assets, liabilities and commitments (otherwise known as re-pricing risk and basis risk, respectively) and positions of non-interest bearing balances and in particular free capital generated by shareholders' funds (otherwise known as structural risk). As a matter of policy, the Bank does not carry financial instruments or offer products to customers that expose the Bank to significant yield curve and option risks. As a result such exposures are insignificant for the Bank. The Bank monitors re-pricing risk by regular sensitivity analyses of the net re-pricing gap of assets and liabilities with reference to their next re-pricing date. Basis risk is monitored by regular sensitivity analysis of the net long/short position of prime/HIBOR/US prime/LIBOR based assets and liabilities with reference to their next re-pricing date. The Bank performs monthly sensitivity and gapping analyses in Hong Kong dollars and other major currencies to which it has significant exposure. The Bank implements certain measures to mitigate its interest rate risk, including but not limited to the avoidance of trading in interest rate derivatives, entry into inter-bank and longer-term debt securities transactions in order to square as much as possible net re-pricing gaps, and adhering to gapping limits.

The Bank measures the exposure of its assets and liabilities to fluctuations in interest rates primarily by way of gap analysis which provides the Bank with a static view of the maturity and re-pricing characteristics of balance sheet positions. An interest rate gap report is prepared by classifying all assets and liabilities into various time period categories according to contracted maturities or anticipated repricing dates whichever is earlier. The difference in the amount of assets and liabilities maturing or being re-priced in any time period category would then give the Bank an indication of the extent to which the Bank is exposed to the risk of potential changes in the net interest income.



The following table sets forth the combined currency asset-liability gap position for the Bank as at 30 June 2010.

	Repayable on demand	Repayable within 1 month (except those repayable on demand)	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
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>At 31 December 2009</b>								
<b>Assets</b>								
Cash and short-term funds .....	4,204,022	10,409,504	235,383	199,771	—	—	—	15,048,680
Placements with banks and other financial institutions.....	—	—	652,017	2,162,549	—	—	—	2,814,566
Derivative financial instruments .....	—	175	119	37	—	—	—	331
Financial assets at fair value through profit or loss .....								
- Held for trading .....	—	—	—	—	—	—	140	140
- Designated at fair value .....	—	—	—	88,276	488,314	—	—	576,590
Available-for-sale securities .....	—	—	—	—	92,272	1,276	179,101	272,649
Held-to-maturity securities .....	—	4,142,804	1,431,063	4,141,778	7,238,821	—	—	16,954,466
Advances to customers...	1,456,020	2,234,769	1,501,287	4,773,751	13,014,912	9,628,458	184,382	32,793,579
Advances to banks and other financial institutions.....	9,958	60,466	30,961	13,298	—	—	—	114,683
Other assets .....	341,785	86,790	22,146	67,812	703	—	910,606	1,429,842
<b>Total assets</b> .....	<u>6,011,785</u>	<u>16,934,508</u>	<u>3,872,976</u>	<u>11,447,272</u>	<u>20,835,022</u>	<u>9,629,734</u>	<u>1,274,229</u>	<u>70,005,526</u>
<b>Liabilities</b>								
Deposits and balances of banks and other financial institutions ..	10,218	1,437,500	—	—	—	—	—	1,447,718
Deposits from customers .....	24,492,361	23,282,401	8,369,759	4,487,837	156,057	—	—	60,788,415
Derivative financial instruments .....	—	296	20	1,373	42,724	—	—	44,413
Loan capital .....	—	—	—	—	—	967,199	—	967,199
Other liabilities .....	462,336	20,846	23,489	48,633	28,155	—	—	583,459
<b>Total liabilities</b> .....	<u>24,964,915</u>	<u>24,741,043</u>	<u>8,393,268</u>	<u>4,537,843</u>	<u>226,936</u>	<u>967,199</u>	<u>—</u>	<u>63,831,204</u>
Net position - total assets and liabilities .....	<u>(18,953,130)</u>	<u>(7,806,535)</u>	<u>(4,520,292)</u>	<u>6,909,429</u>	<u>20,608,086</u>	<u>8,662,535</u>	<u>1,274,229</u>	<u>6,174,322</u>

The following table sets forth, for the period indicated, the impact of changes in Hong Kong dollar and U.S. dollar interest rates on annualised net interest income for the Bank's local operations.

As at 30 June 2010				
Change in interest rates (in basis points)				
	(10)	(5)	50	100
<i>(HK\$ millions, except percentages)</i>				
Change on annualised net interest income .....	(5)	(2)	24	47
As a percentage of the Bank's net interest income for the year 2009 .....	(1)	(0)	3	6

Given the re-pricing position of the assets and liabilities for the Bank's operations as at 30 June 2010, if interest rates decreased by 10 basis points (a basis point being a unit that is equal to one hundredth of 1%), the Bank would expect that annualised net interest income would fall by HK\$5 million, representing less than 1% of the Bank's net interest income for the year ended 31 December 2009. If interest rates increased by 100 basis points, the annualised net interest income would rise by HK\$47 million, representing 6% of the Bank's net interest income for the year ended 31 December 2009. This sensitivity analysis is for risk management purposes and assumes no other changes in the re-pricing structure. Actual changes in net interest income will vary from the model.

The table below sets out the Bank's average balances of interest-earning assets and interest-bearing liabilities, interest and related average interest rates for the years ended 31 December 2007, 2008 and 2009. Average balances of interest-earning assets and interest-bearing liabilities for the years ended 31 December 2007, 2008 and 2009 are based on the arithmetic mean of the respective balances at the beginning and the end of such periods.

	Years ended 31 December								
	2007			2008			2009		
	Average Balance	Interest	Average rate (%)	Average Balance	Interest	Average rate (%)	Average Balance	Interest	Average rate (%)
<i>(HK\$ millions, except percentages)</i>									
<b>ASSETS</b>									
<b>Interest-earning assets:</b>									
<i>Loan and advances</i>									
Bills receivable .....	497			422			319		
Trade bills .....	151			165			142		
Other advances to customers .....	28,650			31,896			32,559		
Advance to banks and other financial institutions .....	57			87			116		
Total .....	29,355	1,613	5.5%	32,570	1,088	3.34%	33,136	682	2.06%
<i>Short term funds and placements</i>									
Cash and short-term funds .....	15,510			16,212			16,354		
Placements with banks and other financial institutions maturing between one to twelve months .....	2,861			4,226			4,091		
Total .....	18,371	979	5.3%	20,438	607	2.97%	20,445	169	0.83%
<i>Securities</i>									
Certificates of deposit .....	1,674			1,021			453		
Other debt securities .....	14,309			12,699			13,590		
Total .....	15,983	719	4.5%	13,720	476	3.47%	14,043	334	2.38%
Total interest-earning assets .....	63,709	3,311	5.2%	66,728	2,171	3.25%	67,624	1,185	1.75%
Impairment allowances .....	(136)			(125)			(124)		
Non-interest earning assets .....	2,466			2,111			1,693		
<b>TOTAL ASSETS</b> .....	<b>66,039</b>			<b>68,714</b>			<b>69,193</b>		
<b>LIABILITIES</b>									
<b>Interest-bearing liabilities:</b>									
<i>Deposits</i>									
Deposits from customers .....	57,501			59,865			60,095		
Deposits and balances of banks and other financial institutions .....	493			991			1,487		
Total .....	57,994	2,276	3.9%	60,856	1,265	2.08%	61,582	342	0.56%
<i>Loan capital</i> .....	969	64	6.6%	968	42	4.35%	966	20	2.04%
Total interest-bearing liabilities .....	58,963	2,340	4.0%	61,824	1,307	2.11%	62,548	362	0.58%
Non interest-bearing liabilities .....	917			777			578		
<b>TOTAL LIABILITIES</b> .....	<b>59,880</b>			<b>62,601</b>			<b>63,126</b>		
<b>NET INTEREST INCOME</b> .....		<b>971</b>			<b>864</b>			<b>823</b>	
<b>NET INTEREST SPREAD</b> .....			<b>1.2%</b>			<b>1.14%</b>			<b>1.17%</b>

*Note:*

- (1) Net interest spread represents the average rate on total interest-earning assets less the average rate on total interest-bearing liabilities.

The table below sets out the Bank's average balances of interest-earning assets and interest-bearing liabilities, interest and related average interest rates for the six months ended 30 June 2009 and 2010. Average balances of interest-earning assets and interest-bearing liabilities for the six months ended 30 June 2009 and 2010 are based on the arithmetic mean of the respective balances at the beginning and the end of such periods.

	Six months ended 30 June					
	2009			2010		
	Average balance	Interest	Average rate (%)	Average balance	Interest	Average rate (%)
<i>(HK\$ millions, except percentages)</i>						
<b>ASSETS</b>						
<b>Interest-earning assets</b>						
<i>Loan and advances</i>						
Bills receivable .....	316			319		
Trade bills .....	145			121		
Other advances to customers .....	32,660			33,733		
Advance to banks and other financial institutions .....	116			314		
Total .....	33,237	350	1.1%	34,487	319	0.9%
<i>Short term funds and placements</i>						
Cash and short-term funds .....	17,727			13,782		
Placements with banks and other financial institutions maturing between one to twelve months .....	4,148			3,261		
Total .....	21,875	119	0.5%	17,043	64	0.4%
<i>Securities</i>						
Certificates of deposit .....	531			528		
Other debt securities .....	11,735			16,802		
Total .....	12,266	139	1.1%	17,330	175	1.0%
Total interest-earning assets .....	67,378	608	0.9%	68,860	558	0.8%
Impairment allowances .....	(118)			(142)		
Non-interest earning assets .....	1,730			1,650		
<b>TOTAL ASSETS</b> .....	<b>68,990</b>			<b>70,368</b>		
<b>LIABILITIES</b>						
<b>Interest-bearing liabilities:</b>						
<i>Deposits</i>						
Deposits from customers .....	59,570			60,652		
Deposits and balances of banks and other financial institutions .....	1,825			1,890		
Total .....	61,395	199	0.3%	62,542	140	0.2%
<i>Loan capital</i> .....	966	12	1.3%	969	6	0.7%
Total interest-bearing liabilities .....	62,361	211	0.3%	63,511	146	0.2%
Non interest-bearing liabilities .....	591			625		
<b>TOTAL LIABILITIES</b> .....	<b>62,952</b>			<b>64,136</b>		
<b>NET INTEREST INCOME</b> .....		<b>397</b>			<b>412</b>	
<b>NET INTEREST SPREAD</b> .....			<b>0.6%</b>			<b>0.6%</b>

*Note:*

- (1) Net interest spread represents the average rate on total interest-earning assets less the average rate on total interest-bearing liabilities.

## **Internal Auditing**

The Internal Audit Department has responsibility for auditing the Bank's operations. Through regular audits of all of the departments, subsidiaries and branches of the Bank, the Internal Audit Department reviews and evaluates the adequacy and effectiveness of internal controls, safeguards the Bank's assets, reviews operations in terms of efficiency and effectiveness, assesses the reliability and integrity of financial and other operating matters and reviews compliance with established policies, procedures and relevant statutory requirements. The results of an internal audit are reported to senior management, the Audit Committee and the head of the relevant audited department, subsidiary or branch, and any internal audit recommendations are generally expected to be implemented shortly after the issuance of the internal audit report. Significant findings arising from internal audits are summarised semi-annually for reporting to the Audit Committee. The significant findings are also shared with the HKMA and Deloitte Touche Tohmatsu, the Bank's external auditor, on a regular basis.

## MANAGEMENT

The Bank is managed by its Board of Directors, which is responsible for the direction and management of the Bank. The Articles of Association of the Bank require that there be not less than seven Directors, unless and until otherwise determined by an ordinary resolution of the shareholders of the Bank. Directors are appointed either by the shareholders at a general meeting of shareholders or by the Board of Directors at any time.

### Board of Directors

The Board of Directors of the Bank is comprised of the following individuals:

Name	Age	Title
Dr. LIU Lit Mo	72	Executive Director and Chairman
Mr. LIU Lit Chi	71	Managing Director and Chief Executive Officer
Mr. Don Tit Shing LIU	48	Executive Director and Deputy Chief Executive Officer
Mr. LAU Wai Man	52	Executive Director and Deputy Chief Executive Officer
Mr. Wilfred Chun Ning LIU	49	Executive Director
Mr. TSANG Chiu Wing	53	Executive Director
Mr. WONG Har Kar	57	Executive Director
Mr. Timothy George FRESHWATER	66	Non-executive Director
Mr. WANG Xiaoming	55	Non-executive Director
Mr. Andrew LIU	54	Non-executive Director
Mr. Hidemitsu OTSUKA	52	Non-executive Director
Mr. Christopher Kwun Shing LIU	35	Non-executive Director
Mr. Alfred Cheuk Yu CHOW	59	Non-executive Director
Mr. MENG Qinghui	54	Non-executive Director
Dr. Robin Yau Hing CHAN	77	Independent Non-executive Director
Mr. Wanchai CHIRANAKHORN	71	Independent Non-executive Director
Mr. CHENG Yuk Wo	49	Independent Non-executive Director
Mr. Andrew Chiu Cheung MA	68	Independent Non-executive Director

**Dr. LIU Lit Mo, LLD, MBE, JP, *Executive Director and Chairman***

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

**Mr. LIU Lit Chi, *Managing Director and Chief Executive Officer***

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

**Mr. Don Tit Shing LIU, *Executive Director and Deputy Chief Executive Officer***

Mr. Liu graduated from Oxford University and is an associate member of the Institute of Chartered Accountants in England & Wales and a fellow of the Hong Kong Institute of Certified Public Accountants. Mr. Liu joined the Bank in 1992.

**Mr. LAU Wai Man, *Executive Director and Deputy Chief Executive Officer***

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

**Mr. Wilfred Chun Ning LIU, *Executive Director***

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

**Mr. TSANG Chiu Wing, *Executive Director***

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



**Mr. WONG Har Kar, *Executive Director***

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

**Mr. Timothy George FRESHWATER, *Non-executive Director***

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

**Mr. WANG Xiaoming, *Non-executive Director***

Mr. Wang has been a member of the Board since March 2008. He has been the Executive Director of the Board of COSCO International Holdings Limited since January 2006. Mr. Wang is also a Director of COSCO (Hong Kong) Group Limited and the Chief Financial Officer of COSCO (H.K.) Shipping Co., Limited. Mr. Wang graduated from Shanghai Maritime University, the PRC, majoring in accounting and has the senior accountant qualification awarded by Ministry of Communications of the PRC. Mr. Wang had been the Deputy Manager of the Audit Department of China Ocean Shipping (Group) Company, Finance Manager of COSCO Bulk Carrier Co. Limited, Deputy General Manager of Finance Division of China Ocean Shipping (Group) Company and General Manager of COSCO Finance Co. Limited. He has extensive experience in corporate financial management.

**Mr. Andrew LIU, *Non-executive Director***

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

**Mr. Hidemitsu OTSUKA, *Non-executive Director***

Mr. Otsuka is Executive Officer, Regional Head for Hong Kong and General Manager of The Bank of Tokyo-Mitsubishi UFJ, Ltd, Hong Kong Branch. He joined The Bank of Tokyo, Ltd (currently The Bank of Tokyo-Mitsubishi UFJ, Ltd) in 1982 and has more than 28 years of experience in banking. Mr. Otsuka’s experience lies in corporate banking, treasury and global banking activities. During this period, Mr. Otsuka was appointed to work in Corporate Banking Division 2 in Tokyo, Japan and Singapore Branch as Deputy General Manager. Mr. Otsuka has been an Executive Officer since June 2009, and served as the General Manager of International Credit Division before he was appointed as the current position at The Bank of Tokyo-Mitsubishi UFJ, Ltd on 1 July 2010. Mr. Otsuka graduated from Keio University in 1982 with a Bachelor’s degree in Economics.

**Mr. Christopher Kwun Shing LIU, *Non-executive Director***

Mr. Liu became a Director of the Bank in 2002 after having served as Alternate Director to Dr. Liu Lit Chung (a former Director of the Bank) between July 2000 and July 2002. Mr. Liu is an Executive Director of Liu Chong Hing Investment Limited (the Bank's controlling shareholder), a post which he has held since August 2008 following a re-designation from his previous role since 2000 as Non-executive Director of the company and Alternate Director to Dr. Liu Lit Chung (who is a Non-executive Director of the company). A holder of a Master of Arts degree in Jurisprudence from the University of Oxford, Mr. Liu is a qualified solicitor in both England & Wales and Hong Kong. Prior to his joining Liu Chong Hing Investment Limited on a full-time basis, he was a partner of Deacons in Hong Kong focusing on corporate finance, mergers and acquisitions and private equity matters, and currently remains as an Advisory Legal Counsel of the international law firm.

**Mr. Alfred Cheuk Yu CHOW, *BBS, JP, Non-executive Director***

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

**Mr. MENG Qinghui, *Non-executive Director***

Mr. Meng has been a member of the Board since March 2008. Mr. Meng was redesignated from Executive Director to Non-executive Director of COSCO International Holdings Limited on 7 July 2008. He is also the Managing Director of Finance Division of COSCO (Hong Kong) Group Limited and the Non-executive Director of Soundwill Holdings Limited. Mr. Meng graduated from Central South University and has the PRC accountant qualification. He has extensive experience in corporate financial management and accounting and is also familiar with corporate financial planning.

**Dr. Robin Yau Hing CHAN, *GBS, LLD, JP, Independent Non-executive Director***

Dr. Chan has been a member of the Board since October 1981, was redesignated from Non-executive Director to Independent Non-executive Director of the Bank in April 2005. Dr. Chan is the Ex-officio Life Honorary Chairman of The Chinese General Chamber of Commerce, Hong Kong and the Vice Chairman of All-China Federation of Returned Overseas Chinese. Dr. Chan had been a Deputy to the National People's Congress of the People's Republic of China from March 1988 to February 2008. Dr. Chan, the Chairman of Asia Financial Holdings Limited, also serves as an Independent Non-executive Director of K. Wah International Holdings Limited and Keck Seng Investments (Hong Kong) Limited respectively. All these companies are listed on the HKSE.

**Mr. Wanchai CHIRANAKHORN, *Independent Non-executive Director***

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

**Mr. CHENG Yuk Wo, *Independent Non-executive Director***

Mr. Cheng has been an Independent Non-executive Director of the Bank since September 2004. Mr. Cheng is also a member of the Bank's Audit Committee and Remuneration Committee. Mr. Cheng, a co-founder of a Hong Kong merchant banking firm, is currently the proprietor of a certified public accountant practice in Hong Kong. Mr. Cheng obtained a Master of Science (Economics) degree in Accounting and Finance from the London School of Economics, England and a Bachelor of Arts (Honours) degree in Accounting from the University of Kent, England. He is a fellow of the Institute of Chartered Accountants in England & Wales and the Hong Kong Institute of Certified Public Accountants, and a member of the Institute of Chartered Accountants of Ontario, Canada. Mr. Cheng has more than 20 years of expertise in financial and corporate advisory services in mergers, acquisitions and investments. He had worked at Coopers and Lybrand (now known as PricewaterhouseCoopers) in London and Swiss Bank Corporation (now known as UBS AG) in Toronto, and held senior management positions in a number of Hong Kong listed companies. Mr. Cheng also serves as a Director for certain other listed companies, including CPMC Holdings Limited (a public company listed on the HKSE since 16 November 2009) in which he has been an Independent Non-executive Director since 23 June 2008.

**Mr. Andrew Chiu Cheung MA, *Independent Non-executive Director***

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

**Organisation**

The Board of Directors of the Bank is responsible for the overall management of the Bank and its subsidiaries. To assist the Board of Directors in managing the Bank, a number of committees have been established, including the Audit Committee and the Remuneration Committee. The Audit Committee comprises two Independent Non-executive Directors and one Non-executive Director and is required, amongst other things, to oversee the relationship with the external auditors, to advise the Board of Directors on the appointment and retention of the external auditors, to review the external auditors' independence and objectivity, to review the half-yearly and annual reports and accounts, to review the external auditors' management letter, to hold meetings with the HKMA, to assess the adequacy and effectiveness of the Bank's systems of internal control, to review the internal audit function, and to review and recommend internal procedures to ensure compliance with regulatory requirements and generally accepted accounting standards. The Remuneration Committee comprises two Independent Non-executive Directors and one Non-executive Director and reviews and makes recommendations to the Board of Directors on the remuneration policy applicable to Directors and senior management of the Bank, and ensures that the Bank is able to attract, retain, and motivate a high-calibre team of senior executives which is essential to the success of the Bank.

In addition to the Audit Committee and the Remuneration Committee, the Bank has a number of other committees which assist management in the operation of the Bank. These include:

- the Executive Committee, which comprises all the Executive Directors and is responsible for steering the Bank's policy and operational decisions on a day-to-day basis and attending to matters that require the review and supervision of the Board of Directors between regular board meetings;
- the Executive Management Committee, comprising the Managing Director and Chief Executive Officer, certain other Executive Directors and division heads, which is responsible for formulating operation and management policies, discussing significant daily operational issues, reviewing key business performance and discussing business opportunities arising from changing market and competitive conditions;
- the Executive Loans Committee which comprises all the Executive Directors and serves to guide and review the operations of, and to delegate proper authorities as it deems appropriate from time to time to, the Loans Committee, as well as approving large and certain specific new loan applications and applications for renewal and amendment of existing loans, having due regard to the Bank's Lending Policy and the relevant laws and regulations;
- the Loans Committee, which is responsible for ensuring that the Bank's Lending Policy is adequate, issuing guidelines from time to time to guide lending activities of the Bank, directing the Credit Control Department to monitor loans portfolio quality and taking timely corrective actions such as implementing debt-restructuring schemes and maintaining adequate provisions for loan losses, meeting regularly to evaluate loan applications and make credit decisions, monitoring of compliance with statutory lending limits, assessing and approving new loan products and attending to instructions of the Executive Loans Committee;
- the Asset and Liability Management Committee, which comprises senior staff members representing major businesses of the Bank and is responsible for facilitating the oversight of the Board of Directors in the management of the assets and liabilities of the Bank from the perspective of containing the pertinent liquidity, interest rate, foreign exchange and other market risks, as well as assessing the impact of the current economic and business climate on the Bank's balance sheet, formulating the corresponding strategies and plans and evaluating non-credit related products;
- the Risk Management and Compliance Committee, which comprises senior staff members who are responsible for risk management, compliance issues and operations of the Bank and is responsible for facilitating the oversight of the Board of Directors concerning risk management and compliance issues of the Bank. It discharges its responsibilities by identifying and analysing major risk management and compliance issues, and by approving and overseeing the implementation of the risk management and compliance policies and procedures. It is also responsible for coordinating and monitoring the implementation of the recommendations made by the regulators. Regular reports as prepared by this committee are submitted to the Board;

- the Information Technology Committee, which comprises senior staff members including the Executive Director in charge of the Information Technology Division and formulates the information technology strategic plan and policy in concurrence with the development of banking business, reviews and approves annual budget proposals of information technology services, appraises the viability and worthiness of Information Technology projects to be undertaken and recommends priorities and funding for projects, promotes and facilitates uniformity in the development of information systems and exchanges of data through use of standards, and facilitates the use of information technology in ways that minimise fraud, enhance security and protect privacy; and
- the Human Resources Committee, which comprises senior staff members of the Bank and formulates human resources policies that cover areas including recruitment and retention, selection and assessment, managing diversity, equal opportunities, grading and succession planning, pay, pensions, performance management and incentives, job rotation, staff training and personal development, management development and employee relationship. It also plans, monitors, evaluates and reviews all matters relating to staff training.

## MATERIAL RELATED PARTY TRANSACTIONS

The Bank has, from time to time, entered into a number of transactions with its related parties, including its jointly controlled entities, substantial shareholders, and directors and their family members and companies controlled or significantly influenced by them. The transactions include, among others, lending, accepting deposits from and extending credit facilities to them, participating in loan syndicates, providing cheque clearing services, stockbroking and nominee services, remittances and foreign exchange services to them, accepting property consultancy and property management services from them, and leasing office premises from them. Such transactions have included transactions with the members of the Liu family or companies controlled or significantly influenced by them, including but not limited to Liu Chong Hing Investment Limited.

The Bank conducts all transactions with its related parties on an arm's length basis and believes that such transactions have been generally as favourable to it as similar transactions with unrelated third parties would have been. The Bank has four directors who are independent directors in accordance with the criteria set out in the Listing Rules and maintains internal policies and procedures to prevent possible conflicts of interest. As a matter of internal policy, the relevant related party as well as all other parties interested in any proposed related party transaction are not allowed to participate in the decision-making process relating to such transaction. The Bank is also subject to, and must comply with, the Listing Rules which govern "connected transactions" (as defined in the Listing Rules) as well as the requirements of the HKMA. As at the date of this Offering Circular, the Bank has been and is in full compliance with all HKMA requirements, including but not limited to Sections 81 and 83 of the Hong Kong Banking Ordinance, and all requirements and regulations of the HKSE and all other relevant regulatory bodies.

The HKSE has issued waiver letter dated 17 June 1994 to the Bank, which states that the Bank will not be required to comply with certain requirements set out in Chapter 14 of the Listing Rules in respect of certain banking transactions between the Bank and Liu Chong Hing Investment Limited and The Bank of Tokyo-Mitsubishi UFJ, Ltd (each a substantial shareholder of the Bank) and their respective subsidiaries, subject to, among others, the condition that an auditor's letter, stating that such transactions have been approved by the Bank's Board of Directors and that they have been entered into based on normal commercial terms, must be submitted by the Bank to the HKSE on an annual basis. As at 31 December 2009 and 30 June 2010, the interest income derived from related party transactions represented 1.05% and 0.47% of the Bank's gross interest income respectively.

In addition, with respect to loan transactions, the Hong Kong Banking Ordinance stipulates, among others, that exposure to any one person or group of companies must be limited to 25.0% of the Bank's capital base and that no unsecured loans above the amount of HK\$1 million may be provided to a related party (being an individual). As at 31 December 2009 and 30 June 2010, related party lending represented 2.90% and 1.80% of the Bank's total assets (as based on total assets, excluding cash and short-term funds, placements with banks and other financial institutions maturing between one and twelve months, interests in jointly controlled entities, property and equipment and prepaid lease payments for land) respectively.

A summary of significant transactions entered into by the Bank with its related parties for the years ended 31 December 2007, 2008, 2009 and the six months ended 30 June 2010 is set out below.

In accordance with a conditional sale and purchase agreement dated 3 March 2005 between the Bank and Liu Chong Hing Investment Limited, the Bank acquired Chong Hing Insurance Company Limited (formerly known as "Liu Chong Hing Insurance Company Limited") from Liu Chong Hing Investment Limited for a total cash consideration of HK\$212 million. The purpose of the transaction was to improve the operation efficiency of both the Bank and Liu Chong Hing Investment Limited. The transaction is entered into under normal commercial terms and priced based on relevant market rates at the time of the transaction and is under the same terms as those available to unrelated third parties.

In accordance with a sale and purchase agreement dated 16 March 2006 between the Bank and Bonsun Enterprises Limited, a wholly-owned subsidiary of Liu Chong Hing Investment Limited, the Bank acquired a property in Hong Kong from Bonsun Enterprises Limited for a total cash consideration of approximately HK\$13.8 million. The purpose of the transaction was to obtain additional warehousing space for the Bank. The transaction is entered into under normal commercial terms and priced based on relevant market rates at the time of the transaction and is under the same terms as those available to unrelated third parties.

As at 30 June 2010, all interest rates in connection with the deposits taken and credit facilities extended are under terms and conditions normally applicable to customers of comparable standing. The interest received from and interest paid to the Bank's related parties for the years ended 31 December 2007, 2008, 2009 and the six months ended 30 June 2010, and the outstanding balances of amounts due from and due to them as at 31 December 2007, 2008, 2009 and 30 June 2010, are set out in the table below as a percentage of the Bank's consolidated interest income, interest expense, total assets and total deposits, respectively:

	As at 31 December			As at 30 June
	2007	2008	2009	2010
Interest income .....	0.73%	1.20%	1.05%	0.47%
Interest expense .....	1.78%	1.57%	1.77%	1.55%
Amount due from related parties <sup>(1)(2)</sup> .....	1.98%	3.95%	2.90%	1.80%
Amount due to related parties <sup>(2)(3)</sup> .....	1.75%	1.54%	1.13%	1.41%

*Notes:*

- (1) Based on total assets (excluding cash and short-term funds, placements with banks and other financial institutions maturing between one and twelve months, interests in jointly controlled entities, property and equipment and prepaid lease payments for land).
- (2) Related parties include, without limitation, members of the Liu family.
- (3) Based on deposits from customers.



## PRINCIPAL SHAREHOLDERS AND DIRECTORS' INTERESTS

### Registered Shareholders

As at 30 June 2010, the following corporations were holding 5.0% or more of the issued shares of the Bank according to its Register of Members:

Name of Shareholder	Number of shares held	Percentage of shares
Liu Chong Hing Estate Company, Limited .....	211,040,628 <sup>(1)(3)</sup>	48.52
Bauhinia 97 Limited .....	87,000,000 <sup>(2)</sup>	20.00
The Bank of Tokyo-Mitsubishi UFJ, Ltd .....	42,000,000 <sup>(3)</sup>	9.66

### Interests of Substantial Shareholders and Other Persons

As at 30 June 2010, the following interests and short positions of Substantial Shareholders and Other Persons of the Bank in the shares and underlying shares of the Bank were recorded in the Register required to be kept by the Bank under section 336 of the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong) (the "SFO"):

Name of Shareholder	Number of shares held	Percentage of shares
Liu Chong Hing Investment Limited .....	211,040,628 <sup>(1)(3)</sup>	48.52
Liu's Holdings Limited .....	211,040,628 <sup>(1)(3)</sup>	48.52
COSCO (Hong Kong) Group Limited.....	87,000,000 <sup>(2)</sup>	20.00
China Ocean Shipping (Group) Company .....	87,000,000 <sup>(2)</sup>	20.00
Mitsubishi UFJ Financial Group, Inc .....	42,000,000 <sup>(3)</sup>	9.66

#### Notes:

- (1) Liu Chong Hing Estate Company, Limited is a wholly-owned subsidiary of Liu Chong Hing Investment Limited, a public company listed on the HKSE. Liu's Holdings Limited, a private company, had interest in about 45% of Liu Chong Hing Investment Limited's issued and fully-paid share capital. The references to the 211,040,628 shares in question all relate to the same block of 211,040,628 shares held by Liu Chong Hing Estate Company, Limited.
- (2) Bauhinia 97 Limited is a wholly-owned subsidiary of COSCO (Hong Kong) Group Limited, which in turn is a wholly-owned subsidiary of China Ocean Shipping (Group) Company. The references to the 87,000,000 shares in question all relate to the same block of 87,000,000 shares registered in the name of Bauhinia 97 Limited.
- (3) The Bank of Tokyo-Mitsubishi UFJ, Ltd is a wholly-owned subsidiary of Mitsubishi UFJ Financial Group, Inc. The references to the 42,000,000 shares in question both relate to the same block of 42,000,000 shares registered in the name of The Bank of Tokyo-Mitsubishi UFJ, Ltd.

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

Save as disclosed above, no other interest or short position in the shares or underlying shares of the Bank were recorded in the Register.

### Interests of Directors (Including the Chief Executive Officer) in the Securities of the Bank and Associated Corporations

As at 30 June 2010, the following interests and short positions of the Directors (including the Chief Executive Officer) of the Bank in the shares and underlying shares of the Bank and its associated corporations were recorded in the Register required to be kept under section 352 of the SFO:

Name of Director	Personal interests	Corporate interests	Total interests
Dr. LIU Lit Mo .....	1,009,650	251,040,628 <sup>(1)</sup>	252,050,278
Mr. LIU Lit Chi .....	313,248	253,303,839 <sup>(1)(2)</sup>	253,617,087
Mr. Don Tit Shing LIU .....	15,000	—	15,000
Dr. Robin Yau Hing CHAN .....	48,400	1,018,000 <sup>(3)</sup>	1,066,400
Mr. Timothy George FRESHWATER .....	396	—	396
Mr. Andrew LIU .....	177,000	—	177,000

Notes:

(1) 251,040,628 shares in the Bank are attributed as follows:

- (i) 211,040,628 shares held by public listed Liu Chong Hing Investment Limited's wholly-owned subsidiary, Liu Chong Hing Estate Company, Limited, in which each of Messrs Liu Lit Mo and Liu Lit Chi is deemed under the SFO to be interested through Liu's Holdings Limited, a private company holding approximately 45% of Liu Chong Hing Investment Limited's issued and fully-paid share capital; and
- (ii) 40,000,000 shares held by The Bank of Tokyo-Mitsubishi UFJ, Ltd. Pursuant to an agreement entered into in 1994, The Bank of Tokyo-Mitsubishi UFJ, Ltd has granted an option to Liu Chong Hing Estate Company, Limited exercisable at any time during the term of that agreement to purchase all such shares and The Bank of Tokyo-Mitsubishi UFJ, Ltd is required to offer to sell all such shares to Liu Chong Hing Estate Company, Limited in certain circumstances. By virtue of the interests of Messrs Liu Lit Mo and Liu Lit Chi in Liu Chong Hing Estate Company, Limited through Liu's Holdings Limited, each of them is deemed under the SFO to be interested in such shares.

(2) 2,263,211 shares in the Bank are held by Alba Holdings Limited, shareholders of which include Mr. Liu Lit Chi and his associates. Accordingly, Mr. Liu Lit Chi is deemed under the SFO to be interested in such shares.

- (3) 1,018,000 shares in the Bank are held collectively by Asia Panich Investment Company (Hong Kong) Limited and United Asia Company Limited. These corporations or their directors are accustomed to acting in accordance with Dr. Robin Yau Hing Chan's directions or instructions.

As a result of the attribution of aggregate corporate interests in shares of the Bank as described above, the Directors and the Chief Executive Officer of the Bank were attributed with the following interests in the shares of the Bank (equal to the sum of the relevant individual's personal interest, if any, and the attributable aggregate corporate interest), as a percentage of the Bank's total issued share capital, as of 30 June 2010:

<b>Name of Director</b>	<b>Percentage of Issued Share Capital</b>
Dr. LIU Lit Mo .....	57.94
Mr. LIU Lit Chi .....	58.30
Mr. Don Tit Shing LIU .....	less than 0.01
Dr. Robin Yau Hing CHAN .....	0.25
Mr. Timothy George FRESHWATER .....	less than 0.01
Mr. Andrew LIU .....	0.04

Save as disclosed above, no other interest or short positions in the shares or underlying shares of the Bank or any of its associated corporations were recorded in the Register.

# THE BANKING INDUSTRY IN HONG KONG

*Unless otherwise expressly stated, the information and statistics set out in this section are derived directly from publicly available information, including materials obtained from the HKMA or published in The Hong Kong Monthly Statistical Bulletin in relation to information as at 30 June 2010, which is in turn based on returns submitted to the HKMA by reporting authorised institutions. The Bank has not independently verified or checked such information and statistics and does not assume any responsibility for the accuracy or completeness thereof. Reporting authorised institutions as at 30 June 2010 comprised of all the licensed banks, restricted licence banks and deposit-taking companies in Hong Kong. References to assets, liabilities, loans, advances, deposits and negotiable certificates of deposit of banks or authorised institutions relate to assets, liabilities, loans, advances, deposits and negotiable certificates of deposit of only reporting licensed banks or other reporting authorised institutions.*

## Introduction

The banking industry in Hong Kong has a three-tier system of authorised institutions, comprising licensed banks, restricted licence banks and deposit-taking companies. As at 31 December 2009, there were 145 licensed banks, 26 restricted licence banks and 28 deposit-taking companies operating in Hong Kong; 23 of the licensed banks were incorporated in Hong Kong (including the Bank), with the balance of 122 incorporated overseas. Furthermore, there were 71 representative offices of overseas banks.

Primary supervision of Hong Kong incorporated authorised institutions is the responsibility of the HKMA, whereas overseas incorporated banks are subject both to the HKMA and home country supervision. The HKMA obtains regular returns from and sends examination teams to all authorised institutions. Off-site reviews, on-site examinations and prudential meetings are the methods usually adopted for the supervision of authorised institutions. Prudential meetings can also take the form of tripartite meetings between the management of an authorised institution, its auditors and the HKMA. In addition, all licensed banks in Hong Kong, whether incorporated overseas or locally, are required to be members of the Hong Kong Association of Banks, a statutory body, the purposes of which include representing the banking industry in banking-related matters and framing rules for the conduct of banking business in Hong Kong.

Since 31 December 1989, locally incorporated banks have been subject to capital adequacy standards similar to those set out in the Basel Accord, with a minimum risk capital adequacy ratio of 8%. In January 2007, the HKMA implemented and adopted the Basel II Accord capital adequacy standards in Hong Kong. The new standards require banks to disclose key pieces of information on capital, risk exposures, risk assessment processes and hence capital adequacy. The aim of the new standards is to encourage banks to demonstrate to the market participants that their risk management systems are robust and that all relevant risks have been identified and controlled. As at 30 June 2010, the Bank's capital adequacy ratio was 15.24%. A summary of banking regulation in Hong Kong is set out in "Regulation and Supervision".

## Recent Trends

### *Assets*

The total assets of all authorised institutions in Hong Kong decreased approximately 1.0% from HK\$10,754 billion as of 31 December 2008 to HK\$10,646 billion as of 30 September 2009.

### *Loans and Advances*

As of 31 July 2010, loans and advances to customers represented approximately 34.4% of the total assets of all authorised institutions in Hong Kong. The total Hong Kong dollar value of loans and advances to customers extended by all authorised institutions in Hong Kong has decreased

approximately 0.3% from HK\$3,286 billion as of 31 December 2008 to HK\$3,288 billion as of 31 December 2009. Approximately 68.59% of loans and advances to customers extended by all authorised institutions in Hong Kong were denominated in Hong Kong dollars as of 31 July 2010, with the rest in foreign currencies. At the same date, of the total loans and advances to customers of HK\$3,844 billion extended by all authorised institutions, approximately 82.2% was classified as “Loans and Advances for use in Hong Kong plus trade finance” and approximately 17.8% was extended for use outside Hong Kong or where the place of use was not known. As of 31 July 2010, 77.1% of loans originated in Hong Kong, 17.8% from outside Hong Kong and the remaining 5.1% comprised trade finance. Loan growth has been consistently driven by demand from corporates as well as mortgages, as demonstrated by its steady growth of 8.1% compound annual growth rate (“CAGR”) from 2003 to the first half of 2009. The table below illustrates the breakdown of loans classified as “Loans and Advances for use in Hong Kong” by economic sector extended by all authorised institutions in Hong Kong as at 30 September 2009.

<b>Sector</b>	<b>Percentage of Total</b>
Professional and Private Individuals.....	35.50
Building, Construction, Property Development and Investment .....	26.20
Financial Concerns .....	8.90
Transport and Transport Equipment .....	5.90
Wholesale and Retail Trade .....	6.00
Manufacturing .....	5.50
Electricity and Gas .....	1.20
Information Technology .....	1.30
Others.....	9.50
Total.....	<u>100.00</u>

### ***Other Assets***

The other assets of authorised institutions in Hong Kong comprise predominantly interbank lending to both authorised institutions in Hong Kong and to banks overseas, as well as negotiable debt instruments, investments in shareholding and fixed assets. As at 30 September 2009, interbank lending represented approximately 35% of the total assets of all authorised institutions in Hong Kong, with approximately 30% of such lending being to banks outside Hong Kong.

### **Funding**

As of 30 September 2009, deposits from customers representing approximately 60.3% of the total liabilities of all authorised institutions in Hong Kong. Total deposits from customers of all authorised institutions increased approximately 6.0% from HK\$6,060 billion as of 31 December 2008 to HK\$6,424 billion as of 30 September, 2009, of which approximately 52.8% of total customer deposits with authorised institutions were denominated in Hong Kong dollars. Hong Kong dollar deposits increased approximately 12% while deposits denominated in foreign currencies increased approximately 0.2%, in each case from 31 December 2008 to 30 September 2009. As of 30 September 2009, deposits from customers with licensed banks represented approximately 99.6% of deposits from customers with all authorised institutions in Hong Kong. As of 30 September 2009, time deposit accounts, savings accounts and demand accounts accounted for approximately 9%, 40.8% and 11.2%, respectively, of total deposits by customers with licensed banks in Hong Kong. As of 30 September 2009, there were 44 authorised institutions engaged in RMB banking business, which includes RMB deposit taking, currency exchange, remittances and cross-border trade settlement. RMB deposits was RMB 58,174 million during the same time, which comprised 69.7% from demand and savings deposits and 30.3% from time deposits.

### ***Interbank Funds***

Interbank transactions are significant in funding the Hong Kong banking system. As at 30 September 2009, interbank liabilities represented 25% of the total liabilities of all authorised institutions in Hong Kong. A portion of the interbank funding for the Hong Kong banking system is sourced from banks outside Hong Kong and, as at 30 September 2009, 20% of all interbank funding came from banks outside Hong Kong.

### ***Negotiable Certificates of Deposit***

Some banks have adopted the practice of issuing medium term negotiable certificates of deposit. As at 31 October 2009, the total outstanding value of negotiable certificates of deposit issued by authorised institutions in Hong Kong amounted to HK\$91,427 million, of which 74.3% was denominated in Hong Kong dollars.

### **Deposit Protection Scheme**

On 14 October 2008, the Hong Kong Government announced the use of the Exchange Fund to guarantee repayment of all eligible customer deposits held with all authorised institutions in Hong Kong subject to the rules laid down in such Deposit Protection Scheme Ordinance (Cap.581 of the Laws of Hong Kong). The guarantee took immediate effect and is scheduled to remain in force until the end of 2010, whereupon the revised protection limit of HK\$500,000 of each eligible customer deposit held with a licensed bank (as opposed to with any authorised institution) will apply.

## REGULATION AND SUPERVISION

The banking business in Hong Kong principally is regulated by and subject to the provisions of the Hong Kong Banking Ordinance and to the powers and functions ascribed by the Hong Kong Banking Ordinance to the HKMA. The Hong Kong Banking Ordinance provides that only banks which have been granted a banking licence (“**licence**”) by the HKMA (“**licensed banks**”) may carry on banking business (as defined in the Hong Kong Banking Ordinance) in Hong Kong, and contains controls and restrictions on such banks. The HKMA regulates the Bank and may examine its subsidiaries.

### Supervision of Licensed Banks in Hong Kong

The provisions of the Hong Kong Banking Ordinance are implemented by the HKMA, the principal function of which is to promote the general stability and effectiveness of the banking system, especially in the area of supervising compliance with the provisions of the Hong Kong Banking Ordinance. The HKMA supervises licensed banks through, inter alia, a regular information gathering process, the main features of which are as follows:

- (1) each licensed bank must submit a monthly return to the HKMA setting out the assets and liabilities of its operations in Hong Kong and a further comprehensive quarterly return relating to its principal place of business in Hong Kong and all local branches, although the HKMA has the right to allow returns to be made at less frequent intervals;
- (2) the HKMA may order a licensed bank, any of its subsidiaries, its holding company or any subsidiaries of its holding company to provide such further information (either specifically or periodically) as it may reasonably require for the exercise of its functions under the Hong Kong Banking Ordinance or as it may consider necessary to be submitted in the interests of the depositors or potential depositors of the licensed bank concerned. Such information shall be submitted within such period and in such manner as the HKMA may require. The HKMA may in certain circumstances also require such information or any return submitted to it to be accompanied by a certificate or report of the licensed bank’s auditors (approved by the HKMA for the purpose of preparing the report) confirming compliance with the main provisions of the Hong Kong Banking Ordinance and certain other matters;
- (3) licensed banks may be required to provide information to the HKMA regarding companies in which they have a 20% or more direct or indirect shareholding or with which they have common directors or managers (as defined in the Hong Kong Banking Ordinance), the same controller, a common name or a concert party arrangement to promote the licensed bank’s business;
- (4) in addition, licensed banks are obliged to report to the HKMA immediately of their likelihood to become unable to meet their obligations and, in the case of licensed banks incorporated in Hong Kong, of the commencement of material civil proceedings;
- (5) the HKMA may direct a licensed bank to appoint an auditor to report to the HKMA on the state of affairs and/or profit and loss of the licensed bank or the adequacy of the systems of control of the licensed bank or other matters as the HKMA may reasonably require;
- (6) the HKMA may, at any time, with or without prior notice, examine the books, accounts and transactions of any licensed bank, and in the case of a licensed bank incorporated in Hong Kong, any local branch, overseas branch, overseas representative office or subsidiary, whether local or overseas, of such institution; such inspections are carried out by the HKMA on a regular basis; and



- (7) licensed banks are required to give written notice to the HKMA immediately of any proposal to remove an auditor before the expiration of his term of office or replace an auditor at the expiration of his term of office.

### **Exercise of Powers Over Licensed Banks**

The HKMA may exercise certain powers over the conduct of licensed banks in any of the following circumstances:

- (1) when a licensed bank informs the HKMA that it is likely to become unable to meet its obligations, that it is insolvent, or that it is about to suspend payment;
- (2) when a licensed bank becomes unable to meet its obligations or suspends payment;
- (3) if after an examination or an investigation, the HKMA is of the opinion that a licensed bank:
  - (i) is carrying on its business in a manner detrimental to the interests of its depositors or potential depositors or of its creditors or of holders or potential holders of multi-purpose cards issued by it or the issue of which is facilitated by it;
  - (ii) is insolvent or is likely to become unable to meet its obligations or is about to suspend payment;
  - (iii) has contravened or failed to comply with any of the provisions of the Hong Kong Banking Ordinance; or
  - (iv) has contravened or failed to comply with any condition attached to its licence or certain conditions in the Hong Kong Banking Ordinance; and
- (4) where the Financial Secretary advises the HKMA that he considers it in the public interest to do so.

In any of the circumstances described above, the HKMA, after consultation with the Financial Secretary, may exercise any of the following powers:

- (1) to require the licensed bank, by notice in writing served on it, forthwith to take any action or to do an act or thing whatsoever in relation to its affairs, business and property as the HKMA may consider necessary;
- (2) to direct the licensed bank to seek advice on the management of its affairs, business and property from an Advisor appointed by the HKMA;
- (3) to assume control of and carry on the business of the licensed bank, or direct some other person to assume control of and carry on the business of the licensed bank; or
- (4) to report the circumstances to the Chief Executive in Council in certain circumstances (in which case the Chief Executive in Council may exercise a number of powers including directing the Financial Secretary to present a petition to the Court of First Instance for the winding up of the licensed bank).

## **Revocation and Suspension of Banking Licence**

The HKMA also has powers to recommend the revocation or suspension of a licence. Both powers are exercisable after consultation with the Financial Secretary and with a right of appeal of the licensed bank concerned except in the event of temporary suspension in urgent cases. The grounds for suspension or revocation include the following:

- (1) the licensed bank no longer fulfils the criteria for authorisation and the requirements for registration;
- (2) the licensed bank is likely to be unable to meet its obligations or to suspend payment or proposes to make, or has made, any arrangement with its creditors or is insolvent;
- (3) the licensed bank has failed to provide material information required under the Hong Kong Banking Ordinance or has provided false information;
- (4) the licensed bank has breached a condition attached to its licence;
- (5) a person has become or continues to be a controller or chief executive or director after the HKMA has made an objection;
- (6) the interests of the depositors require that the licence be revoked; or
- (7) the licensed bank is engaging in practices likely to prejudice Hong Kong as an international financial centre or in practices (specified in the HKMA guidelines) which should not be engaged in.

Revocation or suspension of a licence means that the licensed bank can no longer conduct banking business (for the specified period in the case of a suspension).

## **Principal Obligations of Licensed Banks**

The obligations of a licensed bank under the Hong Kong Banking Ordinance, which are enforced by the HKMA through the system described above, include, but are not limited to, the following:

### ***Capital Adequacy***

A licensed bank incorporated in Hong Kong must at all times maintain a capital adequacy ratio of at least 8.0%, calculated as the ratio (expressed as a percentage) of its capital base to its risk-weighted exposure as more fully described below. In relation to a licensed bank with subsidiaries, the HKMA may require the ratio to be calculated on a consolidated basis, or on both a consolidated and an unconsolidated basis, or on a consolidated basis only in respect of such subsidiaries of the licensed bank as may be specified by the HKMA. The HKMA may, after consultation with the licensed bank concerned, increase the ratio for any particular licensed bank. A licensed bank is under a duty to inform the HKMA immediately of a failure to maintain the required capital adequacy ratio and to provide the HKMA with such particulars as it may require. It is an indictable offence not to do so, and the HKMA is entitled to prescribe remedial action.

The capital base of a licensed bank is, broadly speaking but not limited to, all its paid-up capital and reserves, its profit and loss account including its current year's profit or loss, together with perpetual and term subordinated debt meeting prescribed conditions, general provisions against doubtful debts subject to certain limitations and a portion of its latent reserves arising from the revaluation of long-term holdings of specified equity securities or its reserves on the revaluation of

real property. Investments in, advances to and guarantees of liabilities of certain connected companies, shareholdings in subsidiaries or holding companies and in other companies in which more than 20% of voting power is held and investments in other banks (except for those which are not subject to a cross-holding arrangement or not otherwise a strategic investment) must be deducted.

The risk-weighted exposure is determined by:

- (1) multiplying risk-weight factors to the book value of various categories of assets (including but not limited to notes and coins, Hong Kong Government certificates of indebtedness and cash items in the course of collection);
- (2) multiplying the credit conversion factors to various off balance sheet items (including but not limited to direct credit substitutes, transaction-related contingencies, repurchase contracts, note issuance facilities and exchange rate contracts) to determine their credit equivalent amount;
- (3) aggregating the amounts determined pursuant to (1) and (2); and
- (4) subtracting from the amount determined pursuant to (3) the value of general provisions not included in the capital base of the licensed bank and the amount by which the book value of reserves on revaluation of real property exceeds the book value of such reserves as at the period-end.

Risk-weight factors are specified in the Hong Kong Banking (Capital) Rules (Cap. 155L) as being a percentage varying between 0% and 100% to reflect the extent to which an asset might be regarded as being at risk or the extent to which a liability might arise. Credit conversion factors are also specified in the Hong Kong Banking (Capital) Rules (Cap. 155L) as being percentages varying between 0% to 100% representing the percentage of the relevant item to which the risk-weight factor should be applied.

The capital adequacy standards described above (commonly known as “**Basel I**”) were promulgated by the Basel Committee on Banking Supervision (“**BCBS**”) and have been applied in Hong Kong since 1989. The Banking (Amendment) Ordinance 2005, enacted on 6 July 2005, has put in place a legislative framework for the implementation in Hong Kong of Basel II. In line with the timetable set by BCBS for its members, the Hong Kong BCBS commenced implementation of Basel II in January 2007.

There are three approaches under Basel II to calculate credit risks, namely the basic approach, the standardised approach and the internal ratings based approach. Licensed banks in Hong Kong under Basel II are to adopt the standardised approach initially, under which expanded risk weights (0%, 20%, 35%, 75%, 100% and 150%) are used for assessing capital required.

A licensed bank, if approved by the HKMA, may adopt the basic approach in reporting its capital adequacy as a transitional measure before eventually adopting the internal ratings based approach. Under the internal ratings based approach, the capital required of a licensed bank relies on a bank’s internal ratings system (subject to supervisory validation and approval) and are based on three risk components- probability of default, loss given default and exposure at default.

### ***Liquidity***

Authorised institutions must maintain at all times a liquidity ratio of not less than 25% in each calendar month, calculated as the ratio (expressed as a percentage) of the sum of the net weighted amount of its highly liquid assets to the sum of its qualifying liabilities for each working day of the calendar month concerned as calculated in accordance with the fourth schedule to the Hong Kong Banking Ordinance. In relation to a licensed bank with subsidiaries, the HKMA may require that ratio to be calculated on a consolidated basis, or both on a consolidated basis and an unconsolidated basis,

or on a consolidated basis only in respect of such subsidiaries of the licensed bank as may be specified by the HKMA. The ratio may be varied by the HKMA. A licensed bank has a duty to inform the HKMA if the ratio requirement is not fulfilled and provide it with such particulars of that contravention as it may require, and it is an indictable offence not to do so; the HKMA is entitled to prescribe remedial action. For the purpose of the liquidity ratio, in the case of a licensed bank which has places of business in Hong Kong and elsewhere, its places of business in Hong Kong are collectively treated as a separate licensed bank to which the liquidity ratio provisions would apply.

Liquefiable assets are, broadly speaking, assets held in the form of currency notes and coins, gold, loans due within one month from other banks (after deducting amounts payable to other banks within one month), certain export bills payable within one month, certain kinds of marketable debt securities or prescribed instruments (in some cases subject to a discount) and certain types of loan repayments due on fixed dates within one month for performing loans (subject to a discount).

Qualifying liabilities are, broadly speaking, liabilities which will or could or, in the case of contingent liabilities, in the opinion of the HKMA, may, fall due within one month, except that liabilities to other banks are treated on a net basis.

### ***Financial Exposure to Any One Customer***

The financial exposure of a licensed bank incorporated in Hong Kong to any one person or group of connected persons must not (subject to certain exceptions) exceed 25.0% of the capital base of the licensed bank. Subject to certain exclusions, the licensed bank's financial exposure to any one person or group of connected persons is taken to be the aggregate of:

- (1) all advances, loans and credit facilities granted to that person or group;
- (2) the value of the licensed bank's holdings of shares, debentures and other debt securities issued by that person or group; and
- (3) the principal amount, multiplied by a factor to be specified by the HKMA, for off-balance sheet items resulting from transactions between the licensed bank and that person or group.

For these purposes, persons shall be treated as connected if one company is the subsidiary of another, they have a common holding company, they have a common controller (not being a company) or if one (not being a company) is a controller of another (being a company).

The calculation of financial exposure does not include financial exposure to the Hong Kong Government or authorised institutions or financial exposure generally to the extent it is secured by a cash deposit, a guarantee, an undertaking, certain specified securities or a letter of comfort approved by the HKMA.

If a person or a company to whom an authorised institution is financially exposed is a trustee of more than one trust, the HKMA may, by notice in writing, extend the limit on the licensed bank's financial exposure to that person or company.

### ***Other Restrictions on Lending***

The Hong Kong Banking Ordinance also provides that:

- (1) licensed banks may not grant any loan, advance or credit facility (including letters of credit) or give any guarantee against the security of their own shares (or, except with the approval of the HKMA, that of their respective holding companies, subsidiaries or fellow subsidiaries of such holding companies);

- (2) the amount of the facilities which a Hong Kong incorporated licensed bank may make available on an unsecured basis to its controllers, its directors, their relatives or certain of its employees and persons associated with any of them shall be subject to the restrictions set out therein; and
- (3) licensed banks may not, except with the written consent of the HKMA, provide to any one of their employees any unsecured facility of an amount in excess of that employee's salary for one year.

### ***Restrictions on Investments in Land***

A licensed bank incorporated in Hong Kong cannot purchase or hold any interest in land, whether situated in or outside Hong Kong, of a value or to an aggregate value in excess of 25.0% of its capital base. There are exceptions for land held which in the opinion of the HKMA is necessary for the operation of the business or for providing housing or amenities for staff.

### ***Shareholding in Other Companies***

A licensed bank incorporated in Hong Kong may not acquire or hold any part of the share capital of any other company or companies to an aggregate value which exceeds 25.0% of the licensed bank's capital base except for shares held by way of security for facilities and by virtue of acquisitions in satisfaction of debts due to it (which must, however, be disposed of at the earliest suitable opportunity and not later than 18 months after their acquisition unless the HKMA agrees to a longer period). Shares held by virtue of underwriting and sub-underwriting commitments are, nevertheless, permitted provided the relevant shares are disposed of within 7 working days or such longer period as the HKMA may agree.

There are other exemptions for any holding of share capital approved by the HKMA in other banks and companies carrying on nominee, executor, trustee or other functions related to banking business, the business of deposit taking, insurance, investments or other financial services.

### ***Other Restrictions on Investment***

The aggregate of the outstanding amounts of all facilities granted to or on behalf of a licensed bank's controllers, directors, their relatives, certain of its employees and their associates; the value of all holdings of share capital in other companies; and the value of all holdings of interests in land (including land purchased or held which is necessary for the conduct of business or the provision of housing or amenities for the staff of the institution) must not exceed 80.0% of a licensed bank's capital base.

### ***Charges***

A licensed bank incorporated in Hong Kong is not permitted to create any charges over its assets if either the aggregate value of all charges existing over its total assets is 5.0% or more of the value of those total assets or creating that charge would cause the aggregate value of all charges over its total assets to be more than 5.0% of the value of those total assets.

### ***Restrictions on Overseas Activities***

A licensed bank which is incorporated in Hong Kong is subject to a condition that it shall not establish or maintain any overseas branch or overseas representative office without the approval of the HKMA. The HKMA is empowered by the Hong Kong Banking Ordinance to require financial and other information regarding any such overseas branch to be supplied to it.

Further, a licensed bank incorporated in Hong Kong or its Hong Kong incorporated holding company may not without the consent of the HKMA own a company incorporated outside Hong Kong which may (whether or not in or outside Hong Kong) lawfully take deposits from the public. The HKMA may at any time impose in respect of any such approved overseas companies such conditions as the HKMA may think proper.

## Shareholders, Chief Executives and Directors

### *Limitations on Shareholders*

The HKMA has the power to object, on certain specified grounds, to persons becoming or being “controllers” of licensed banks incorporated in Hong Kong. “**Controller**” in this context means:

- (1) a person who, either alone or with any associate(s), is entitled to exercise, or control the exercise of, 10.0% or more, but not more than 50.0%, of the voting power at any general meeting of the licensed bank or of another company of which it is a subsidiary; or
- (2) a person who, either alone or with any associate(s), is entitled to exercise, or control the exercise of, more than 50.0% of the voting power at any general meeting of the licensed bank or of another company of which it is a subsidiary; or
- (3) a person in accordance with whose directions or instructions the directors of the licensed bank or of another company of which it is a subsidiary are accustomed to act (but does not include any professional advisors or managers appointed by the HKMA to manage the licensed bank).

A person may not become a controller of a licensed bank incorporated in Hong Kong unless he has served a written notice on the HKMA of his proposal to that effect and the HKMA consents to his becoming such a controller or does not object within three months.

Within the three-month period, the HKMA may object to the applicant’s proposal, unless it is satisfied that the applicant is a fit and proper person to become a controller; that depositors’ or potential depositors’ interests will not be threatened by that person being such a controller; and having regard to the applicant’s likely influence on that institution as a controller, the licensed bank is likely to continue to conduct its business prudently or that the applicant is likely to undertake adequate remedial action to ensure that the licensed bank will conduct its business prudently. The HKMA may also object to the continuation of a person as a controller on similar grounds as in respect of new controllers.

Where a person becomes a controller (by virtue of being able to exercise or control the exercise of certain voting power in a licensed bank) after a notice of objection has been served on him or otherwise in the contravention of the procedure prescribed by the Hong Kong Banking Ordinance, the HKMA may notify the controller that until further notice, any specified shares are subject to one or more of the following restrictions:

- (1) any transfer of the shares or, in the case of unissued shares, any transfer of the right to be issued with them, and any issue of such shares, shall be void;
- (2) voting rights in respect of those shares shall not be exercisable;
- (3) no further shares in right or pursuant to any offer made to the shareholder shall be issued; or
- (4) except in a liquidation, no payments of any sums due from the licensed bank on the shares shall be paid.

In addition, the HKMA may apply to court for an order that the shares be sold. Once the shares are sold, the proceeds (less the costs of sale) shall be paid into court and held for the benefit of the persons beneficially interested in them.

In the case of an indirect controller who does not have the approval of the HKMA, the person concerned is prohibited from giving directions or instructions to the directors of the licensed bank.

### ***Limitations on Persons Becoming Chief Executives or Directors***

All licensed banks must have a chief executive ordinarily resident in Hong Kong. A person requires the written consent of the HKMA before becoming a chief executive.

The consent of the HKMA is also required for a person to become a director of a Hong Kong incorporated licensed bank.

### **Supervision of Securities Business**

The SFO, which came into operation in April 2003, introduced a substantial change to the conduct of securities business by banks. Banks are no longer exempted from the relevant regulations when they engage in securities business. Instead they are required to apply for registration with the Securities and Futures Commission (“SFC”), which means they will have to meet the Fit and Proper Criteria set by the SFC. Likewise, staff engaged by banks in securities business will have to meet the Fit and Proper Criteria applicable to staff of brokerage firms. It is a statutory condition of registration for banks that each member of staff engaged by them in securities business is a fit and proper person. Banks will also have to comply with the various regulatory requirements set by the SFC in relation to their securities business, including the subsidiary legislation and the business conduct codes. Under the SFO, banks and their securities staff will be subject to the same range of disciplinary actions that are applicable to brokers and their staff in case they are guilty of misconduct or otherwise not fit and proper.

With the introduction of a new licensing regime under the SFO, corresponding changes have been made to the Hong Kong Banking Ordinance by way of the introduction of the Banking (Amendment) Ordinance 2002. Such ordinance came into operation simultaneously with the SFO and has enabled the HKMA to enhance their regulatory functions in relation to the securities businesses of banks and other authorised institutions that are registered under the SFO.



## TERMS AND CONDITIONS OF THE NOTES

*The following is the text of the Conditions of the Notes which (subject to modification and completion and except for the paragraphs in italics) will be endorsed on each Note in definitive form (if issued):*

The U.S.\$225,000,000 6.000% Subordinated Notes due 2020 (the “**Notes**”, which expression shall in these Conditions, unless the context otherwise requires, include any further Notes issued pursuant to Condition 17) of Chong Hing Bank Limited (the “**Issuer**”) are constituted by a Trust Deed (the “**Trust Deed**”) dated 4 November 2010 (the “**Issue Date**”) made between the Issuer and DB Trustees (Hong Kong) Limited (the “**Trustee**”, which expression shall include its successors(s)) as trustee for the holders (as defined below) of the Notes.

The issue of the Notes was authorised by a resolution of the Board of Directors of the Issuer on 14 October 2010.

The statements in these Conditions include summaries of, and are subject to, the detailed provisions of and definitions in the Trust Deed. Copies of the Trust Deed and the Agency Agreement dated 4 November 2010 (the “**Agency Agreement**”) made between the Issuer, Deutsche Bank AG, Hong Kong Branch as principal paying agent, registrar and transfer agent (the “**Principal Paying Agent**”, the “**Registrar**” and the “**Transfer Agent**” (together, the “**Agents**”)) and the Trustee are available for inspection during normal business hours by the Noteholders at the principal office for the time being of the Trustee, being at the date of issue of the Notes at 48th Floor, Cheung Kong Center, 2 Queen’s Road Central, Hong Kong, and at the specified office of each of the Agents. The Noteholders are entitled to the benefit of, are bound by, and are deemed to have notice of, all the provisions of the Trust Deed and the Agency Agreement applicable to them. References in these Conditions to an Agent shall include any successor appointed under the Agency Agreement.

The owners shown in the records of Euroclear Bank SA/NV (“**Euroclear**”) and Clearstream Banking, société anonyme (“**Clearstream, Luxembourg**”) of book-entry interests in Notes are entitled to the benefit of, are bound by and are deemed to have notice of, all the provisions of the Trust Deed and the Agency Agreement applicable to them.

### 1. Form, Denomination and Title

#### (1) *Form and Denomination*

The Notes are issued in registered form, serially numbered, in denominations of U.S.\$100,000 and integral multiples of U.S.\$1,000 in excess thereof. A note certificate (each a “**Certificate**”) will be issued to each Noteholder in respect of its registered holding of Notes. Each Certificate will be numbered serially with an identifying number which will be recorded on the relevant Certificate and in the register of Noteholders which the Issuer will procure to be kept by the Registrar.

*Upon issue, the Notes will be represented by a Global Certificate deposited with the custodian for and registered in the name of a nominee for a common depositary for Euroclear and Clearstream, Luxembourg. The Conditions are modified by certain provisions contained in the Global Certificate. Except in the limited circumstances described in the Global Certificate, owners of interests in Notes represented by the Global Certificate will not be entitled to receive definitive Certificates in respect of their individual holdings of Notes. The Notes are not issuable in bearer form.*

(2) *Title*

Title to the Notes passes only by registration in the register of Noteholders. The holder of any Note will (except as otherwise required by law) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any interest or any writing on (other than a duly completed and signed form of transfer), or the theft or loss of, the Certificate issued in respect of it) and no person will be liable for so treating the holder. In these Conditions “**Noteholder**” and (in relation to a Note) “**holder**” mean the person in whose name a Note is registered in the register of Noteholders.

**2. Transfers of Notes and Issue of Certificates**

(1) *Register*

The Issuer will cause to be kept at the specified office of the Registrar and in accordance with the terms of the Agency Agreement a register on which shall be entered the names and addresses of the holders of the Notes and the particulars of the Notes held by them and of all transfers of the Notes (the “**Register**”).

Each Noteholder shall be entitled to receive only one Certificate in respect of its entire holding.

(2) *Transfers*

A Note may be transferred by depositing the Certificate issued in respect of that Note, with the form of transfer on the back duly completed and signed, at the specified office of the Registrar or any of the Agents.

(3) *Delivery of new Certificates*

Each new Certificate to be issued upon transfer of Notes will, within seven business days of receipt by the Registrar or the relevant Agent of the duly completed form of transfer endorsed on the relevant Certificate, be mailed by uninsured mail at the risk of the holder entitled to the Note to the address specified in the form of transfer. For the purposes of this Condition, “**business day**” shall mean a day on which banks are open for business in the city in which the specified office of the Agent with whom a Certificate is deposited in connection with a transfer is located.

*Except in the limited circumstances described herein, owners of interests in the Notes will not be entitled to receive physical delivery of Certificates.*

Where some but not all of the Notes in respect of which a Certificate is issued are to be transferred, a new Certificate in respect of the Notes not so transferred will, within seven business days of receipt by the Registrar or the relevant Agent of the original Certificate, be mailed by uninsured mail at the risk of the holder of the Notes not so transferred to the address of such holder appearing on the register of Noteholders or as specified in the form of transfer.

(4) *Formalities free of charge*

Registration of transfer of Notes will be effected without charge by or on behalf of the Issuer or any Agent but upon payment (or the giving of such indemnity as the Issuer or any Agent may reasonably require) in respect of any tax or other governmental charges which may be imposed in relation to such transfer.

(5) *Closed Periods*

No Noteholder may require the transfer of a Note to be registered during the period of 15 days ending on the due date for any payment of principal, premium or interest on that Note.

(6) *Regulations*

All transfers of Notes and entries on the register of Noteholders will be made subject to the detailed regulations concerning transfer of Notes scheduled to the Trust Deed. The regulations may be changed by the Issuer with the prior written approval of the Registrar and the Trustee. A copy of the current regulations will be mailed (free of charge and at the expense of the Issuer) by the Registrar to any Noteholder who requests one.

**3. Status**

(1) *Subordination*

- (a) The Notes constitute direct, unsecured and, in accordance with sub-paragraph (b) below, subordinated obligations of the Issuer, ranking *pari passu* without any preference among themselves.
- (b) The claims of the holders of the Notes will, in the event of the winding up of the Issuer, be subordinated in right of payment in the manner provided in the Trust Deed to the claims of depositors and all other unsubordinated creditors of the Issuer and will rank, in the event of the winding up of the Issuer, at least *pari passu* in right of payment with all other Subordinated Indebtedness (as defined below), present and future, of the Issuer. Claims in respect of the Notes will rank in priority to the rights and claims of holders of subordinated liabilities which by their terms rank or are expressed to rank in right of payment junior to the Notes and of all classes of equity securities of the Issuer, including holders of preference shares, if any.

*The Notes do not limit the amount of unsubordinated indebtedness or deposits or other liabilities, which rank senior to the Notes, that the Issuer may hereafter incur.*

(2) *Waiver of Set-Off*

Claims in respect of any Notes may not be set-off, or be the subject of a counterclaim, by the holder against or in respect of any obligations of the holder to the Issuer or to any other persons and the holder of any Note shall, by virtue of being the holder of any Note, be deemed to have waived all such rights of set-off and counterclaim to the fullest extent permitted by applicable law.

(3) *Noteholders to Account*

In the event that any Noteholder nevertheless receives (whether by set-off or otherwise) directly in a winding up proceeding in respect of the Issuer any payment by, or distribution of assets of, the Issuer of any kind or character, whether in cash, property or securities, in respect of any amount owing to it by the Issuer arising under or in connection with the Notes, other than in accordance with Condition 3(1) and Clause 7 (Subordination) of the Trust Deed, such Noteholder shall, subject to applicable law, immediately pay an amount equal to the amount of such payment or discharge to the liquidator for the time being in the winding up of the Issuer for distribution in accordance with Clause 7 (Subordination) of the Trust Deed and each Noteholder, by virtue of becoming a Noteholder, shall be deemed to have so agreed and undertaken with and to the Issuer and all depositors and other unsubordinated creditors of the Issuer for good consideration.

(4) *Change in Status Upon Regulatory Event*

- (a) If at any time the Hong Kong Monetary Authority or any successor thereto (the “HKMA”) decides, having regard to the applicable regulatory framework, that the Notes no longer fully qualify as term subordinated debt for inclusion in Category II — Supplementary Capital of the Issuer, subject to paragraph (b) below, the Issuer may, on or after 1 January 2013, at its option, and subject to the prior written approval of the HKMA, provide notice

to such effect to Noteholders in accordance with Condition 13. Such notice (a “**Change in Status Notice**”) shall become effective on an Interest Payment Date falling after 1 January 2013 specified therein, and must be given at least 30 days prior to the Interest Payment Date on which it is to become effective. Upon a Change in Status Notice becoming effective, Condition 3(1) and Condition 10(1) will no longer apply, and the Notes shall thereafter constitute direct, unconditional, unsubordinated and (subject to Condition 4) unsecured obligations of the Issuer and shall at all times thereafter rank *pari passu* and without any preference among themselves. The payment obligations of the Issuer under the Notes shall, save for such exceptions as may be provided by applicable legislation and subject to Condition 4, at all times thereafter rank at least equally with all its other present and future unsecured and unsubordinated obligations including liabilities in respect of deposits.

- (b) Notwithstanding the foregoing, the Issuer may not give a Change in Status Notice if the Notes are excluded from Category II — Supplementary Capital solely due to the following reasons:
- (i) amortisation applicable to Category II — Supplementary Capital status as contemplated in Banking (Capital) Rules of Hong Kong (Cap. 155L), or any successor rule or ordinance that contemplates amortisation of Category II — Supplementary Capital status prior to the Maturity Date (as defined in Condition 7(1));
  - (ii) amortisation due to transitional arrangements for future amendments to Banking (Capital) Rules of Hong Kong (Cap. 155L) relative to its status as of the date of issue of the Notes, except where such transitional arrangements cause the Notes to be fully disqualified from Category II — Supplementary Capital prior to their Maturity Date; or
  - (iii) where such exclusion is only due to the application of regulatory limitations on the amount of Category II — Supplementary Capital that may be recognised as supplementary capital of the Issuer.

#### (5) *Definition*

For the purposes of this Condition, “**Subordinated Indebtedness**” means all indebtedness which is subordinated, in the event of the winding up of the Issuer, in right of payment to the claims of depositors and other unsubordinated creditors of the Issuer, and for this purpose, indebtedness shall include all liabilities, whether actual or contingent.

#### 4. **Negative Pledge**

From and including the date on which a Change in Status Notice becomes effective pursuant to Condition 3(4) and so long as any of the Notes remains outstanding (as defined in the Trust Deed), the Issuer will not create or permit to subsist, and will procure that no Subsidiary (as defined in the Trust Deed) of the Issuer creates or permits to subsist, any mortgage, charge, pledge, lien or other form of encumbrance or security interest (“**Security**”) upon the whole or any part of its undertaking, assets or revenues, present or future, to secure any Relevant Indebtedness (as defined below) or to secure any guarantee of or indemnity in respect of any Relevant Indebtedness unless, at the same time or prior thereto, the Issuer’s obligations under the Notes are, to the satisfaction of the Trustee, (a) secured equally and rateably therewith or benefit from a guarantee or indemnity that is secured equally and rateably therewith, as the case may be, or (b) have the benefit of such other security, guarantee, indemnity or other arrangement as shall be approved by an Extraordinary Resolution (as defined in the Trust Deed) of the Noteholders.

For the purposes of these Conditions, “**Relevant Indebtedness**” means (i) any present or future indebtedness (whether being principal, premium, interest or other amounts) for or in respect of any notes, bonds, debentures, debenture stock, loan stock or other securities which are for the time being, or capable of being, quoted, listed or ordinarily dealt in on any stock exchange, over-the-counter or other securities market, and (ii) any guarantee or indemnity of any such indebtedness.

## 5. Interest

### (1) *Interest Rate and Interest Payment Dates*

The Notes bear interest at the rate of 6.000% per annum from, and including, 4 November 2010 to, but excluding, the Maturity Date (as defined in Condition 7(1)), provided however, that from and including the Interest Payment Date immediately on which a Change in Status Notice becomes effective pursuant to Condition 3(4), the rate of interest on the Notes shall be reduced by 0.500% per annum. For the avoidance of doubt, the rate of interest on the Notes upon a Change in Status Notice becoming effective shall be 5.500% per annum. Interest on the Notes is payable semi-annually in arrear on 4 May and 4 November in each year (each an “**Interest Payment Date**”). The period from and including an Interest Payment Date (or, in the case of the first Interest Period, the Issue Date) to but excluding the next succeeding Interest Payment Date (or, in the case of the last Interest Period, the Maturity Date), is called an “**Interest Period**”.

### (2) *Determination of Interest Amount*

During the period from, and including, 4 November 2010 to, but excluding, the Maturity Date, when interest required to be calculated in respect of a period of less than a full six months, it shall be calculated on the basis of a 360-day year consisting of 12 months of 30 days each and, in the case of an incomplete month, the number of days elapsed on the basis of a month of 30 days.

### (3) *Interest Accrual*

Each Note will cease to bear interest from, and including, its due date for redemption unless, upon due presentation, payment of the principal in respect of the Note is improperly withheld or refused or unless default is otherwise made in respect of payment in which event interest will continue to accrue (as well after as before any judgment) as provided in the Trust Deed.

## 6. Payments

### (1) *Payments in respect of Notes*

Payments of principal and interest will be made by transfer to the registered account of the Noteholder or by U.S. dollar cheque drawn on a bank that processes payments in U.S. dollars mailed to the registered address of the Noteholder if it does not have a registered account. Payments of principal and payments of interest due otherwise than on an Interest Payment Date will only be made against surrender of the relevant Certificate at the specified office of any of the Agents. Interest on Notes due on an Interest Payment Date will be paid to the holder shown on the register of Noteholders at the close of business on the date (the “**record date**”) being the fifteenth day before the relevant Interest Payment Date.

For the purposes of this Condition, a Noteholder’s “**registered account**” means the U.S. dollar account maintained by or on behalf of it with a bank that processes payments in U.S. dollars, details of which appear on the register of Noteholders at the close of business, in the case of principal and interest due otherwise than on an Interest Payment Date, on the second Business Day (as defined below) before the due date for payment and, in the case of interest due on an Interest Payment Date, on the relevant record date, and a Noteholder’s registered address means its address appearing on the register of Noteholders at that time.

(2) *Payments subject to Applicable Laws*

Payments in respect of principal and interest on Notes are subject in all cases to any fiscal or other laws and regulations applicable in the place of payment, but without prejudice to the provisions of Condition 8.

(3) *No commissions*

No commissions or expenses shall be charged to the Noteholders in respect of any payments made in accordance with this Condition.

(4) *Payment on Business Days*

Where payment is to be made by transfer to a registered account, payment instructions (for value the due date or, if that is not a Business Day (as defined below), for value the first following day which is a Business Day) will be initiated and, where payment is to be made by cheque, the cheque will be mailed, on the Business Day preceding the due date for payment or, in the case of a payment of principal or a payment of interest due otherwise than on an Interest Payment Date, if later, on the Business Day on which the relevant Certificate is surrendered at the specified office of an Agent.

Noteholders will not be entitled to any interest or other payment for any delay after the due date in receiving the amount due if the due date is not a Business Day, if the Noteholder is late in surrendering its Certificate (if required to do so) or if a cheque mailed in accordance with this Condition arrives after the due date for payment or is lost in the mail.

In this Condition, “**Business Day**” means a day (other than a Saturday or Sunday) on which commercial banks are open for business in Hong Kong, New York City, London and, in the case of presentation of a Note Certificate, in the place in which the Note Certificate is presented.

(5) *Partial Payments*

If the amount of principal or interest which is due on the Notes is not paid in full, the Registrar will annotate the register of Noteholders with a record of the amount of principal or interest in fact paid.

(6) *Agents*

The names of the initial Agents and their initial specified offices are set out at the end of these Conditions. The Issuer reserves the right, subject to the prior written approval of the Trustee, at any time to vary or terminate the appointment of any Agent and to appoint additional or other Agents provided that it will at all times maintain:

- (a) a Principal Paying Agent;
- (b) a Registrar with a specified office in Hong Kong; and
- (c) so long as the Notes are listed on the Hong Kong Stock Exchange, a Paying Agent (which may be the Principal Paying Agent) with a specified office in Hong Kong unless the Issuer obtains an exemption from The Stock Exchange of Hong Kong Limited.

Notice of any termination or appointment and of any changes in specified offices will be given to the Noteholders promptly by the Issuer in accordance with Condition 13.



## 7. Redemption and Purchase

### (1) *Redemption at Maturity*

Unless previously redeemed or purchased and cancelled as provided below, the Issuer will redeem the Notes at their principal amount on the Interest Payment Date falling on or about 4 November 2020 (the “**Maturity Date**”).

### (2) *Redemption for Taxation Reasons*

Subject to Condition 7(6), if the Issuer satisfies the Trustee immediately before the giving of the notice referred to below that (a) as a result of any change in, or amendment to, the laws or regulations of a Relevant Jurisdiction (as defined in Condition 8(2)(b) below) or any change in the official interpretation of the laws or regulations of a Relevant Jurisdiction, which change or amendment becomes effective after 28 October 2010, on the occasion of the next payment due in respect of the Notes the Issuer would be required to pay additional amounts as provided or referred to in Condition 8, and (b) the requirement cannot be avoided by the Issuer taking reasonable measures available to it, the Issuer may at its option, having given not less than 30 nor more than 60 days’ notice to the Noteholders in accordance with Condition 13 (which notice shall be irrevocable and shall specify the date fixed for redemption), redeem all the Notes, but not some only, at any time at their principal amount together with interest accrued to but excluding the date of redemption, provided that no notice of redemption shall be given earlier than 90 days before the earliest date on which the Issuer would be required to pay the additional amounts were a payment in respect of the Notes then due. Prior to the publication of any notice of redemption pursuant to this paragraph, the Issuer shall deliver to the Trustee a certificate signed by two Authorised Signatories (as defined in the Trust Deed) of the Issuer stating that the requirement referred to in (a) above will apply on the occasion of the next payment due in respect of the Notes and cannot be avoided by the Issuer taking reasonable measures available to it and the Trustee shall be entitled to accept the certificate as sufficient evidence of the satisfaction of the conditions precedent set out above, in which event it shall be binding on the Noteholders.

### (3) *Purchases*

Subject to Condition 7(6) below, the Issuer or any of its Subsidiaries may at any time purchase Notes in any manner and at any price.

### (4) *Cancellations*

All Notes which are (a) redeemed or (b) purchased by or on behalf of the Issuer will forthwith be cancelled and accordingly may not be held, reissued or resold. For the avoidance of doubt, this provision shall not apply to the Issuer holding the Notes in a purely nominee capacity.

### (5) *Notices Final*

Upon the expiry of any notice as is referred to in paragraph (2) above, the Issuer shall be bound to redeem the Notes to which the notice refers in accordance with the terms of such paragraph.

### (6) *Conditions for Redemption and Purchase*

Notwithstanding any other provision in these Conditions and prior to a Change in Status Notice becoming effective pursuant to Condition 3(4), the Notes (subject as provided below) may not be redeemed (other than pursuant to Condition 7(1) or 10(1)) or purchased without the prior written consent of the HKMA. Accordingly, the Issuer shall not redeem any of the Notes (other than pursuant to Condition 7(1) or 10(1)) and the Issuer or any of its Subsidiaries shall not purchase any of the Notes unless the prior written consent of the HKMA thereto shall have been obtained, provided however, that if from time to time the consent of the HKMA is not a requirement of any such Notes to constitute “Supplementary Capital” (or equivalent) of the Issuer for the purposes of, and as defined in,



the Banking (Capital) Rules (Cap. 155L) of Hong Kong, or any successor legislation, then the condition to the redemption or purchase and cancellation of the Notes set out in this Condition 7(6) shall not apply for so long as such consent is not required. For the avoidance of doubt, this provision shall not apply to the Issuer or any of its Subsidiaries holding the Notes in a purely nominee capacity.

*Upon a Change in Status Notice becoming effective, prior consent, written or otherwise, of the HKMA for the redemption or purchase of the Notes will not be required.*

*Noteholders should note that it is intended that the Notes should constitute Category II Supplementary Capital of the Issuer and, accordingly, under statutory requirements prevailing at the date hereof relating to Category II Supplementary Capital, and by virtue of the above provisions, any redemption of the Notes, other than at maturity or following an event of default, and any purchase of the Notes by the Issuer or any of its Subsidiaries, is subject to the prior written consent of the HKMA at the relevant time.*

## **8. Taxation**

### *(1) Payment without Withholding or Deduction*

All payments in respect of the Notes by or on behalf of the Issuer shall be made without withholding or deduction for, or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature (“**Taxes**”) imposed or levied by or on behalf of the Relevant Jurisdiction, unless the withholding or deduction of the Taxes is required by law. In that event, the Issuer will pay such additional amounts as may be necessary in order that the net amounts received by the Noteholders after the withholding or deduction shall equal the respective amounts which would have been receivable in respect of the Notes in the absence of the withholding or deduction; except that no additional amounts shall be payable in relation to any payment in respect of any Note:

- (a) presented for payment by or on behalf of a holder who is liable to the Taxes in respect of the Note by reason of his having some connection with the Relevant Jurisdiction other than the mere holding of the Note;
- (b) presented for payment more than 30 days after the Relevant Date except to the extent that a holder would have been entitled to additional amounts on presenting the same for payment on the last day of the period of 30 days assuming, whether or not such is in fact the case, that day to have been a Business Day (as defined in Condition 6(4)); or
- (c) where such withholding or deduction is imposed on a payment to an individual and is required to be made pursuant to European Council Directive 2003/48/EC or any law implementing or complying with, or introduced in order to conform to, such Directive.

### *(2) Interpretation*

In these Conditions:

- (a) “**Relevant Date**” means the date on which the payment first becomes due but, if the full amount of the money payable has not been received by the Principal Paying Agent or the Trustee on or before the due date, it means the date on which, the full amount of the money having been so received, notice to that effect shall have been duly given to the Noteholders by the Issuer in accordance with Condition 13; and

- (b) “**Relevant Jurisdiction**” means the Hong Kong Special Administrative Region of the People’s Republic of China (“**Hong Kong**”) or any political subdivision or any authority thereof or therein having power to tax or any other jurisdiction or any political subdivision or any authority thereof or therein having power to tax to which the Issuer becomes subject in respect of payments made by it of principal or interest on the Notes.

(3) *Additional Amounts*

Any reference in these Conditions to any amounts in respect of the Notes shall be deemed also to refer to any additional amounts which may be payable under this Condition or under any undertaking given in addition to, or in substitution for, this Condition pursuant to the Trust Deed.

**9. Prescription**

Claims in respect of principal and interest will become prescribed unless made within 10 years (in the case of principal) and five years (in the case of interest) from the Relevant Date.

**10. Events of Default**

(1) *Events of Default prior to a Change in Status Notice becoming effective*

The following are events of default (each a “**Subordinated Note Event of Default**”) with respect to the Notes until (but excluding) the date on which a Change in Status Notice becomes effective pursuant to Condition 3(4):

- (a) if default is made in the payment of principal or interest due in respect of the Notes or any of them and the default continues for a period of five Business Days in Hong Kong (in the case of principal) or ten Business Days in Hong Kong (in the case of interest), then the Trustee at its discretion may, without prejudice to (b) below and subject as provided in Condition 11(2), without further notice, institute proceedings for the winding up of the Issuer in Hong Kong, but may take no further action in respect of such default; or
- (b) if an order is made or an effective resolution is passed for the winding up or dissolution of the Issuer in Hong Kong (except for the purposes of a reconstruction, amalgamation or reorganisation the terms of which have previously been approved by an Extraordinary Resolution (which is defined in the Trust Deed as a resolution duly passed by a majority of not less than three-fourths of the votes cast thereon) of the Noteholders), then the Trustee at its discretion may, subject as provided in Condition 11(2), give written notice to the Issuer that the Notes are, and they shall forthwith thereupon become, immediately due and repayable at their principal amount together with accrued interest as provided in the Trust Deed.

(2) *Events of Default on and after a Change in Status Notice becomes effective*

From and including the date on which a Change in Status Notice becomes effective pursuant to Condition 3(4) and in circumstances where there is an unremedied Senior Note Event of Default, the Trustee at its discretion may, and if so requested in writing by the holders of at least one-quarter in principal amount of the Notes then outstanding or if so directed by an Extraordinary Resolution of the Noteholders shall (subject in each case to being indemnified and/or secured and/or put in funds to its satisfaction), give notice in writing to the Issuer that each Note is and each Note shall thereupon become immediately due and repayable at its principal amount, together with accrued interest (if any) as provided in the Trust Deed, if any of the following events (each a “**Senior Note Event of Default**”) shall occur:

- (a) a default is made for more than seven days in the payment of any principal or 14 days in the payment of any interest due in respect of the Notes;

- (b) the Issuer does not perform or comply with one or more of its other obligations in the Notes, which default is incapable of remedy or, if in the opinion of the Trustee acting, if the Trustee considers it necessary, on the instructions of the Noteholders, it is capable of remedy, is not remedied within 30 days after written notice of such default shall have been given to the Issuer by the Trustee;
- (c) the Issuer or any of its Subsidiaries is (or is, or could be deemed by law or a court to be) insolvent or bankrupt or is unable to pay its debts as or when they fall due, stops, suspends or threatens to stop or suspend payment of all or a material part of (or of a particular type of) its debts as or when they fall due, proposes or makes any agreement for the deferral, rescheduling or other readjustment of all of (or all of a particular type of) its debts (or of any part which it will or might otherwise be unable to pay when due) (but excluding any deferral, rescheduling or other readjustment of any deposits in the ordinary course of business of the Issuer or any of its Subsidiaries) or proposes or makes a general assignments, arrangement or composition with or for the benefit of the relevant creditors in respect of any of such debts or a moratorium is agreed or declared in respect of or affecting all or any part of (or a particular type of) the debts of the Issuer or any of its Subsidiaries;
- (d) (i) any other present or future indebtedness of the Issuer or any of its Subsidiaries for or in respect of moneys borrowed or raised becomes capable of being declared due and payable prior to its stated maturity by reason of any actual or potential default, event of default or the like (howsoever described), or (ii) any such indebtedness is not paid when due or, as the case may be, within any applicable grace period, or (iii) the Issuer or any of its Subsidiaries fails to pay when due any amount payable by it under any present or future guarantee for, or indemnity in respect of, any moneys borrowed or raised, provided that the aggregate amount of the relevant indebtedness, guarantees and indemnities in respect of which one or more of the events mentioned above in this paragraph (d) have occurred equals or exceeds U.S.\$20,000,000 or its equivalent in any other currency (on the basis of the middle spot rate for the relevant currency against the US dollar as quoted by any lead bank on the day on which this paragraph operates) on the day on which such indebtedness becomes due and payable or is not paid or any such amount becomes due and payable or is not paid under any such guarantee or indemnity;
- (e) a distress, attachment, execution or other legal process is levied, enforced or sued out on or against any material part of the property, assets or turnover of the Issuer or any of its Subsidiaries and is not discharged or stayed within 60 days;
- (f) an order is made or an effective resolution passed for the winding-up or dissolution or administration of the Issuer or any of its Subsidiaries, or the Issuer or any of its Subsidiaries ceases or threatens to cease to carry on all or substantially all of its business or operations, except for the purpose of and followed by a reconstruction, amalgamation, reorganisation, merger or consolidation (i) on terms approved by an Extraordinary Resolution of the Noteholders, or (ii) in the case of a Subsidiary, whereby the undertaking and assets of such Subsidiary are transferred to or otherwise vested in the Issuer or another of its Subsidiaries;
- (g) an encumbrancer takes possession of, or a receiver or other administrator is appointed by an encumbrancer or a court in respect of, any of the assets or undertaking (or a substantial part thereof) of the Issuer or any of its Subsidiaries and such possession is not surrendered, or appointment discharged, within 60 days.
- (h) any step is taken by any person with a view to the seizure, compulsory acquisition, expropriation or nationalisation of all or a material part of the assets of the Issuer or any of its Subsidiaries;

- (i) it is or will become unlawful for the Issuer to perform or comply with any one or more of its obligations under any of the Notes;
- (j) any action, condition or thing (including the obtaining or effecting of any necessary consent, approval, authorisation, exemption, filing, license, order, recording or registration) at any time required to be taken, fulfilled or done in order (i) to enable the Issuer lawfully to enter into, exercise its rights and perform and comply with its obligations under the Notes, (b) to ensure that those obligations are legally binding and enforceable and (c) to make the Notes admissible in evidence in the courts of Hong Kong is not taken, fulfilled or done; or
- (k) any event occurs which, under the laws of any relevant jurisdiction, has an analogous effect to any of the events referred to in any of the foregoing paragraphs.

## **11. Enforcement**

- (1) Without prejudice to Condition 10, the Trustee may at any time, subject as provided below, at its discretion and without further notice, institute such proceedings against the Issuer as it may think fit to enforce any obligation, condition or provision binding on the Issuer under the Notes or the Trust Deed (other than any obligation for the payment of any principal or interest in respect of the Notes), provided, in relation to Condition 10(1)(a) only, that the Issuer shall not as a consequence of such proceedings be obliged to pay any sum or sums representing or measured by reference to principal or interest in respect of the Notes sooner than the same would otherwise have been payable by it.
- (2) The Trustee shall not be bound to take action as referred to in Condition 10 or paragraph (1) above or any other action under the Trust Deed unless (i) it shall have been so requested in writing by Noteholders holding at least one-quarter of the principal amount of the Notes then outstanding or if so directed by an Extraordinary Resolution of the Noteholders and (ii) it shall have been indemnified and/or secured to its satisfaction.
- (3) So long as the Notes constitute subordinated obligations of the Issuer in accordance with Condition 3(1), no Noteholder shall be entitled to proceed directly against the Issuer unless the Trustee having become bound so to proceed, fails to do so within a reasonable period and such failure is continuing. No Noteholder shall be entitled to institute proceedings in Hong Kong (or elsewhere) for the winding up of the Issuer or to submit a claim in such winding up except that, if the Trustee, having become bound to institute such proceedings as aforesaid, fails to do so, or, being able and bound to submit a claim in such winding up, fails to do so, in each case within a reasonable period and such failure is continuing, then any such holder may, on giving an indemnity and/or a security satisfactory to the Trustee, in the name of the Trustee (but not otherwise), himself institute proceedings for the winding up of the Issuer in Hong Kong (but not elsewhere) and/or submit a claim in such winding up to the same extent (but not further or otherwise) that the Trustee would have been entitled to do.

## **12. Replacement of Certificates**

Should any Certificate be lost, stolen, mutilated, defaced or destroyed it may be replaced at the specified office of the Principal Paying Agent upon payment by the claimant of the expenses incurred in connection with the replacement and on such terms as to evidence and indemnity as the Issuer may reasonably require. Mutilated or defaced Certificates must be surrendered before replacements will be issued.

## **13. Notices**

All notices to the Noteholders will be valid if mailed to them at their respective addresses in the register of Noteholders maintained by the Registrar. The Issuer shall also ensure that notices are duly

given in a manner which complies with the rules and regulations of any stock exchange on which the Notes are for the time being listed. Any such notice will be deemed to have been given on the second day after being so mailed. If notification as provided above is not practicable, notice shall be given in such other manner, and shall be deemed to have been given on such date, as the Trustee may approve.

#### **14. Meeting of Noteholders, Modification etc.**

##### *(1) Provisions for Meetings*

The Trust Deed contains provisions for convening meetings of the Noteholders to consider any matter affecting their interests, including the modification by Extraordinary Resolution of any of these Conditions or any of the provisions of the Trust Deed. The quorum at any meeting for passing an Extraordinary Resolution will be one or more persons present holding or representing more than 50% in principal amount of the Notes for the time being outstanding, or at any adjourned meeting one or more persons present whatever the principal amount of the Notes held or represented by him or them, except that at any meeting the business of which includes the modification of certain of these Conditions and certain of the provisions of the Trust Deed the necessary quorum for passing an Extraordinary Resolution will be one or more persons present holding or representing not less than two-thirds, or at any adjourned meeting not less than one-third, of the principal amount of the Notes for the time being outstanding. An Extraordinary Resolution passed at any meeting of the Noteholders will be binding on all Noteholders, whether or not they are present at the meeting.

In addition, a resolution in writing signed by or on behalf of Noteholders of at least 90% in aggregate principal amount of Notes for the time being outstanding who for the time being are entitled to receive notice of a meeting of Noteholders will take effect as if it were an Extraordinary Resolution. Such a resolution in writing may be contained in one document or several documents in the same form, each signed by or on behalf of one or more Noteholders.

##### *(2) Modification*

The Trustee may agree, without the consent of the Noteholders but, prior to a Change of Status Notice becoming effective, with the prior written consent of the HKMA, to any modification of, or to the waiver or authorisation of any breach or proposed breach of, any of these Conditions or any of the provisions of the Trust Deed, or determine, without any such consent as aforesaid, that any Subordinated Note Event of Default, Senior Note Event of Default or Potential Event of Default (as defined in the Trust Deed) shall not be treated as such, provided that, in any such case, it is not, in the opinion of the Trustee, materially prejudicial to the interests of the Noteholders or may agree, without any such consent as aforesaid, to any modification which is of a formal, minor or technical nature or to correct a manifest error or an error which, in the opinion of the Trustee, is proven. Any such modification, waiver, authorisation or determination, or substitution referred to in Condition 15 shall be binding on the Noteholders and, unless the Trustee agrees otherwise, shall be notified by the Issuer to the Noteholders as soon as practicable thereafter in accordance with Condition 13.

##### *(3) Exercise of Powers by Trustee*

In connection with the exercise by it of any of its trusts, powers, authorities or discretions (including, without limitation, any modification, waiver, authorisation, determination or substitution), the Trustee shall have regard to the general interests of the Noteholders as a class but shall not have regard to any interests arising from circumstances particular to individual Noteholders (whatever their number) and, in particular but without limitation, shall not have regard to the consequences of any such exercise for individual Noteholders (whatever their number) resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory or any political subdivision thereof and the Trustee shall not be entitled to require,

nor shall any Noteholder be entitled to claim, from the Issuer, the Trustee or any other person any indemnification or payment in respect of any tax consequences of any such exercise upon individual Noteholders except to the extent already provided for in Condition 8 and/or any undertaking given in addition to, or in substitution for, Condition 8 pursuant to the Trust Deed.

## **15. Substitution**

The Trustee may, without the consent of the Noteholders, agree with the Issuer to the substitution in place of the Issuer (or of any previous substitute under this Condition) as the principal debtor under the Notes and the Trust Deed of any Subsidiary of the Issuer, subject to:

- (a) so long as the Notes qualify as term subordinated debt for inclusion in Category II — Supplementary Capital of the Issuer, prior written approval of the HKMA and (if and to the extent as required under applicable laws and regulations) any other approval;
- (b) the Trustee being satisfied that the interests of the Noteholders will not be materially prejudiced by the substitution; and
- (c) certain other conditions set out in the Trust Deed being complied with.

## **16. Indemnification of the Trustee and its Contracting with the Issuer**

The Trust Deed contains provisions for the indemnification of the Trustee and for its relief from responsibility, including provisions relieving it from taking action unless indemnified and/or secured to its satisfaction.

The Trust Deed also contains provisions pursuant to which the Trustee is entitled, inter alia, (i) to enter into business transactions with the Issuer and/or any of its Subsidiaries and to act as trustee for the holders of any other securities issued or guaranteed by, or relating to, the Issuer and/or any of its Subsidiaries, (ii) to exercise and enforce its rights, comply with its obligations and perform its duties under or in relation to any such transactions or, as the case may be, any such trusteeship without regard to the interests of, or consequences for, the Noteholders, and (iii) to retain and not be liable to account for any profit made or any other amount or benefit received thereby or in connection therewith.

## **17. Further Issues**

The Issuer is at liberty from time to time, without the consent of the Noteholders, to create and issue further notes or bonds (in registered form) either (a) ranking *pari passu* in all respects (or in all respects save for the first payment of interest thereon) and so that the same shall be consolidated and form a single series with the outstanding notes or bonds of any series (including the Notes) constituted by the Trust Deed or any supplemental deed or (b) upon such terms as to ranking, interest, conversion, redemption and otherwise as the Issuer may determine at the time of the issue. Any further notes or bonds which are to form a single series with the outstanding notes or bonds of any series (including the Notes) constituted by the Trust Deed or any supplemental deed shall, and any other further notes or bonds may (with the consent of the Trustee), be constituted by a deed supplemental to the Trust Deed. The Trust Deed contains provisions for convening a single meeting of the Noteholders and the holders of notes or bonds of other series in certain circumstances where the Trustee so decides.

## **18. Contracts (Rights of Third Parties) Act 1999**

The Notes confer no rights under the Contracts (Rights of Third Parties) Act 1999 to enforce any term of the Notes, but this does not affect any right or remedy of a third party which exists or is available apart from that Act.

## 19. Governing Law and Submission to Jurisdiction

### (1) *Governing Law*

The Trust Deed and the Notes and any non-contractual obligations arising out of or in connection with them are governed by, and will be construed in accordance with, English law, save for Condition 3 which is governed by, and will be construed in accordance with, Hong Kong law.

### (2) *Jurisdiction of English Courts*

Each of the Issuer and the Trustee has in the Trust Deed irrevocably and unconditionally agreed that the courts of England are to have exclusive jurisdiction to settle any disputes which may arise out of or in connection with the Trust Deed or the Notes and that accordingly any suit, action or proceedings arising out of or in connection therewith (together referred to as “**Proceedings**”) may be brought in the courts of England. Each of the Issuer and the Trustee has in the Trust Deed irrevocably and unconditionally waived and agreed not to raise any objection which it may have now or subsequently to the laying of the venue of any Proceedings in the courts of England and any claim that any Proceedings have been brought in an inconvenient or inappropriate forum.

### (3) *Appointment of Process Agent*

The Issuer has in the Trust Deed appointed Law Debenture Corporate Services Limited at its office for the time being (now at Fifth Floor, 100 Wood Street, London) as its agent for service of process in England in respect of any Proceedings and has undertaken that in the event of such agent ceasing so to act it will appoint such other person as the Trustee may approve as its agent for that purpose.



## THE GLOBAL CERTIFICATE

*The Global Certificate contains the following provisions which apply to the Notes whilst they are represented by the Global Certificate, some of which modify the effect of the Conditions. Terms defined in the Conditions have the same meaning in paragraphs 1 to 6 below.*

### 1. **Accountholders**

For so long as all of the Notes are represented by the Global Certificate and the Global Certificate is held on behalf of a clearing system, each person (other than another clearing system) who is for the time being shown in the records of Euroclear or Clearstream, Luxembourg (as the case may be) as the holder of a particular aggregate principal amount of such Notes (each an “**Accountholder**”) (in which regard any certificate or other document issued by Euroclear or Clearstream, Luxembourg (as the case may be) as to the aggregate principal amount of such Notes standing to the account of any person shall, in the absence of manifest error, be conclusive and binding for all purposes) shall be treated as the holder of such aggregate principal amount of such Notes (and the expression “**Noteholders**” and references to “**holding Notes**” and to “**holder of Notes**” shall be construed accordingly) for all purposes other than with respect to payments on such Notes, the right to which shall be vested, as against the Issuer and the Trustee, solely in the nominee for the relevant clearing system (the “**Relevant Nominee**”) in accordance with and subject to the terms of the Global Certificate. Each Accountholder must look solely to Euroclear or Clearstream, Luxembourg, as the case may be, for its share of each payment made to the Relevant Nominee.

### 2. **Cancellation**

Cancellation of any Note following its redemption or purchase by the Issuer will be effected by reduction in the aggregate principal amount of the Notes in the register of Noteholders and by the annotation of the appropriate schedule to the Global Certificate.

### 3. **Payments**

Payments of principal and interest in respect of Notes represented by the Global Certificate will be made upon presentation or, if no further payment falls to be made in respect of the Notes, against presentation and surrender of the Global Certificate to or to the order of the Registrar or such other Agent as shall have been notified to the holder of the Global Certificate for such purpose.

Distributions of amounts with respect to book-entry interests in the Notes held through Euroclear or Clearstream, Luxembourg will be credited, to the extent received by the Principal Paying Agent, to the cash accounts of Euroclear or Clearstream, Luxembourg participants in accordance with the relevant system’s rules and procedures.

A record of each payment made will be endorsed on the appropriate schedule to the Global Certificate by or on behalf of the Registrar and shall be prima facie evidence that payment has been made.

### 4. **Notices**

So long as all the Notes are represented by the Global Certificate and the Global Certificate is held on behalf of a clearing system, notices to Noteholders may be given by delivery of the relevant notice to that clearing system for communication by it to entitled Accountholders in substitution for notification as required by the Conditions. The Issuer shall also ensure that notices are duly given in a manner which complies with the rules and regulations of any stock exchange on which the Notes are for the time being listed.

## **5. Change of Registration of Title**

Registration of title to Notes in a name other than that of the Relevant Nominee will not be permitted unless Euroclear or Clearstream, Luxembourg, as appropriate, notifies the Issuer that it is unwilling or unable to continue as a clearing system in connection with the Global Certificate, and a successor clearing system approved by the Trustee is not appointed by the Issuer within 90 days after receiving such notice from Euroclear or Clearstream, Luxembourg. In these circumstances, title to a Note may be transferred into the names of holders notified by the Relevant Nominee in accordance with the Conditions, except that Certificates in respect of Notes so transferred may not be available until 21 days after the request for transfer is duly made.

The Registrar will not register title to the Notes in a name other than that of the Relevant Nominee for a period of 15 days preceding the due date for any payment of principal or interest in respect of the Notes.

## **6. Transfers**

Transfers of book-entry interests in the Notes will be effected through the records of Euroclear and Clearstream, Luxembourg and their respective participants in accordance with the rules and procedures of Euroclear and Clearstream, Luxembourg and their respective direct and indirect participants.

## TAXATION

*The statements herein regarding taxation are based on the laws in force as at the date of this Offering Circular and are subject to any changes in law occurring after such date, which changes could be made on a retroactive basis. The following summary does not purport to be a comprehensive description of all of the tax considerations that may be relevant to a decision to purchase, own or dispose of the Notes and does not purport to deal with the tax consequences applicable to all categories of investors, some of which (such as dealers in securities or commodities) may be subject to special rules. Persons considering the purchase of the Notes should consult their own tax advisers concerning the application of Hong Kong tax laws to their particular situations as well as any consequences of the purchase, ownership and disposition of the Notes arising under the laws of any other taxing jurisdiction.*

### **Hong Kong**

#### ***Withholding Tax***

No withholding tax is payable in Hong Kong in respect of payments of principal or interest on the Notes or in respect of any capital gains arising from the sale of the Notes.

#### ***Profits tax***

Hong Kong profits tax is chargeable on every person carrying on a trade, profession or business in Hong Kong in respect of profits arising in or derived from Hong Kong from such trade, profession or business (excluding profits arising from the sale of capital assets).

Under the Inland Revenue Ordinance (Cap. 112 of the Laws of Hong Kong) (the “**Inland Revenue Ordinance**”) as it is currently applied by the Inland Revenue Department, interest on the Notes may be deemed to be profits arising or derived from Hong Kong from a trade, profession or business carried on in Hong Kong in the following circumstances:

- (i) interest on the Notes is derived from Hong Kong and is received by or accrues to a company (other than a financial institution) carrying on a trade, profession or business in Hong Kong; or
- (ii) interest on the Notes is derived from Hong Kong and is received by or accrues to a person (other than a company), carrying on a trade, profession or business in Hong Kong and is in respect of the funds of that trade, profession or business; or
- (iii) interest on the Notes is received by or accrues to a financial institution (as defined in the Inland Revenue Ordinance) and arises through or from the carrying on by the financial institution of its business in Hong Kong.

Pursuant to the Exemption from Profits Tax (Interest Income) Order, interest income accruing to a person (other than a financial institution) on deposits (denominated in any currency and whether or not the deposit is evidenced by a certificate of deposit) placed with, *inter alia*, an authorised institution in Hong Kong (within the meaning of section 2 of the Banking Ordinance (Cap. 155 of the Laws of Hong Kong)) is exempt from the payment of Hong Kong profits tax. This exemption does not apply, however, to deposits that are used to secure or guarantee money borrowed in certain circumstances.

Sums derived from the sale, disposal or redemption of Notes will be subject to Hong Kong profits tax where received by or accrued to a person who carries on a trade, profession or business in Hong Kong and the sum has a Hong Kong source. The source of such sums will generally be determined by having regard to the manner in which the Notes are acquired and disposed.

Sums received by or accrued to a financial institution by way of gains or profits arising through or from the carrying on by the financial institution of its business in Hong Kong from the sale, disposal and redemption of Notes will be subject to profits tax.

### ***Stamp Duty***

No Hong Kong stamp duty will be chargeable upon the issue or subsequent transfer of a Note.

### **EU Savings Directive**

Under EC Council Directive 2003/48/EC on the taxation of savings income, Member States of the European Economic Area are required, from 1st July, 2005, to provide to the tax authorities of another Member State details of payments of interest (or similar income) paid by a person within its jurisdiction to an individual resident in that other Member State. However, for a transitional period, Belgium, Luxembourg and Austria are instead required (unless during that period they elect otherwise) to operate a withholding system in relation to such payments (the ending of such transitional period being dependent upon the conclusion of certain other agreements relating to information exchange with certain other countries). A number of non-EU countries and territories including Switzerland have agreed to adopt similar measures (a withholding system in the case of Switzerland) with effect from the same date.

On 15 September 2008 the European Commission issued a report to the Council of the European Union on the operation of the Directive, which included the Commission's advice on the need for changes to the Directive. On 13 November 2008 the European Commission published a more detailed proposal for amendments to the Directive, which included a number of suggested changes. The European Parliament approved an amended version of this proposal on 24 April 2009. If any proposed changes are made in relation to the Directive, they may amend or broaden the scope of requirements described above.

## SUBSCRIPTION AND SALE

Each of Goldman Sachs (Asia) L.L.C., The Hongkong and Shanghai Banking Corporation Limited and UBS AG, Hong Kong Branch (together the “**Joint Lead Managers**”) has, pursuant to a subscription agreement dated 28 October 2010 (the “**Subscription Agreement**”), severally agreed with the Issuer, subject to the satisfaction of certain conditions, to subscribe for the principal amount of the Notes set out opposite its name below as its underwriting commitment. Each Joint Lead Manager’s underwriting commitment may not represent the amount of Notes actually subscribed by each Joint Lead Manager.

<b>Joint Lead Manager</b>	<b>Underwriting Commitment</b>
Goldman Sachs (Asia) L.L.C.....	75,000,000
The Hongkong and Shanghai Banking Corporation Limited .....	75,000,000
UBS AG, Hong Kong Branch .....	<u>75,000,000</u>
	<u><u>225,000,000</u></u>

The Issuer has agreed to pay to the Joint Lead Managers a management and underwriting commission in connection with their underwriting commitments in accordance with the Subscription Agreement. The Issuer has also agreed to indemnify the Joint Lead Managers against certain liabilities incurred in connection with the issue of the Notes. In addition, the Issuer has agreed to reimburse the Joint Lead Managers for certain of their expenses in connection with the issue of the Notes. The Subscription Agreement provides that the obligations of the Joint Lead Managers are subject to certain conditions precedent, and entitles the Joint Lead Managers to terminate the Subscription Agreement in certain circumstances at any time up to the time when subscription moneys have been received and the Notes issued.

The Issuer has agreed that, from the date of this Offering Circular until the date falling 30 days after the Closing Date, it will ensure that no other international offering of foreign currency denominated debt instruments or debt securities (other than certificates of deposit and for the avoidance of doubt, any financial products offered in the ordinary course of its business by the Issuer to its customers) issued or guaranteed by the Issuer are either placed or syndicated, directly or on its behalf, in any manner which might, in the opinion of the Joint Lead Managers (following consultation with the Issuer, if practicable), have a detrimental effect on the successful placement of the Notes.

In connection with the offering of the Notes, the Joint Lead Managers may purchase and sell Notes in the open market. These transactions may include short sales, stabilising transactions and purchases to cover positions created by short sales. Short sales involve the sale by the Joint Lead Managers of a greater number of Notes than they are required to purchase in the offering. Stabilising transactions consist of certain bids or purchases made for the purpose of preventing or retarding a decline in the market price of the Notes while the offering is in progress.

The Joint Lead Managers may also impose a penalty bid. This occurs when a particular Joint Lead Manager repays to the Joint Lead Managers a portion of the underwriting discount received by it because the representatives have repurchased Notes sold by or for the account of such Joint Lead Manager in stabilising or short covering transactions.

These activities by the Joint Lead Managers may stabilise, maintain or otherwise affect the market price of the Notes. As a result, the price of the Notes may be higher than the price that otherwise might exist in the open market. If these activities are commenced, they may be discontinued by the Joint Lead Managers at any time. These transactions may be effected in the over-the-counter market or otherwise.

The Issuer has agreed to indemnify the Joint Lead Managers against certain liabilities, including liabilities under the Securities Act.

Certain of the Joint Lead Managers and their respective affiliates have, from time to time, performed, and may in the future perform, various financial advisory and investment banking services for the Issuer, for which they received or will receive customary fees and expenses.

### **United States**

The Notes have not been and will not be registered under the Securities Act, and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except in accordance with Regulation S or pursuant to any other exemption from the registration requirements of the Securities Act.

Each Joint Lead Manager has represented, warranted and agreed that it will not offer or sell the Notes (i) as part of their distribution at any time or (ii) otherwise until 40 days after the later of the commencement of the offering and the Closing Date (the distribution compliance period), except only in accordance with Rule 903 of Regulation S under the Securities Act, and it will have sent to each distributor, dealer or person receiving a selling concession, fee or other remuneration that purchases Notes from it during the distribution compliance period a confirmation or notice setting forth the restrictions on offers and sales of the Notes within the United States or to, or for the account or benefit of, U.S. persons.

Terms used in the paragraph above have the meanings given to them by Regulation S.

In addition, until 40 days after the commencement of the offering of the Notes, an offer or sale of Notes within the United States by a dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act.

### **United Kingdom**

Each Joint Lead Manager has represented and agreed that:

- (1) it has only communicated or caused to be communicated and will only communicate or cause to be communicated any invitation or inducement to engage in investment activity (within the meaning of section 21 of the Financial Services and Markets Act 2000 (the “FSMA”), received by it in connection with the issue or sale of any Notes in circumstances in which section 21(1) of the FSMA does not apply to the Issuer; and
- (2) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the Notes in, from or otherwise involving the United Kingdom.

### **Hong Kong**

Each Joint Lead Manager has represented and agreed that:

- (1) it has not offered or sold and will not offer or sell in Hong Kong, by means of any document, any Notes other than (a) to “professional investors” as defined in the SFO and any rules made under the SFO; or (b) in other circumstances which do not result in the document being a “prospectus” as defined in the Companies Ordinance (Cap. 32) (the “CO”) of Hong Kong or which do not constitute an offer to the public within the meaning of the CO; and
- (2) it has not issued or had in its possession for the purposes of issue, and will not issue or have in its possession for the purposes of issue, whether in Hong Kong or elsewhere, any

advertisement, invitation or document relating to the Notes, which is directed at, or the contents of which are likely to be accessed or read by, the public of Hong Kong (except if permitted to do so under the securities laws of Hong Kong) other than with respect to Notes which are or are intended to be disposed of only to persons outside Hong Kong or only to “professional investors” as defined in the SFO and any rules made under the SFO.

## Singapore

Each Joint Lead Manager has represented and agreed that this Offering Circular has not been registered as a prospectus with the Monetary Authority of Singapore. Each Joint Lead Manager has represented, warranted and agreed that the Notes may not be offered or sold or made the subject of an invitation for subscription or purchase nor may this Offering Circular and any other document or material in connection with the offer or sale, or invitation for subscription or purchase, of the Notes may not be circulated or distributed, nor may the Notes be offered or sold, or be made the subject of an invitation for subscription or purchase, whether directly or indirectly, to persons in Singapore other than (i) to an institutional investor under Section 274 of the Securities and Futures Act, Chapter 289 of Singapore (the “SFA”), (ii) to a relevant person pursuant to Section 275(1) of the SFA or any person pursuant to Section 275(1A) and in accordance with the conditions specified in Section 275 of the SFA or (iii) otherwise pursuant to, and in accordance with, the conditions of any other applicable provision of the SFA.

Where the Notes are subscribed or purchased under Section 275 by a relevant person which is:

- (a) a corporation (which is not an accredited investor) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or
- (b) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary is an accredited investor,

shares, debentures and units of shares and debentures of that corporation or the beneficiaries’ rights and interest in that trust shall not be transferable for 6 months after that corporation or that trust has acquired the Notes under Section 275 except:

- (1) to an institutional investor (for corporations, under Section 274 of the SFA) or to a relevant person defined in Section 275(2) of the SFA or any person pursuant to an offer that is made on terms that such shares, debentures and units of shares and debentures of that corporation or such rights and interest in that trust are acquired at a consideration of not less than \$200,000 Singapore dollars (or its equivalent in a foreign currency) for each transaction, whether such amount is to be paid for in cash or by exchange of securities or other assets, and in addition, for corporations, pursuant to Section 275(1A) and in accordance with the conditions specified in Section 275 of the SFA;
- (2) where no consideration is given for the transfer; or
- (3) where the transfer is by operation of law.

## Japan

The Notes have not been and will not be registered under the Financial Instruments and Exchange Act of Japan (Law No. 25 of 1948, as amended; the “FIEA”) and each Joint Lead Manager has represented and agreed that it will not offer or sell any Notes, directly or indirectly, in Japan or to, or for the benefit of, any resident of Japan (as defined under Item 5, Paragraph 1, Article 6 of the



Foreign Exchange and Foreign Trade Control Act (Law No. 228 of 1949, as amended)), or to others for re-offering or resale, directly or indirectly, in Japan or to, or for the benefit of, a resident of Japan except pursuant to an exemption from the registration requirements of, and otherwise in compliance with, the FIEA and any other applicable laws, regulations and ministerial guidelines of Japan.

## Italy

The offering of the Notes has not been registered pursuant to Italian securities legislation and, accordingly, each Joint Lead Manager has represented and agreed that no Notes may be offered, sold or delivered, nor may copies of the Offering Circular or of any other document relating to the Notes be distributed in the Republic of Italy, except:

- (i) to qualified investors (*investitori qualificati*), as defined pursuant to Article 100 of Legislative Decree No. 58 of 24 February 1998, as amended (the “**Financial Services Act**”) and Article 34-*ter*, first paragraph, letter (b) of CONSOB Regulation No. 11971 of 14 May 1999, as amended from time to time (“**Regulation No. 11971**”); or
- (ii) in other circumstances which are exempted from the rules on public offerings pursuant to Article 100 of the Financial Services Act and Article 34-*ter* of Regulation No. 11971.

Each Joint Lead Manager has represented and agreed that any offer, sale or delivery of the Notes or distribution of copies of the Offering Circular or any other document relating to the Notes in the Republic of Italy under (i) or (ii) above must be:

- (a) made by an investment firm, bank or financial intermediary permitted to conduct such activities in the Republic of Italy in accordance with the Financial Services Act, CONSOB Regulation No. 16190 of 29 October 2007 (as amended from time to time) and Legislative Decree No. 385 of 1 September 1993, as amended (the “**Banking Act**”); and
- (b) in compliance with Article 129 of the Banking Act, as amended, and the implementing guidelines of the Bank of Italy, as amended from time to time, pursuant to which the Bank of Italy may request information on the issue or the offer of securities in the Republic of Italy; and
- (c) in compliance with any other applicable laws and regulations or requirement imposed by CONSOB or other Italian authority.

## General

No action has been taken or will be taken by the Issuer or the Joint Lead Managers that would, or is intended to, permit a public offer of the Notes or possession or distribution of this Offering Circular or any other offering or publicity material relating to the Notes in any country or jurisdiction where action for any such purpose is required. Accordingly, each Joint Lead Manager has undertaken that it will not, directly or indirectly, offer or sell any Notes or have in its possession, distribute or publish any offering circular, prospectus, form of application, advertisement or other document or information in any country or jurisdiction except under circumstances that will result in compliance in all material respects with any applicable laws and regulations and all offers and sales of Notes by it will be made on the same terms.

Investors who purchase Notes from a Joint Lead Manager may be required to pay stamp taxes and other charges in accordance with the laws and practices of the country of purchase in addition to the issue price set forth on the cover page of this Offering Circular.

## GENERAL INFORMATION

1. **Clearing Systems:** The Notes have been accepted for clearance through Euroclear and Clearstream, Luxembourg with the Common Code of 055630216. The International Securities Identification Number (ISIN) for the Notes is XS0556302163.
2. **Listing of Notes:** Application has been made to the HKSE for the listing of, and permission to deal in, the Notes. It is expected that dealing will, if permission is granted to deal in and for the listing of the Notes on the HKSE, commence on or about 5 November 2010.
3. **Litigation:** Except as disclosed in this Offering Circular, neither the Issuer nor any of its subsidiaries is involved in any litigation or arbitration proceedings relating to claims or amounts which are material in the context of the issue of the Notes, nor is the Issuer or any of its subsidiaries aware that any such proceedings are pending or threatened.
4. **Authorisations:** The Issuer has obtained all necessary consents, approvals and authorisations as may be required in connection with the issue and performance of the Notes, including, but not limited to, approval by the HKMA. The issue of the Notes was authorised by a resolution of the Board of Directors of the Issuer passed on 14 October 2010. Listing of the Notes on the HKSE is conditional upon satisfaction of the requirements of that exchange, including execution of the Trust Deed and the agency agreement relating to the Notes (the “Agency Agreement”).
5. **No Material Adverse Change:** Except as disclosed in this Offering Circular, there has been no material adverse change in the financial or trading position of the Issuer and the Bank since 31 December 2009 and no material adverse change in the financial position or prospects of the Bank since 31 December 2009.
6. **Available Documents:** For so long as any of the Notes is outstanding, copies of the following documents may be inspected at a specified office of the Principal Paying Agent at 48th Floor, Cheung Kong Center, 2 Queen’s Road Central, Hong Kong and at the specified office of a Paying Agent:
  - (a) the Memorandum and Articles of Association of the Issuer;
  - (b) a copy of the auditor’s reports of Deloitte Touche Tohmatsu, the Issuer’s external auditor, and the audited consolidated financial statements of the Issuer as at and for the years ended 31 December 2009, 2008 and 2007;
  - (c) a copy of the independent review report of Deloitte Touche Tohmatsu, the Issuer’s external auditor, and the unaudited consolidated financial statements of the Issuer as at and for the six months ended 30 June 2010;
  - (d) copies of the most recent annual and interim reports (including the financial statements) published by the Issuer; and
  - (e) the Trust Deed and the Agency Agreement, each to be dated on or about 4 November 2010.

Copies of the auditor’s reports and the audited consolidated financial statements referred to above and the most recent annual audited consolidated financial statements (and audited unconsolidated statement of financial position) of the Issuer and interim unaudited consolidated financial statements published by the Issuer, will be made available free of charge at the specified office of the Principal Paying Agent at 48th Floor, Cheung Kong Center, 2 Queen’s Road Central, Hong Kong and at the specified office of a Paying Agent.

7. Auditor: The consolidated financial statements of the Issuer as at and for the years ended 31 December 2009 and 2008 included in this Offering Circular have been audited by Deloitte Touche Tohmatsu, Certified Public Accountants, as stated in the auditor's reports appearing in this Offering Circular in relation to such consolidated financial statements. The consolidated interim financial statements of the Issuer as at and for the six months ended 30 June 2010 included in this Offering Circular have not been audited by Deloitte Touche Tohmatsu. Deloitte Touche Tohmatsu have conducted a review of such interim financial statements in accordance with the Hong Kong Standard on Review Engagements 2410 issued by the HKICPA, as stated in its independent review report appearing in this Offering Circular in respect of such consolidated interim financial statements.

Deloitte Touche Tohmatsu has given and not withdrawn its written consent for the purposes of paragraph 8(2) of Appendix 1 Part C of the Listing Rules to the issue of this Offering Circular with references to its auditor's reports on the published annual consolidated financial statements of the Issuer for the years ended 31 December 2009 and 2008 and with references to Deloitte Touche Tohmatsu and to its independent review report on the published interim consolidated financial statements of the Issuer for the six months ended 30 June 2010, in each case in the form and context in which they appear.

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# **REPORT ON REVIEW OF INTERIM FINANCIAL INFORMATION TO THE BOARD OF DIRECTORS OF CHONG HING BANK LIMITED**

## **Introduction**

We have reviewed the interim financial information set out on pages F-3 to F-28 which comprises the condensed consolidated statement of financial position of Chong Hing Bank Limited (the “Bank”) and of its subsidiaries (collectively referred to as the “Group”) as of 30 June 2010 and the related condensed consolidated income statement, statement of comprehensive income, statement of changes in equity and statement of cash flows for the six-month period then ended and certain explanatory notes. The Main Board Listing Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of a report on interim financial information to be in compliance with the relevant provisions thereof and Hong Kong Accounting Standard “Interim Financial Reporting” 34 (“HKAS 34”) issued by the Hong Kong Institute of Certified Public Accountants. The directors are responsible for the preparation and presentation of this interim financial information in accordance with HKAS 34. Our responsibility is to express a conclusion on this interim financial information based on our review, and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

## **Scope of review**

We conducted our review in accordance with Hong Kong Standard on Review Engagements 2410, “Review of Interim Financial Information Performed by the Independent Auditor of the Entity” issued by the Hong Kong Institute of Certified Public Accountants. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

## **Conclusion**

Based on our review, nothing has come to our attention that causes us to believe that the interim financial information is not prepared, in all material respects, in accordance with HKAS 34.

**Deloitte Touche Tohmatsu**  
*Certified Public Accountants*  
Hong Kong

11 August 2010

**CONDENSED CONSOLIDATED INCOME STATEMENT**  
**FOR THE SIX MONTHS ENDED 30 JUNE 2010**

	Notes	Six months ended 30 June	
		2010	2009
		<i>HK\$'000</i>	<i>HK\$'000</i>
		<i>(Unaudited)</i>	<i>(Unaudited)</i>
Interest income .....		558,193	607,759
Interest expense .....		(146,725)	(211,229)
Net interest income .....	4	<u>411,468</u>	<u>396,530</u>
Fee and commission income .....		133,915	137,657
Fee and commission expense .....		(24,182)	(20,667)
Net fee and commission income .....	5	<u>109,733</u>	<u>116,990</u>
Net (loss) gain on financial assets at fair value through profit or loss .....	6	(5,270)	41,961
Other operating income .....	7	73,342	73,813
Operating expenses .....	8	(348,977)	(360,869)
		<u>240,296</u>	<u>268,425</u>
Impairment allowances on loans and advances			
- New allowances .....		(25,571)	(57,520)
- Amounts reversed .....		<u>5,835</u>	<u>3,389</u>
		(19,736)	(54,131)
Net gain (loss) on disposal of property and equipment .....		82	(4)
Net gain on disposal of available-for-sale securities .....		—	20,133
Net gain on disposal of and fair value adjustments on investment properties .....	17	6,630	1,374
Impairment loss on goodwill .....	9	—	(10,000)
Impairment loss on available-for-sale securities .....		<u>(1,818)</u>	<u>(44,292)</u>
Profit from operations .....		225,454	181,505
Share of profits of jointly controlled entities .....		<u>2,883</u>	<u>7,257</u>
Profit before taxation .....		<u>228,337</u>	<u>188,762</u>
Taxation	10		
- Hong Kong .....		(33,941)	(27,692)
- Overseas .....		(570)	(854)
- Deferred tax .....		<u>(434)</u>	<u>413</u>
		<u>(34,945)</u>	<u>(28,133)</u>
Profit for the period .....		<u>193,392</u>	<u>160,629</u>
Earnings per share, basic .....	11	<u>HK\$0.44</u>	<u>HK\$0.37</u>

**CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**  
**FOR THE SIX MONTHS ENDED 30 JUNE 2010**

	<b>Six months ended 30 June</b>	
	<b>2010</b>	<b>2009</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
	<i>(Unaudited)</i>	<i>(Unaudited)</i>
Profit for the period.....	<u>193,392</u>	<u>160,629</u>
Other comprehensive income		
Exchange differences arising on translation.....	2,347	(8)
Revaluation of available-for-sale securities:		
Revaluation gain (loss) on available-for-sale securities, net .....	3,491	(189)
Share of reserves of jointly controlled entities.....	126	4,454
Reclassification adjustment upon disposal and impairment.....	1,818	24,159
	5,435	28,424
Income tax relating to available-for-sale securities .....	<u>(1,184)</u>	<u>(6,168)</u>
Other comprehensive income for the period (net of tax).....	<u>6,598</u>	<u>22,248</u>
Total comprehensive income for the period .....	<u>199,990</u>	<u>182,877</u>
Total comprehensive income attributable to:		
Owners of the Bank.....	<u>199,990</u>	<u>182,877</u>



# CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 30 JUNE 2010

		30 June 2010	31 December 2009
	Notes	HK\$'000 (Unaudited)	HK\$'000 (Audited and restated)
<b>ASSETS</b>			
Cash and short-term funds .....	13	12,515,314	15,048,680
Placements with banks and other financial institutions maturing between one and twelve months .....		3,707,638	2,814,566
Derivative financial instruments .....	14	6,108	331
Financial assets at fair value through profit or loss .....	15	847,604	576,730
Available-for-sale securities .....	15	433,789	272,649
Held-to-maturity securities .....	15	15,934,387	16,954,466
Advances and other accounts .....	16	36,253,832	33,267,735
Tax recoverable .....		4,462	31,925
Interests in jointly controlled entities .....		120,747	119,418
Investment properties .....	17	105,970	103,199
Property and equipment .....	18	745,446	762,657
Prepaid lease payments for land .....	19	2,532	2,564
Goodwill .....		50,606	50,606
<b>Total assets</b> .....		<u>70,728,435</u>	<u>70,005,526</u>
<b>LIABILITIES</b>			
Deposits and balances of banks and other financial institutions .....		2,332,547	1,447,718
Deposits from customers .....	20	60,515,020	60,788,415
Derivative financial instruments .....	14	53,643	44,413
Other accounts and accruals .....		537,826	556,016
Current tax liabilities .....		17,151	15,671
Loan capital .....	21	971,546	967,199
Deferred tax liabilities .....	22	13,390	11,772
<b>Total liabilities</b> .....		<u>64,441,123</u>	<u>63,831,204</u>
<b>Shareholders' equity</b>			
Share capital .....		217,500	217,500
Reserves .....		6,069,812	5,956,822
<b>Shareholders' funds</b> .....		<u>6,287,312</u>	<u>6,174,322</u>
<b>Total liabilities and shareholders' equity</b> .....		<u>70,728,435</u>	<u>70,005,526</u>

**CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**  
**FOR THE SIX MONTHS ENDED 30 JUNE 2010**

		Share capital	Share premium	Goodwill	Investment revaluation reserve	General reserve	Translation reserve	Regulatory reserve	Retained profits	Total
	Note	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 1 January 2010 (audited) .....		217,500	1,542,817	(182)	55,328	1,388,500	8,048	287,000	2,675,311	6,174,322
Profit for the period.....		—	—	—	—	—	—	—	193,392	193,392
Other comprehensive income for the period...		—	—	—	4,251	—	2,347	—	—	6,598
Total comprehensive income for the period...		—	—	—	4,251	—	2,347	—	193,392	199,990
Final dividend for financial year 2009, paid .....	12	—	—	—	—	—	—	—	(87,000)	(87,000)
Earmark of retained profits as regulatory reserve .....		—	—	—	—	—	—	24,000	(24,000)	—
At 30 June 2010 (unaudited).....		<u>217,500</u>	<u>1,542,817</u>	<u>(182)</u>	<u>59,579</u>	<u>1,388,500</u>	<u>10,395</u>	<u>311,000</u>	<u>2,757,703</u>	<u>6,287,312</u>
At 1 January 2009 (audited) .....		217,500	1,542,817	(182)	13,352	1,388,500	7,524	307,000	2,480,113	5,956,624
Profit for the period.....		—	—	—	—	—	—	—	160,629	160,629
Other comprehensive income (expense) for the period.....		—	—	—	22,256	—	(8)	—	—	22,248
Total comprehensive income (expense) for the period.....		—	—	—	22,256	—	(8)	—	160,629	182,877
Final dividends for financial year 2008, paid .....	12	—	—	—	—	—	—	—	(21,750)	(21,750)
Earmark of retained profits as regulatory reserve .....		—	—	—	—	—	—	(19,000)	19,000	—
At 30 June 2009 (unaudited).....		<u>217,500</u>	<u>1,542,817</u>	<u>(182)</u>	<u>35,608</u>	<u>1,388,500</u>	<u>7,516</u>	<u>288,000</u>	<u>2,637,992</u>	<u>6,117,751</u>

The regulatory reserve is set up in compliance with the Hong Kong Monetary Authority (“HKMA”)’s requirements and is distributable to the shareholders of the Bank subject to consultation with the HKMA.

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

**CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS**  
**FOR THE SIX MONTHS ENDED 30 JUNE 2010**

	<b>Six months ended 30 June</b>	
	<b>2010</b>	<b>2009</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
	<i>(Unaudited)</i>	<i>(Unaudited and restated)</i>
<b>OPERATING ACTIVITIES</b>		
Profit before taxation .....	228,337	188,762
Adjustments for:		
Net (gain) loss on disposal of property and equipment .....	(82)	4
Net gain on disposal of available-for-sale securities .....	—	(20,133)
Impairment allowances on loans and advances .....	19,736	54,131
Impairment loss on goodwill .....	—	10,000
Impairment loss on available-for-sale securities .....	1,818	44,292
Dividend income from investments .....	(4,617)	(5,357)
Share of profits of jointly controlled entities .....	(2,883)	(7,257)
Net gain on disposal of and fair value adjustments on investment properties .....	(6,630)	(1,374)
Depreciation .....	27,353	24,464
Release of prepaid lease payments for land .....	32	35
Interest income from available-for-sale securities and held-to-maturity securities .....	(174,721)	(134,745)
Interest expense on loan capital .....	6,466	12,444
Exchange adjustments .....	5,753	44
Operating cash flows before movements in operating assets and liabilities .....	100,562	165,310
(Increase) decrease in operating assets:		
Money at call and short notice with original maturity over three months .....	1,970,103	(684,993)
Exchange fund bills with original maturity over three months .....	(138,342)	(536,264)
Placements with banks and other financial institutions with original maturity over three months .....	(963,204)	(33,714)
Financial assets at fair value through profit or loss .....	(270,874)	111,594
Bills receivable .....	(31,773)	36,925
Trade bills .....	(6,003)	39,735
Other advances to customers .....	(2,724,127)	123,068
Interest receivable and other accounts .....	160,851	(202,389)
Advances to banks and other financial institutions .....	(399,093)	1,160
Increase (decrease) in operating liabilities:		
Deposits and balances of banks and other financial institutions with original maturity over three months .....	1,066	100,018
Deposits from customers .....	(273,395)	336,049
Other accounts and accruals .....	(18,118)	97,109
Derivative financial instruments .....	3,453	22,298
Cash used in operations .....	(2,588,894)	(424,094)
Hong Kong Profits Tax paid .....	(4,998)	(5,034)
Overseas tax paid .....	(570)	(854)
<b>NET CASH USED IN OPERATING ACTIVITIES .....</b>	<b>(2,594,462)</b>	<b>(429,982)</b>

**CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS**  
**FOR THE SIX MONTHS ENDED 30 JUNE 2010**

	<b>Six months ended 30 June</b>	
	<b>2010</b>	<b>2009</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
	<i>(Unaudited)</i>	<i>(Unaudited and restated)</i>
<b>INVESTING ACTIVITIES</b>		
Interest received on available-for-sale securities and held-to-maturity securities .....	172,549	124,578
Dividends received on investments.....	4,617	5,357
Dividends received from jointly controlled entities .....	1,680	—
Purchase of available-for-sale securities.....	(157,649)	(6,427)
Purchase of held-to-maturity securities.....	(18,478,973)	(13,621,510)
Purchase of property and equipment.....	(10,096)	(7,226)
Proceeds from sale and redemption of available-for-sale securities.....	—	25,929
Proceeds from redemption of held-to-maturity securities .....	19,499,052	9,883,837
Proceeds from disposals of land.....	—	303
Proceeds from disposals of property and equipment .....	125	139
Proceeds from disposal of an investment property .....	635	—
<b>NET CASH GENERATED FROM (USED IN) INVESTING ACTIVITIES .....</b>	<b>1,031,940</b>	<b>(3,595,020)</b>
<b>FINANCING ACTIVITIES</b>		
Interest paid on loan capital.....	(5,978)	(12,485)
Dividends paid.....	(87,000)	(21,750)
<b>NET CASH USED IN FINANCING ACTIVITIES.....</b>	<b>(92,978)</b>	<b>(34,235)</b>
<b>NET DECREASE IN CASH AND CASH EQUIVALENTS .....</b>	<b>(1,655,500)</b>	<b>(4,059,237)</b>
<b>CASH AND CASH EQUIVALENTS AT 1 JANUARY.....</b>	<b>11,074,304</b>	<b>17,533,299</b>
<b>CASH AND CASH EQUIVALENTS AT 30 JUNE .....</b>	<b>9,418,804</b>	<b>13,474,062</b>
Represented by:		
Cash and balances with banks and other financial institutions .....	9,461,679	3,396,468
Money at call and short notice .....	2,498,001	13,488,971
Exchange fund bills .....	555,634	908,373
Placements with banks and other financial institutions maturing between one and twelve months .....	3,707,638	2,927,805
Deposits and balances of banks and other financial institutions .....	(2,332,547)	(2,123,625)
Less: Amounts with original maturity over three months.....	(4,471,601)	(5,123,930)
	<u>9,418,804</u>	<u>13,474,062</u>

**NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE SIX MONTHS ENDED 30 JUNE 2010**

**1. BASIS OF PREPARATION**

The condensed consolidated financial statements have been prepared in accordance with the applicable disclosure requirements of Appendix 16 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and with Hong Kong Accounting Standard 34 “Interim Financial Reporting”.

**2. PRINCIPAL ACCOUNTING POLICIES**

The condensed consolidated financial statements have been prepared under the historical cost convention except for investment properties and certain financial instruments that are measured at fair values.

The accounting policies adopted in the 2009 annual financial statements have been applied consistently to this interim financial information except for the following:

There are a number of new or revised standards, amendments and interpretations (“new or revised HKFRSs”) issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”), which are effective for the Group’s financial year beginning on 1 January 2010. Except as described below, the adoption of these new or revised HKFRSs had no material effect on the condensed consolidated financial statements of the Group for the current or prior accounting periods.

**Amendment to HKAS 17 Leases**

As part of Improvements to HKFRSs issued in 2009, HKAS 17 Leases has been amended in relation to the classification of leasehold land. Before the amendment to HKAS 17, lessees were required to classify leasehold land as operating leases and to present leasehold land as prepaid lease payments in the consolidated statement of financial position. The amendment has removed such a requirement. Instead, the amendment requires the classification of leasehold land to be based on the general principles set out in HKAS 17, that is, whether or not the risks and rewards incidental to ownership of a leased asset have been transferred substantially to the lessee.

In accordance with the transitional provisions set out in the amendment to HKAS 17 Leases, the Group reassessed the classification of unexpired leasehold land as at 1 January 2010 based on information which existed at the inception of these leases. Leasehold land which met finance lease classification have been reclassified from prepaid lease payments for land to property and equipment retrospectively, resulting in a reclassification of prepaid lease payments for land with carrying amount of HK\$324,980,000 as at 1 January 2009 and HK\$318,969,000 as at 31 December 2009 as property and equipment that are measured at cost model. The application of the amendment has had no significant financial impact to profit or loss for current or prior accounting periods.

The effect of changes in accounting policies described above on the financial position of the Group as at 31 December 2009 is as follows:

	As at 31 December 2009	Adjustments	As at 31 December 2009
	<i>HK\$'000</i> <i>(originally stated)</i>	<i>HK\$'000</i>	<i>HK\$'000</i> <i>(restated)</i>
Property and equipment.....	443,688	318,969	762,657
Prepaid lease payments for land .....	<u>321,533</u>	<u>(318,969)</u>	<u>2,564</u>

The effect of changes in accounting policies described above on the financial position of the Group as at 1 January 2009 is as follows:

	As at 1 January 2009	Adjustments	As at 1 January 2009
	<i>HK\$'000</i> <i>(originally stated)</i>	<i>HK\$'000</i>	<i>HK\$'000</i> <i>(restated)</i>
Property and equipment.....	469,724	324,980	794,704
Prepaid lease payments for land .....	<u>328,127</u>	<u>(324,980)</u>	<u>3,147</u>

The Group has not early applied the following new or revised standards, amendments and interpretations that have been issued but are not yet effective:

HKFRSs (Amendments)	Improvements to HKFRSs 2010 <sup>1</sup>
HKAS 24 (Revised)	Related party disclosures <sup>4</sup>
HKAS 32 (Amendment)	Classification of rights issues <sup>2</sup>
HKFRS 1 (Amendment)	Limited exemption from comparative HKFRS 7 disclosures for first-time adopters <sup>3</sup>
HKFRS 9	Financial instruments <sup>5</sup>
HK(IFRIC) - INT 14 (Amendment)	Prepayments of a minimum funding requirement <sup>4</sup>
HK(IFRIC) - INT 19	Extinguishing financial liabilities with equity instruments <sup>3</sup>

<sup>1</sup> Effective for annual periods beginning on or after 1 July 2010 and 1 January 2011, as appropriate

<sup>2</sup> Effective for annual periods beginning on or after 1 February 2010

<sup>3</sup> Effective for annual periods beginning on or after 1 July 2010

<sup>4</sup> Effective for annual periods beginning on or after 1 January 2011

<sup>5</sup> Effective for annual periods beginning on or after 1 January 2013

HKFRS 9 Financial Instruments introduces new requirements for the classification and measurement of financial assets and will be effective from 1 January 2013, with earlier application permitted. The Standard requires all recognised financial assets that are within the scope of HKAS 39 “Financial Instruments: Recognition and Measurement” to be measured at either amortised cost or fair value. Specifically, debt investments that (i) are held within a business model whose objective is to collect the contractual cash flows and (ii) have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost. All other debt investments and equity investments are measured at fair value. The application of HKFRS 9 might affect the classification and measurement of the Group’s financial assets.

The management of the Bank anticipates that the application of the other new or revised standards, amendments and interpretation will have no material impact on the results and the financial position of the Group.

### 3. SEGMENT INFORMATION

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

1. Corporate and retail banking
2. Treasury activities
3. Securities dealing
4. Others comprising investment holding, insurance, other investment advisory services and property investments.

The following is an analysis of the Group's revenue and results by operating segment for the periods under review:

**Six months ended 30 June 2010**

	<b>Corporate and retail banking</b>	<b>Treasury activities</b>	<b>Securities dealing</b>	<b>Others</b>	<b>Segment total</b>	<b>Eliminations</b>	<b>Consolidated</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Interest income from external customers .....	320,918	236,384	891	—	558,193	—	558,193
Interest expense to external customers .....	(139,833)	(6,892)	—	—	(146,725)	—	(146,725)
Inter-segment interest income (Note) .....	59,182	—	—	—	59,182	(59,182)	—
Inter-segment interest expense (Note) .....	—	(59,182)	—	—	(59,182)	59,182	—
Net interest income .....	240,267	170,310	891	—	411,468	—	411,468
Fees and commission income .....	50,654	—	83,261	—	133,915	—	133,915
Fees and commission expense .....	(23,745)	—	(437)	—	(24,182)	—	(24,182)
Net gain (loss) on financial assets at fair value through profit or loss .....	206	(5,286)	—	(190)	(5,270)	—	(5,270)
Other operating income .....	36,992	19,314	—	17,036	73,342	—	73,342
Total operating income (segment revenue) .....	304,374	184,338	83,715	16,846	589,273	—	589,273
Operating expenses .....	(210,160)	(12,684)	(28,322)	(5,107)	(256,273)	—	(256,273)
Impairment allowances on loans and advances .....	(19,736)	—	—	—	(19,736)	—	(19,736)
Net gain on disposal of property and equipment ....	82	—	—	—	82	—	82
Net gain on disposal of and fair value adjustments on investment properties .....	—	—	—	6,630	6,630	—	6,630
Impairment loss on available-for-sale securities .....	—	(1,818)	—	—	(1,818)	—	(1,818)
Segment profit .....	<u>74,560</u>	<u>169,836</u>	<u>55,393</u>	<u>18,369</u>	<u>318,158</u>	<u>—</u>	<u>318,158</u>
Unallocated expenses .....							(92,704)
Share of profits of jointly controlled entities .....							2,883
Profit before taxation .....							<u>228,337</u>

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



As at 30 June 2010

	Corporate and retail banking	Treasury activities	Securities dealing	Others	Consolidated
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Segment assets.....	46,026,309	23,726,979	182,161	359,877	70,295,326
Interests in jointly controlled entities.....					120,747
Unallocated assets.....					312,362
Consolidated total assets.....					70,728,435
Segment liabilities .....	60,652,713	3,360,784	110,226	42,284	64,166,007
Unallocated liabilities .....					275,116
Consolidated total liabilities .....					64,441,123

Other information

Six months ended 30 June 2010

	Corporate and retail banking	Treasury activities	Securities dealing	Others	Segment total	Unallocated	Consolidated
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Capital additions.....	3,676	124	533	11	4,344	5,752	10,096
Depreciation .....	15,651	828	2,813	255	19,547	7,806	27,353
Release of prepaid lease payments for land.....	32	—	—	—	32	—	32

Six months ended 30 June 2009

	Corporate and retail banking	Treasury activities	Securities dealing	Others	Segment total	Eliminations	Consolidated
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Interest income from external customers .....	352,141	255,216	402	—	607,759	—	607,759
Interest expense to external customers .....	(196,126)	(15,103)	—	—	(211,229)	—	(211,229)
Inter-segment interest income (Note) .....	85,702	—	—	—	85,702	(85,702)	—
Inter-segment interest expense (Note) .....	—	(85,702)	—	—	(85,702)	85,702	—
Net interest income .....	241,717	154,411	402	—	396,530	—	396,530
Fees and commission income .....	35,650	—	92,810	9,197	137,657	—	137,657
Fees and commission expense .....	(19,570)	—	(333)	(764)	(20,667)	—	(20,667)
Net gain on financial assets at fair value through profit or loss .....	—	41,567	—	394	41,961	—	41,961
Other operating income .....	33,416	16,697	(45)	23,745	73,813	—	73,813
Total operating income (segment revenue) .....	291,213	212,675	92,834	32,572	629,294	—	629,294
Operating expenses .....	(204,410)	(13,179)	(25,087)	(11,638)	(254,314)	—	(254,314)
Impairment allowances on loans and advances .....	(54,131)	—	—	—	(54,131)	—	(54,131)
Net loss on disposal of property and equipment ....	(4)	—	—	—	(4)	—	(4)
Net gain on disposal of available-for-sale securities .....	—	—	—	20,133	20,133	—	20,133
Net gain on disposal of and fair value adjustments on investment properties .....	—	—	—	1,374	1,374	—	1,374
Impairment loss on goodwill ..	—	—	—	(10,000)	(10,000)	—	(10,000)
Impairment loss on available-for-sale securities .....	—	(44,292)	—	—	(44,292)	—	(44,292)
Segment profit .....	32,668	155,204	67,747	32,441	288,060	—	288,060
Unallocated expenses .....							(106,555)
Share of profits of jointly controlled entities .....							7,257
Profit before taxation .....							188,762

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

As at 31 December 2009

	Corporate and retail banking	Treasury activities	Securities dealing	Others	Consolidated
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Segment assets .....	37,788,842	31,059,086	304,754	402,153	69,554,835
Interests in jointly controlled entities .....					119,418
Unallocated assets .....					331,273
Consolidated total assets .....					70,005,526
Segment liabilities .....	60,987,105	2,464,100	240,003	41,854	63,733,062
Unallocated liabilities .....					98,142
Consolidated total liabilities .....					63,831,204

Other information

Six months ended 30 June 2009

	Corporate and retail banking	Treasury activities	Securities dealing	Others	Segment total	Unallocated	Consolidated
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Capital additions .....	4,490	49	1,272	108	5,919	1,307	7,226
Depreciation (restated) .....	15,096	695	541	431	16,763	7,701	24,464
Release of prepaid lease payments for land (restated) .....	35	—	—	—	35	—	35

Segment profit represents the profit earned by each segment without allocation of central administration costs and share of results of jointly-controlled entities. 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 amounts to 10% of the Group's total operating income.

Geographical information

Geographical information is analysed by the Group based on the locations of the principal operations of the branches and subsidiary companies responsible for reporting the results or booking the assets.

	Six months ended 30 June 2010		As at 30 June 2010			
	Total operating income	Profit before taxation	Total assets	Total liabilities	Total contingent liabilities and commitments	Capital expenditure during the period
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Hong Kong .....	575,000	222,778	68,956,561	63,408,164	17,250,043	9,970
Macau and Shantou .....	7,526	1,605	1,166,055	808,551	140,881	93
America .....	6,747	3,954	605,819	224,408	53,328	33
Total .....	589,273	228,337	70,728,435	64,441,123	17,444,252	10,096

	Six months ended 30 June 2009		As at 31 December 2009			
	Total operating income	Profit before taxation	Total assets	Total liabilities	Total contingent liabilities and commitments	Capital expenditure during the year
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Hong Kong.....	608,971	176,626	68,439,215	62,917,441	15,331,875	20,682
Macau and Shantou .....	13,085	7,622	1,108,307	753,065	174,768	530
America.....	7,238	4,514	458,004	160,698	79,603	114
Total.....	<u>629,294</u>	<u>188,762</u>	<u>70,005,526</u>	<u>63,831,204</u>	<u>15,586,246</u>	<u>21,326</u>

#### 4. NET INTEREST INCOME

	Six months ended 30 June	
	2010	2009
	HK\$'000	HK\$'000
Interest income		
Short-term funds and placements .....	64,252	119,087
Investments in securities.....	175,191	139,093
Loans and advances .....	<u>318,750</u>	<u>349,579</u>
	<u>558,193</u>	<u>607,759</u>
Interest expense		
Deposits and balances from banks and customers.....	(140,259)	(198,785)
Loan capital in issue.....	<u>(6,466)</u>	<u>(12,444)</u>
	<u>(146,725)</u>	<u>(211,229)</u>
Net interest income.....	<u>411,468</u>	<u>396,530</u>
Included within interest income		
Interest income on impaired loans and advances .....	<u>415</u>	<u>1,707</u>

Included within interest income and interest expense are HK\$557,451,000 (2009: HK\$603,411,000) and HK\$146,725,000 (2009: HK\$211,229,000) earned and incurred from financial assets and financial liabilities that are not at fair value through profit or loss, respectively.

#### 5. NET FEE AND COMMISSION INCOME

	Six months ended 30 June	
	2010	2009
	HK\$'000	HK\$'000
Fees and commission income		
Securities dealings .....	83,261	92,810
Credit lines.....	6,170	4,374
Trade finance .....	4,890	5,723
Credit card services .....	25,901	21,917
Agency services.....	8,532	9,197
Others.....	<u>5,161</u>	<u>3,636</u>
Total fees and commission income .....	133,915	137,657
Less: Fees and commission expense .....	<u>(24,182)</u>	<u>(20,667)</u>
Net fees and commission income .....	<u>109,733</u>	<u>116,990</u>

## 6. NET (LOSS) GAIN ON FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

	Six months ended 30 June	
	2010	2009
	HK\$'000	HK\$'000
Net (loss) gain on financial assets at fair value through profit or loss		
- Designated at fair value through profit or loss .....	(5,049)	64,215
- Held for trading .....	17	(22,254)
Net losses on fair value hedge .....	(238)	—
	<u>(5,270)</u>	<u>41,961</u>

## 7. OTHER OPERATING INCOME

	Six months ended 30 June	
	2010	2009
	HK\$'000	HK\$'000
Dividend income .....	4,617	5,357
- Listed investments .....	2,337	3,075
- Unlisted investments .....	2,280	2,282
Net gains on dealing in foreign currencies .....	19,314	16,697
Net rental income .....	6,583	5,972
- Gross rents from properties .....	7,024	6,657
- Less: Outgoings .....	(441)	(685)
Safe deposit box rentals .....	12,233	12,208
Insurance underwriting profit .....	5,855	7,047
Other banking services income .....	22,571	19,422
Others .....	2,169	7,110
	<u>73,342</u>	<u>73,813</u>

## 8. OPERATING EXPENSES

	Six months ended 30 June	
	2010	2009
	HK\$'000	HK\$'000
Auditor's remuneration .....	1,850	1,751
Staff costs:		(restated)
Salaries and other costs .....	189,673	190,181
Retirement benefits scheme contributions .....	10,721	11,601
Total staff costs .....	200,394	201,782
Depreciation .....	27,353	24,464
Release of prepaid lease payments for land .....	32	35
Premises and equipment expenses, excluding depreciation and release of prepaid lease payments for land		
Rentals and rates for premises .....	21,634	20,998
Others .....	9,305	8,660
Other operating expenses .....	88,409	103,179
	<u>348,977</u>	<u>360,869</u>

## 9. IMPAIRMENT LOSS ON GOODWILL

For the six-month period ended 30 June 2010, the management has reviewed the goodwill for impairment testing purposes. The review comprises of a comparison of the carrying amount and the value in use of an acquired subsidiary (the cash-generating unit) to which the goodwill has been allocated. The acquired subsidiary is involved in insurance business.

The value in use calculations primarily use cash flow projections based on five-year financial budgets approved by management and with a stable growth beyond the five-year projection period. There are a number of assumptions and estimates involved for the preparation of cash flow projections for the period covered by the approved budget. Key assumptions include a growth rate of 4% (2009: 0%) in revenues and selection of discount rates of 12% (2009: 12%).

The management of the Group determines that there is no impairment loss on the goodwill for the six-month period ended 30 June 2010.

A goodwill impairment loss of HK\$10,000,000, representing the excess of the carrying amount above the value in use of the cash generating unit described above, was recognised for the six-month period ended 30 June 2009.

## 10. TAXATION

Hong Kong Profits Tax is calculated at 16.5% (2009: 16.5%) of the estimated assessable profit for the period.

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

## 11. EARNINGS PER SHARE

The calculation of basic earnings per share is based on the profit attributable to owners of the Bank of HK\$193,392,000 (2009: HK\$160,629,000) and on 435,000,000 (2009: 435,000,000) ordinary shares in issue during the period.

There is no potential dilutive ordinary shares in issue during both periods.

## 12. DIVIDENDS

On 29 April 2010, a dividend of HK\$0.20 per share totalling HK\$87,000,000 was paid to shareholders as the final dividend for 2009.

On 30 April 2009, a dividend of HK\$0.05 per share totalling HK\$21,750,000 was paid to shareholders as the final dividend for 2008.

The directors have determined that a total amount of interim dividend in respect of the financial year ending 31 December 2010 of HK\$43,500,000 (2009: HK\$34,800,000) at a rate of HK\$0.10 (2009: HK\$0.08) per share should be paid to the shareholders of the Bank whose names appear in the Register of Members on 22 September 2010.

## 13. CASH AND SHORT-TERM FUNDS

	30 June 2010	31 December 2009
	<i>HK\$'000</i>	<i>HK\$'000</i>
Cash and balances with banks and other financial institutions .....	9,461,679	4,427,240
Money at call and short notice.....	2,498,001	6,704,160
Exchange fund bills .....	555,634	3,917,280
	<u>12,515,314</u>	<u>15,048,680</u>

#### 14. DERIVATIVE FINANCIAL INSTRUMENTS

30 June 2010			
	Notional amount	Fair values	
		Assets	Liabilities
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Derivatives held for trading:			
- Foreign currency related contracts .....	95,363	1,191	1,723
- Interest rate swaps .....	580,000	4,917	44,191
Derivatives held for hedging:			
- Interest rate swaps .....	210,203	—	7,729
		<u>6,108</u>	<u>53,643</u>
31 December 2009			
	Notional amount	Fair values	
		Assets	Liabilities
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Derivatives held for trading:			
- Foreign currency related contracts .....	57,830	331	131
- Interest rate swaps .....	535,100	—	44,154
Derivatives held for hedging:			
- Interest rate swaps .....	54,285	—	128
		<u>331</u>	<u>44,413</u>



# 15. INVESTMENTS IN SECURITIES

	Financial assets at fair value through profit or loss		Available- for-sale securities	Held-to- maturity securities	Total
	Held for trading	Designated at fair value			
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>30 June 2010</b>					
Equity securities:					
Listed in Hong Kong.....	409	—	138,831	—	139,240
Listed overseas.....	—	—	7,074	—	7,074
	409	—	145,905	—	146,314
Unlisted .....	—	—	35,183	—	35,183
	409	—	181,088	—	181,497
Debt securities:					
Certificates of deposits.....	—	—	—	707,571	707,571
Structured products .....	—	847,195	—	—	847,195
Other debt securities - Unlisted.....	—	—	252,701	15,226,816	15,479,517
	—	847,195	252,701	15,934,387	17,034,283
Total:					
Listed in Hong Kong.....	409	—	138,831	—	139,240
Listed overseas.....	—	—	7,074	—	7,074
Unlisted .....	—	847,195	287,884	15,934,387	17,069,466
	409	847,195	433,789	15,934,387	17,215,780
Market value of listed securities:					
Listed in Hong Kong.....	409	—	138,831	—	139,240
Listed overseas.....	—	—	7,074	—	7,074
	409	—	145,905	—	146,314
As analysed by issuing entities:					
Central government and central banks .....	—	—	—	180,447	180,447
Public sector entities .....	—	—	56,858	57,268	114,126
Banks and other financial institutions.....	3	150,178	54,897	13,920,454	14,125,532
Corporate entities .....	406	697,017	315,344	1,776,218	2,788,985
Others .....	—	—	6,690	—	6,690
	409	847,195	433,789	15,934,387	17,215,780

	Financial assets at fair value through profit or loss				
	Held for trading	Designated at fair value	Available- for-sale securities	Held-to- maturity securities	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>31 December 2009</b>					
Equity securities:					
Listed in Hong Kong.....	140	—	135,287	—	135,427
Listed overseas.....	—	—	6,912	—	6,912
	140	—	142,199	—	142,339
Unlisted .....	—	—	36,902	—	36,902
	140	—	179,101	—	179,241
Debt securities:					
Certificates of deposits.....	—	—	—	347,510	347,510
Structured products .....	—	576,590	—	—	576,590
Other debt securities - Unlisted.....	—	—	93,548	16,606,956	16,700,504
	—	576,590	93,548	16,954,466	17,624,604
Total:					
Listed in Hong Kong.....	140	—	135,287	—	135,427
Listed overseas.....	—	—	6,912	—	6,912
Unlisted .....	—	576,590	130,450	16,954,466	17,661,506
	140	576,590	272,649	16,954,466	17,803,845
Market value of listed securities:					
Listed in Hong Kong.....	140	—	135,287	—	135,427
Listed overseas.....	—	—	6,912	—	6,912
	140	—	142,199	—	142,339
As analysed by issuing entities:					
Central government and central banks .....	—	—	—	182,203	182,203
Public sector entities .....	—	—	54,947	56,328	111,275
Banks and other financial institutions.....	45	82,389	54,067	14,766,614	14,903,115
Corporate entities .....	95	494,201	155,225	1,949,321	2,598,842
Others .....	—	—	8,410	—	8,410
	140	576,590	272,649	16,954,466	17,803,845

The fair value of held-to-maturity securities as at 30 June 2010 amounted to HK\$15,979,761,000 (31 December 2009: HK\$16,975,145,000).

Included in available-for-sale securities (other debt securities-unlisted) are financial instruments issued by structured investment vehicles with gross investment cost of approximately HK\$116,748,000 (31 December 2009: HK\$116,294,000). Impairment losses of HK\$115,749,000 (31 December 2009: HK\$115,018,000) has been recognised for these investments.

Certain held-to-maturity certificates of deposit of approximately HK\$15,571,000 (31 December 2009: HK\$15,510,000) held by the San Francisco Branch of the Bank have been pledged to the State of California of the United States of America in compliance with the requirements of the California Financial Code.

## 16. ADVANCES AND OTHER ACCOUNTS

	<b>30 June 2010</b>	<b>31 December 2009</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Advances to customers		
Bills receivable.....	334,759	302,986
Trade bills .....	124,261	118,258
Other advances to customers.....	35,093,684	32,372,335
	35,552,704	32,793,579
Interest receivable.....	103,839	90,429
Impairment allowances		
- Individually assessed.....	(33,563)	(25,905)
- Collectively assessed.....	(117,435)	(108,096)
	35,505,545	32,750,007
Advances to banks and other financial institutions.....	513,776	114,683
	36,019,321	32,864,690
Other accounts .....	234,511	403,045
	<u>36,253,832</u>	<u>33,267,735</u>

Included in the “Advances to banks and other financial institutions” of the Group of HK\$125,113,000 (31 December 2009: HK\$114,683,000) are amounts placed as reserve funds with financial institutions in the People’s Republic of China by the Shantou Branch of the Bank in compliance with the requirements of Regulations Governing Foreign Financial Institutions of the People’s Republic of China.

Included in the “other accounts” of the Group is retirement benefits scheme assets of HK\$52,000 (31 December 2009: HK\$52,000) due to the excess of scheme assets over defined benefit obligations.

Details of the impaired loans are as follows:

	<b>30 June 2010</b>	<b>31 December 2009</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Gross impaired loans .....	43,692	53,707
Less: Impairment allowances under individual assessment.....	(33,563)	(25,905)
Net impaired loans.....	<u>10,129</u>	<u>27,802</u>
Gross impaired loans as a percentage of gross advances to customers.....	<u>0.12%</u>	<u>0.16%</u>
Market value of collateral pledged.....	<u>92,184</u>	<u>103,950</u>

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.

## 17. INVESTMENT PROPERTIES

	30 June 2010	31 December 2009
	<i>HK\$'000</i>	<i>HK\$'000</i>
At 1 January .....	103,199	129,801
Disposals .....	(1,060)	(32,000)
Net increase in fair value recognised in the consolidated income statement.....	3,500	5,148
Exchange difference.....	331	250
At 30 June/31 December .....	<u>105,970</u>	<u>103,199</u>

Net gain on disposal and fair value adjustments on investment properties:

	Six months ended 30 June	
	2010	2009
	<i>HK\$'000</i>	<i>HK\$'000</i>
Net gain on disposal of investment properties .....	3,130	—
Net gain on fair value adjustments on investment properties .....	3,500	1,374
	<u>6,630</u>	<u>1,374</u>

Investment properties owned by the Group were revalued at 30 June 2010 on an open market value basis by Vigers Hong Kong Limited, independent professionally qualified valuers. The market value is mainly arrived at by reference to comparable market transactions for similar properties.

## 18. PROPERTY AND EQUIPMENT

	Leasehold land	Buildings	Equipment	Total
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
<b>COST</b>				
At 1 January 2010 .....	396,264	316,663	498,720	1,211,647
Additions .....	—	—	10,096	10,096
Disposals .....	—	—	(2,434)	(2,434)
Exchange adjustments .....	—	—	94	94
At 30 June 2010 .....	<u>396,264</u>	<u>316,663</u>	<u>506,476</u>	<u>1,219,403</u>
<b>ACCUMULATED DEPRECIATION</b>				
At 1 January 2010 .....	77,295	40,746	330,949	448,990
Provided for the period .....	3,003	3,320	21,030	27,353
Eliminated on disposals .....	—	—	(2,391)	(2,391)
Exchange adjustments .....	—	—	5	5
At 30 June 2010 .....	<u>80,298</u>	<u>44,066</u>	<u>349,593</u>	<u>473,957</u>
<b>CARRYING AMOUNTS</b>				
At 30 June 2010 .....	<u>315,966</u>	<u>272,597</u>	<u>156,883</u>	<u>745,446</u>

	<b>Leasehold land</b>	<b>Buildings</b>	<b>Equipment</b>	<b>Total</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
	<i>(restated)</i>			<i>(restated)</i>
<b>COST</b>				
At 1 January 2009, as originally stated .....	—	316,883	477,734	794,617
Adjustment on application of amendment to HKAS 17 .....	396,264	—	—	396,264
At 1 January 2009, as restated .....	396,264	316,883	477,734	1,190,881
Additions .....	—	—	21,326	21,326
Disposals .....	—	(220)	(344)	(564)
Exchange adjustments .....	—	—	4	4
At 31 December 2009, as restated .....	396,264	316,663	498,720	1,211,647
<b>ACCUMULATED DEPRECIATION</b>				
At 1 January 2009, as originally stated .....	—	34,204	290,689	324,893
Adjustment on application of amendment to HKAS 17 .....	71,284	—	—	71,284
At 1 January 2009, as restated .....	71,284	34,204	290,689	396,177
Provided for the year .....	6,011	6,624	40,589	53,224
Eliminated on disposals .....	—	(82)	(329)	(411)
At 31 December 2009, as restated .....	77,295	40,746	330,949	448,990
<b>CARRYING AMOUNTS</b>				
At 31 December 2009, as restated .....	<u>318,969</u>	<u>275,917</u>	<u>167,771</u>	<u>762,657</u>

#### 19. PREPAID LEASE PAYMENTS FOR LAND

	<b>HK\$'000</b>
	<i>(restated)</i>
At 1 January 2009, as originally stated .....	328,127
Adjustment on application of amendment to HKAS 17 .....	(324,980)
At 1 January 2009, as restated .....	3,147
Release to profit or loss .....	(64)
Disposal .....	(519)
At 31 December 2009, as restated .....	2,564
Release to profit or loss .....	(32)
At 30 June 2010 .....	<u>2,532</u>

#### 20. DEPOSITS FROM CUSTOMERS

	<b>30 June 2010</b>	<b>31 December 2009</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Demand deposits and current accounts .....	4,283,118	4,790,745
Savings deposits .....	19,134,870	19,644,533
Time, call and notice deposits .....	<u>37,097,032</u>	<u>36,353,137</u>
	<u>60,515,020</u>	<u>60,788,415</u>

## 21. LOAN CAPITAL

	<b>30 June 2010</b>	<b>31 December 2009</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
US\$125 million callable floating rate subordinated notes due 2016.....	<u>971,546</u>	<u>967,199</u>

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

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

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

## 22. DEFERRED TAXATION

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

	<b>Accelerated tax depreciation</b>	<b>Collectively assessed impairment allowance</b>	<b>Investment properties</b>	<b>Revaluation of available- for-sale securities</b>	<b>Total</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 1 January 2010.....	15,533	(19,645)	8,919	6,965	11,772
(Credit) charge to profit or loss for the period .....	(1,087)	1,042	479	—	434
Charge to other comprehensive income for the period.....	—	—	—	1,184	1,184
At 30 June 2010.....	<u>14,446</u>	<u>(18,603)</u>	<u>9,398</u>	<u>8,149</u>	<u>13,390</u>
At 1 January 2009.....	15,645	(18,428)	12,557	(3,491)	6,283
Credit to profit or loss for the year .....	(112)	(1,217)	(3,638)	—	(4,967)
Charge to other comprehensive income for the year.....	—	—	—	10,456	10,456
At 31 December 2009.....	<u>15,533</u>	<u>(19,645)</u>	<u>8,919</u>	<u>6,965</u>	<u>11,772</u>

## 23. MATURITY PROFILES

The maturity profile of assets and liabilities shown on the condensed consolidated statement of financial position, based on the remaining period at the end of the reporting period to the contractual maturity date in accordance with the guideline issued by the Hong Kong Monetary Authority, is shown below:

	Repayable on demand	Repayable within 1 month (except those repayable on demand)	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
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>At 30 June 2010</b>								
<b>Assets</b>								
Cash and short-term funds .....	9,272,023	2,535,163	454,441	253,687	—	—	—	12,515,314
Placements with banks and other financial institutions .....	—	—	1,324,218	2,383,420	—	—	—	3,707,638
Derivative financial instruments .....	—	67	559	565	4,917	—	—	6,108
Financial assets at fair value through profit or loss								
- Held for trading ....	—	—	—	—	—	—	409	409
- Designated at fair value .....	—	—	—	—	817,331	29,864	—	847,195
Available-for-sale securities .....	—	—	—	—	251,702	999	181,088	433,789
Held-to-maturity securities .....	—	4,822,391	1,410,151	3,137,523	6,564,322	—	—	15,934,387
Advances to customers .	1,386,202	2,450,901	2,851,138	6,710,862	12,024,857	10,048,822	79,922	35,552,704
Advances to banks and other financial institutions .....	13,245	60,752	420,204	19,575	—	—	—	513,776
Other assets .....	176,195	72,428	36,439	52,260	643	—	879,150	1,217,115
<b>Total assets</b> .....	<u>10,847,665</u>	<u>9,941,702</u>	<u>6,497,150</u>	<u>12,557,892</u>	<u>19,663,772</u>	<u>10,079,685</u>	<u>1,140,569</u>	<u>70,728,435</u>
<b>Liabilities</b>								
Deposits and balances of banks and other financial institutions .....	19,100	2,313,447	—	—	—	—	—	2,332,547
Deposits from customers .....	23,436,555	24,660,745	9,233,013	3,173,419	11,288	—	—	60,515,020
Derivative financial instruments .....	—	76	198	26,835	26,534	—	—	53,643
Loan capital .....	—	—	—	—	—	971,546	—	971,546
Other liabilities .....	437,396	24,990	27,049	50,912	28,020	—	—	568,367
<b>Total liabilities</b> .....	<u>23,893,051</u>	<u>26,999,258</u>	<u>9,260,260</u>	<u>3,251,166</u>	<u>65,842</u>	<u>971,546</u>	<u>—</u>	<u>64,441,123</u>
Net position - total assets and liabilities .....	<u>(13,045,386)</u>	<u>(17,057,556)</u>	<u>(2,763,110)</u>	<u>9,306,726</u>	<u>19,597,930</u>	<u>9,108,139</u>	<u>1,140,569</u>	<u>6,287,312</u>
Of which certificates of deposits included in:								
Held-to-maturity securities .....	<u>—</u>	<u>52,000</u>	<u>—</u>	<u>375,571</u>	<u>280,000</u>	<u>—</u>	<u>—</u>	<u>707,571</u>
Of which debt securities included in:								
Financial assets at fair value through profit or loss								
- Designated at fair value .....	—	—	—	—	817,331	29,864	—	847,195
Available-for-sale securities .....	—	—	—	—	251,702	999	—	252,701
Held-to-maturity securities .....	—	4,822,391	1,410,151	3,137,523	6,564,322	—	—	15,934,387
	<u>—</u>	<u>4,822,391</u>	<u>1,410,151</u>	<u>3,137,523</u>	<u>7,633,355</u>	<u>30,863</u>	<u>—</u>	<u>17,034,283</u>

	Repayable on demand	Repayable within 1 month (except those repayable on demand)	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
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>At 31 December 2009</b>								
<b>Assets</b>								
Cash and short-term funds .....	4,204,022	10,409,504	235,383	199,771	—	—	—	15,048,680
Placements with banks and other financial institutions.....	—	—	652,017	2,162,549	—	—	—	2,814,566
Derivative financial instruments .....	—	175	119	37	—	—	—	331
Financial assets at fair value through profit or loss .....								
- Held for trading .....	—	—	—	—	—	—	140	140
- Designated at fair value .....	—	—	—	88,276	488,314	—	—	576,590
Available-for-sale securities .....	—	—	—	—	92,272	1,276	179,101	272,649
Held-to-maturity securities .....	—	4,142,804	1,431,063	4,141,778	7,238,821	—	—	16,954,466
Advances to customers...	1,456,020	2,234,769	1,501,287	4,773,751	13,014,912	9,628,458	184,382	32,793,579
Advances to banks and other financial institutions.....	9,958	60,466	30,961	13,298	—	—	—	114,683
Other assets .....	341,785	86,790	22,146	67,812	703	—	910,606	1,429,842
<b>Total assets</b> .....	<u>6,011,785</u>	<u>16,934,508</u>	<u>3,872,976</u>	<u>11,447,272</u>	<u>20,835,022</u>	<u>9,629,734</u>	<u>1,274,229</u>	<u>70,005,526</u>
<b>Liabilities</b>								
Deposits and balances of banks and other financial institutions ..	10,218	1,437,500	—	—	—	—	—	1,447,718
Deposits from customers .....	24,492,361	23,282,401	8,369,759	4,487,837	156,057	—	—	60,788,415
Derivative financial instruments .....	—	296	20	1,373	42,724	—	—	44,413
Loan capital .....	—	—	—	—	—	967,199	—	967,199
Other liabilities .....	462,336	20,846	23,489	48,633	28,155	—	—	583,459
<b>Total liabilities</b> .....	<u>24,964,915</u>	<u>24,741,043</u>	<u>8,393,268</u>	<u>4,537,843</u>	<u>226,936</u>	<u>967,199</u>	<u>—</u>	<u>63,831,204</u>
Net position - total assets and liabilities .....	<u>(18,953,130)</u>	<u>(7,806,535)</u>	<u>(4,520,292)</u>	<u>6,909,429</u>	<u>20,608,086</u>	<u>8,662,535</u>	<u>1,274,229</u>	<u>6,174,322</u>
Of which certificates of deposits included in:								
Held-to-maturity securities .....	<u>—</u>	<u>—</u>	<u>—</u>	<u>67,510</u>	<u>280,000</u>	<u>—</u>	<u>—</u>	<u>347,510</u>
Of which debt securities included in:								
Financial assets at fair value through profit or loss								
- Designated at fair value .....	—	—	—	88,276	488,314	—	—	576,590
Available-for-sale securities .....	—	—	—	—	92,272	1,276	—	93,548
Held-to-maturity securities .....	<u>—</u>	<u>4,142,804</u>	<u>1,431,063</u>	<u>4,141,778</u>	<u>7,238,821</u>	<u>—</u>	<u>—</u>	<u>16,954,466</u>
	<u>—</u>	<u>4,142,804</u>	<u>1,431,063</u>	<u>4,230,054</u>	<u>7,819,407</u>	<u>1,276</u>	<u>—</u>	<u>17,624,604</u>



## 24. RELATED PARTY TRANSACTIONS

During the period, the Group entered into the following material transactions with related parties:

	Interest, commission and rental income		Interest and rental expenses	
	Six months ended 30 June 2010	Six months ended 30 June 2009	Six months ended 30 June 2010	Six months ended 30 June 2009
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Investing enterprises having significant influence on the Group.....	3,867	3,515	11,530	11,617
Jointly controlled entities .....	5,875	6,197	1,135	1,593
Directors of the Bank and their associates .....	2,449	8,149	2,138	3,752

At the end of the reporting period, the Group had the following material outstanding balances with related parties:

	Amounts due from related parties		Amounts due to related parties	
	30 June 2010	31 December 2009	30 June 2010	31 December 2009
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Investing enterprises having significant influence on the Group.....	—	—	207,137	59,749
Jointly controlled entities .....	51,647	53,790	116,456	96,034
Directors of the Bank and their associates .....	913,563	1,434,806	532,372	530,733

### Compensation of key management personnel

The remuneration of directors and key management was as follows:

	Six months ended 30 June	
	2010	2009
	HK\$'000	HK\$'000
Short term benefits .....	24,949	24,128
Post employment benefits .....	1,757	1,399
	26,706	25,527

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

**25. LIST OF SUBSIDIARIES FOR FINANCIAL INFORMATION CONSOLIDATION**

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

Liu Chong Hing Banking Corporation, Cayman

Right Way Investments Limited

## INDEPENDENT AUDITOR'S REPORT

**Deloitte.**

**德勤**

### **TO THE MEMBERS OF CHONG HING BANK LIMITED**

*(incorporated in Hong Kong with limited liability)*

We have audited the consolidated financial statements of Chong Hing Bank Limited (the “Bank”) and its subsidiaries (collectively referred to as the “Group”) set out on pages F-30 to F-101, which comprise the consolidated and the Bank’s statements of financial position as at 31 December 2009, the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

### **Directors’ responsibility for the consolidated financial statements**

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

### **Auditor’s responsibility**

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

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

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

### **Opinion**

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Bank and of the Group as at 31 December 2009 and of the Group’s profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

**Deloitte Touche Tohmatsu**  
*Certified Public Accountants*  
Hong Kong

3 March 2010

**CONSOLIDATED INCOME STATEMENT**  
**FOR THE YEAR ENDED 31 DECEMBER 2009**

	<b>NOTES</b>	<b>2009</b>	<b>2008</b>
		<i>HK\$'000</i>	<i>HK\$'000</i>
Interest income .....		1,184,922	2,171,336
Interest expense .....		(361,591)	(1,307,010)
Net interest income .....	8	823,331	864,326
Fee and commission income .....		307,299	265,220
Fee and commission expense .....		(43,670)	(48,419)
Net fee and commission income .....	9	263,629	216,801
Net gains (losses) on financial assets at fair value through profit or loss .....	10	76,760	(48,299)
Other operating income .....	11	146,222	146,566
Operating expenses .....	12	(978,415)	(772,431)
		331,527	406,963
Impairment allowances on loans and advances .....	20	(102,289)	(91,334)
Net gain on disposal of prepaid lease payments for land .....		362	—
Net (loss) gain on disposal of property and equipment .....		(14)	294
Net gain on disposal of available-for-sale securities .....		24,810	108,706
Net gain on disposal of and fair value adjustments on investment properties .....	23	31,148	39,560
Impairment loss on available-for-sale securities .....		(43,571)	(264,654)
Impairment loss on goodwill .....	33	(10,000)	(20,000)
Profit from operations .....		231,973	179,535
Share of profit (loss) of jointly controlled entities .....		32,410	(90,240)
Profit before taxation .....		264,383	89,295
Taxation .....	14	(32,635)	(28,675)
Profit for the year .....		231,748	60,620
Earnings per share .....	16	HK\$0.53	HK\$0.14

**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**  
**FOR THE YEAR ENDED 31 DECEMBER 2009**

	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Profit for the year .....	<u>231,748</u>	<u>60,620</u>
Other comprehensive income		
Exchange differences arising on translation .....	524	7,194
Available-for-sale securities investment revaluation reserve:		
- Revaluation gain (loss) .....	29,662	(300,495)
- Reclassification adjustment upon disposal and impairment .....	18,761	155,948
- Share of reserve of a jointly controlled entity .....	4,009	(841)
- Income tax relating to available-for-sale securities .....	<u>(10,456)</u>	<u>20,060</u>
Other comprehensive income (expense) for the year (net of tax) .....	<u>42,500</u>	<u>(118,134)</u>
Total comprehensive income (expense) for the year .....	<u><u>274,248</u></u>	<u><u>(57,514)</u></u>
Total comprehensive income (expense) attributable to:		
Owners of the Bank .....	<u><u>274,248</u></u>	<u><u>(57,514)</u></u>

**CONSOLIDATED STATEMENT OF FINANCIAL POSITION**  
**AT 31 DECEMBER 2009**

	NOTES	2009 HK\$'000	2008 HK\$'000
<b>Assets</b>			
Cash and short-term funds .....	17	15,048,680	17,659,927
Placements with banks and other financial institutions maturing between one to twelve months .....		2,814,566	5,367,858
Derivative financial instruments .....	18	331	429
Financial assets at fair value through profit or loss .....	19	576,730	680,680
Available-for-sale securities .....	19	272,649	196,527
Held-to-maturity securities .....	19	16,954,466	9,727,685
Advances and other accounts .....	20	33,267,735	33,634,842
Tax recoverable .....		31,925	38,113
Interests in jointly controlled entities .....	22	119,418	82,999
Investment properties .....	23	103,199	129,801
Property and equipment .....	24	443,688	469,724
Prepaid lease payments for land .....	25	321,533	328,127
Goodwill .....	33	50,606	60,606
<b>Total assets</b> .....		<u>70,005,526</u>	<u>68,377,318</u>
<b>Liabilities</b>			
Deposits and balances of banks and other financial institutions ..		1,447,718	1,525,509
Deposits from customers .....	26	60,788,415	59,401,660
Derivative financial instruments .....	18	44,413	39,303
Other accounts and accruals .....		556,016	477,381
Current tax liabilities .....		15,671	5,104
Loan capital .....	27	967,199	965,454
Deferred tax liabilities .....	30	11,772	6,283
<b>Total liabilities</b> .....		<u>63,831,204</u>	<u>62,420,694</u>
<b>Shareholders' equity</b>			
Share capital .....	28	217,500	217,500
Reserves .....		5,956,822	5,739,124
<b>Shareholders' funds</b> .....		<u>6,174,322</u>	<u>5,956,624</u>
<b>Total liabilities and shareholders' equity</b> .....		<u>70,005,526</u>	<u>68,377,318</u>

Approved and authorised for issue by the Board of Directors on 3 March 2010 and signed on its behalf by:

**Liu Lit Mo**, *Chairman*

**Liu Lit Chi**, *Managing Director & Chief Executive Officer*

**Lau Wai Man**, *Executive Director and Deputy Chief Executive Officer*

**Michael K W Yeung**, *Company Secretary*

**STATEMENT OF FINANCIAL POSITION**  
**AT 31 DECEMBER 2009**

	NOTES	2009 HK\$'000	2008 HK\$'000
<b>Assets</b>			
Cash and short-term funds .....	17	15,006,177	17,617,546
Placements with banks and other financial institutions maturing between one to twelve months.....		2,814,566	5,367,858
Derivative financial instruments .....	18	331	429
Financial assets at fair value through profit or loss .....	19	576,590	680,567
Available-for-sale securities .....	19	196,464	150,725
Held-to-maturity securities.....	19	16,954,466	9,727,685
Advances and other accounts .....	20	32,990,451	33,477,333
Tax recoverable .....		31,620	37,976
Investments in subsidiaries .....	21(i)	338,323	348,323
Amounts due from subsidiaries .....	21(ii)	4,985	3,711
Interests in jointly controlled entities .....	22	21,500	21,500
Investment properties.....	23	76,160	104,050
Property and equipment .....	24	420,498	449,072
Prepaid lease payments for land .....	25	835,087	842,027
<b>Total assets</b> .....		<u>70,267,218</u>	<u>68,828,802</u>
<b>Liabilities</b>			
Deposits and balances of banks and other financial institutions ..		1,447,718	1,525,509
Deposits from customers.....	26	60,785,525	59,398,427
Amounts due to subsidiaries .....	36	763,072	704,828
Derivative financial instruments .....	18	44,413	39,303
Other accounts and accruals.....		272,449	297,748
Current tax liabilities.....		574	2,422
Loan capital .....	27	967,199	965,454
Deferred tax liabilities.....	30	3,769	3,744
<b>Total liabilities</b> .....		<u>64,284,719</u>	<u>62,937,435</u>
<b>Shareholders' equity</b>			
Share capital.....	28	217,500	217,500
Reserves .....	29	<u>5,764,999</u>	<u>5,673,867</u>
<b>Shareholders' funds</b> .....		<u>5,982,499</u>	<u>5,891,367</u>
<b>Total liabilities and shareholders' equity</b> .....		<u>70,267,218</u>	<u>68,828,802</u>

Approved and authorised for issue by the Board of Directors on 3 March 2010 and signed on its behalf by:

**Liu Lit Mo**, *Chairman*

**Liu Lit Chi**, *Managing Director & Chief Executive Officer*

**Lau Wai Man**, *Executive Director and Deputy Chief Executive Officer*

**Michael K W Yeung**, *Company Secretary*

**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**  
**FOR THE YEAR ENDED 31 DECEMBER 2009**

	Notes	Share capital	Share premium	Goodwill	Investment revaluation reserve	General reserve	Translation reserve	Regulatory reserve	Retained profits	Total
		HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 1 January 2009 .....		217,500	1,542,817	(182)	13,352	1,388,500	7,524	307,000	2,480,113	5,956,624
Profit for the year .....		—	—	—	—	—	—	—	231,748	231,748
Other comprehensive income for the year ....		—	—	—	41,976	—	524	—	—	42,500
Total comprehensive income for the year ....		—	—	—	41,976	—	524	—	231,748	274,248
Interim dividend paid for financial year 2009 .....	15	—	—	—	—	—	—	—	(34,800)	(34,800)
Final dividend paid for financial year 2008 .....	15	—	—	—	—	—	—	—	(21,750)	(21,750)
Earmark of retained profits as regulatory reserve .....		—	—	—	—	—	—	(20,000)	20,000	—
At 31 December 2009 .....		<u>217,500</u>	<u>1,542,817</u>	<u>(182)</u>	<u>55,328</u>	<u>1,388,500</u>	<u>8,048</u>	<u>287,000</u>	<u>2,675,311</u>	<u>6,174,322</u>
At 1 January 2008 .....		217,500	1,542,817	(182)	138,680	1,388,500	330	356,000	2,627,143	6,270,788
Profit for the year .....		—	—	—	—	—	—	—	60,620	60,620
Other comprehensive income (expense) for the year .....		—	—	—	(125,328)	—	7,194	—	—	(118,134)
Total comprehensive income (expense) for the year .....		—	—	—	(125,328)	—	7,194	—	60,620	(57,514)
Interim dividend paid for financial year 2008 .....	15	—	—	—	—	—	—	—	(65,250)	(65,250)
Final dividend paid for financial year 2007 .....	15	—	—	—	—	—	—	—	(191,400)	(191,400)
Earmark of retained profits as regulatory reserve .....		—	—	—	—	—	—	(49,000)	49,000	—
At 31 December 2008 .....		<u>217,500</u>	<u>1,542,817</u>	<u>(182)</u>	<u>13,352</u>	<u>1,388,500</u>	<u>7,524</u>	<u>307,000</u>	<u>2,480,113</u>	<u>5,956,624</u>

The retained profits of the Group included retained profit of HK\$3,534,000 (2008: accumulated loss of HK\$28,876,000) retained by the jointly controlled entities of the Group.

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

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



**CONSOLIDATED STATEMENT OF CASH FLOWS**  
**FOR THE YEAR ENDED 31 DECEMBER 2009**

	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
<b>OPERATING ACTIVITIES</b>		
Profit before taxation .....	264,383	89,295
Adjustments for:		
Net loss (gain) on disposal of property and equipment .....	14	(294)
Net gain on disposal of prepaid lease payments for land.....	(362)	—
Net gain on disposal of investment properties.....	(26,000)	—
Net gain on disposal of available-for-sale securities .....	(24,810)	(108,706)
Impairment allowances on loans and advances .....	102,289	91,334
Impairment loss on goodwill.....	10,000	20,000
Impairment loss on available-for-sale securities .....	43,571	264,654
Dividend income from equity securities .....	(8,067)	(12,853)
Share of (profit) loss of jointly controlled entities .....	(32,410)	90,240
Net gain on fair value adjustments on investment properties.....	(5,148)	(39,560)
Depreciation .....	47,213	43,925
Release of prepaid lease payments for land .....	6,075	6,104
Interest income from held-to-maturity securities and available-for-sale securities .....	(312,585)	(462,018)
Interest expense on loan capital .....	19,736	42,122
Exchange adjustments .....	900	615
Operating cash flows before movements in operating assets and liabilities.....	84,799	24,858
(Increase) decrease in operating assets:		
Interest receivable and other accounts.....	(45,860)	381,973
Placements with banks and other financial institutions with original maturity over three months.....	149,657	(303,466)
Exchange fund bills with original maturity over three months .....	(105,182)	47,155
Money at call and short notice with original maturity over three months .....	(1,416,898)	690,017
Bills receivable.....	31,229	175,514
Trade bills .....	47,035	(736)
Other advances to customers.....	289,704	(1,808,623)
Advances to banks and other financial institutions.....	1,729	(59,328)
Financial assets at fair value through profit or loss .....	103,950	453,742
Derivative assets.....	98	(369)
Increase (decrease) in operating liabilities:		
Derivative liabilities .....	5,110	(75,243)
Deposits from customers.....	1,386,755	(925,777)
Deposits and balances of banks and other financial institutions with original maturity over three months.....	176	(1,841)
Other accounts and accruals.....	79,353	(383,060)
Cash generated from (used in) operations.....	611,655	(1,785,184)
Hong Kong Profits Tax paid.....	(17,459)	(58,868)
Overseas tax paid.....	(3,388)	(6,939)
<b>NET CASH GENERATED FROM (USED IN) OPERATING ACTIVITIES .....</b>	<b>590,808</b>	<b>(1,850,991)</b>

	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
<b>INVESTING ACTIVITIES</b>		
Interest received on held-to-maturity securities and available-for-sale securities.....	305,761	542,974
Dividends received on investments.....	8,067	12,853
Dividend income from jointly controlled entities.....	—	3,150
Capital investment in jointly controlled entities .....	—	(35,000)
Purchase of held-to-maturity securities.....	(33,547,891)	(24,380,625)
Purchase of available-for-sale securities.....	(78,367)	(42,160)
Purchase of property and equipment.....	(21,326)	(67,667)
Proceeds from redemption of held-to-maturity securities .....	26,321,110	30,260,920
Proceeds from sale and redemption of available-for-sale securities.....	31,907	421,799
Proceeds from disposal of property and equipment.....	139	1,185
Proceeds from disposal of land .....	881	—
Purchases of investment properties.....	—	(30,000)
Proceeds from disposal of investment property .....	5,800	—
Repayment of loan from a jointly controlled entity .....	—	5,267
<b>NET CASH (USED IN) GENERATED FROM INVESTING ACTIVITIES .....</b>	<b>(6,973,919)</b>	<b>6,692,696</b>
<b>FINANCING ACTIVITIES</b>		
Interest paid on loan capital.....	(19,334)	(42,180)
Dividends paid.....	(56,550)	(256,650)
<b>NET CASH USED IN FINANCING ACTIVITIES.....</b>	<b>(75,884)</b>	<b>(298,830)</b>
<b>NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS.....</b>	<b>(6,458,995)</b>	<b>4,542,875</b>
<b>CASH AND CASH EQUIVALENTS AT 1 JANUARY.....</b>	<b>17,533,299</b>	<b>12,990,424</b>
<b>CASH AND CASH EQUIVALENTS AT 31 DECEMBER,</b> represented by		
Cash and balances with banks and other financial institutions.....	4,427,240	4,087,415
Money at call and short notice .....	6,704,160	13,180,425
Exchange fund bills .....	3,917,280	392,087
Placements with banks and other financial institutions maturing between one to twelve months .....	2,814,566	5,367,858
Deposits and balances of banks and other financial institutions.....	(1,447,718)	(1,525,509)
Less: Amounts with original maturity over three months.....	(5,341,224)	(3,968,977)
	<u>11,074,304</u>	<u>17,533,299</u>

**NOTES TO THE FINANCIAL STATEMENTS**  
FOR THE YEAR ENDED 31 DECEMBER 2009

**1. GENERAL**

The Bank is a public limited company incorporated in Hong Kong and its shares are listed on the Stock Exchange of Hong Kong Limited. The Bank is engaged in the provision of banking and related financial services. The address of the registered office and principal place of business of the Bank is disclosed in the Annual Report.

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

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

In the current year, the Group and the Bank have applied a number of new and revised standards, amendments and interpretations (“new HKFRSs”) issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”) which are or have become effective.

Except as described below, the adoption of the new HKFRSs has had no material effect on the consolidated financial statements of the Group and the financial position of the Bank for the current or prior accounting periods.

**New and revised HKFRSs affecting presentation and disclosure only**

*HKAS 1 (Revised 2007) Presentation of Financial Statements*

HKAS 1 (Revised 2007) has introduced terminology changes (including revised titles for the consolidated financial statements) and changes in the format and content of the consolidated financial statements.

*Improving Disclosures about Financial Instruments  
(Amendments to HKFRS 7 Financial Instruments: Disclosures)*

The amendments to HKFRS 7 expand the disclosures required in relation to fair value measurements in respect of financial instruments which are measured at fair value. The amendments also expand and amend the disclosures required in relation to liquidity risk. The Group has not provided comparative information for the expanded disclosures in accordance with the transitional provision set out in the amendments.

**3. NEW AND REVISED HKFRSs ISSUED BUT NOT YET EFFECTIVE**

The Group and the Bank have not early applied the following new and revised standards, amendments or interpretations that have been issued but are not yet effective.

HKFRSs (Amendments) . . . . .	Amendment to HKFRS 5 as part of Improvements to HKFRSs 2008 <sup>1</sup>
HKFRSs (Amendments) . . . . .	Improvements to HKFRSs 2009 <sup>2</sup>
HKAS 24 (Revised) . . . . .	Related party disclosures <sup>6</sup>
HKAS 27 (Revised) . . . . .	Consolidated and separate financial statements <sup>1</sup>
HKAS 32 (Amendment) . . . . .	Classification of right issues <sup>4</sup>
HKAS 39 (Amendment) . . . . .	Eligible hedged items <sup>1</sup>
HKFRS 1 (Amendment) . . . . .	Additional exemptions for first-time adopters <sup>3</sup>
HKFRS 1 (Amendment) . . . . .	Limited exemption from comparative HKFRS 7 disclosures for first-time adopters <sup>5</sup>
HKFRS 2 (Amendments) . . . . .	Group cash-settled share-based payment transactions <sup>3</sup>
HKFRS 3 (Revised) . . . . .	Business combinations <sup>1</sup>
HKFRS 9 . . . . .	Financial instruments <sup>7</sup>

HK(IFRIC) - INT 14 (Amendment) . . . . .	Prepayments of a minimum funding requirement <sup>6</sup>
HK(IFRIC) - INT 17 . . . . .	Distributions of non-cash assets to owners <sup>1</sup>
HK(IFRIC) - INT 19 . . . . .	Extinguishing financial liabilities with equity instruments <sup>5</sup>

<sup>1</sup> Effective for annual periods beginning on or after 1 July 2009.

<sup>2</sup> Amendments that are effective for annual periods beginning on or after 1 July 2009 and 1 January 2010, as appropriate.

<sup>3</sup> Effective for annual periods beginning on or after 1 January 2010.

<sup>4</sup> Effective for annual periods beginning on or after 1 February 2010.

<sup>5</sup> Effective for annual periods beginning on or after 1 July 2010.

<sup>6</sup> Effective for annual periods beginning on or after 1 January 2011.

<sup>7</sup> Effective for annual periods beginning on or after 1 January 2013.

The application of HKFRS 3 (Revised) may affect the accounting for the Group's business combination for which the acquisition date is on or after 1 January 2010. HKAS 27 (Revised) will affect the accounting treatment for changes in the Group's ownership interest in a subsidiary.

HKFRS 9 "Financial instruments" introduces new requirements for the classification and measurement of financial assets and will be effective from 1 January 2013, with earlier application permitted. The Standard requires all recognised financial assets that are within the scope of HKAS 39 "Financial instruments: Recognition and measurement" to be measured at either amortised cost or fair value. Specifically, debt investments that (i) are held within a business model whose objective is to collect the contractual cash flows and (ii) have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost. All other debt investments and equity investments are measured at fair value. The application of HKFRS 9 might affect the classification and measurement of the Group's and the Bank's financial assets.

In addition, as part of Improvements to HKFRSs issued in 2009, HKAS 17 "Leases" has been amended in relation to the classification of leasehold land. The amendments will be effective from 1 January 2010, with earlier application permitted. Before the amendments to HKAS 17, lessees were required to classify leasehold land as operating leases and presented as prepaid lease payments in the statement of financial position. The amendments have removed such a requirement. Instead, the amendments require the classification of leasehold land to be based on the general principles set out in HKAS 17, that are based on the extent to which risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee. The application of the amendments to HKAS 17 might affect the classification and measurement of the Group's and the Bank's leasehold land.

The management of the Bank anticipate that the application of the other new and revised standards, amendments or interpretations will have no material impact on the consolidated financial statements.

#### 4. SIGNIFICANT ACCOUNTING POLICIES

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

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

##### **Basis of consolidation**

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

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

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

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

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

## **Goodwill**

### *Goodwill arising on acquisitions prior to 1 January 2005*

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

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

### *Goodwill arising on acquisitions on or after 1 January 2005*

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

Capitalised goodwill arising on an acquisition of a business is presented separately in the consolidated 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 acquisition. A cash-generating unit to which goodwill has been allocated is tested for impairment annually, and whenever there is an indication that the unit may be impaired. For goodwill arising on an acquisition in a financial year, the cash-generating unit to which goodwill has been allocated is tested for impairment before the end of that financial year. When the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated to reduce the carrying amount of any goodwill allocated to the unit first, and then to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the unit. Any impairment loss for goodwill is recognised directly in the consolidated income statement. Impairment losses relating to goodwill cannot be reversed for subsequent increases in its recoverable amount in future periods.

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

## **Jointly controlled entities**

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

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

When an entity of the Group transacts with a jointly controlled entity of the Group, profits or losses are eliminated to the extent of the Group's interest in the jointly controlled entity.

## **Revenue recognition**

### *Interest income and expenses*

Interest income and expenses are recognised on a time-proportion basis by reference to the principal outstanding and at the effective interest rate applicable. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, where appropriate, a shorter period to the net carrying amount of the financial asset or financial liability 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 a financial asset has been written down as a result of an impairment loss, interest income is recognised using the original rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

#### *Fees and commission income*

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

Other fees and commission income, including account servicing fees, investment management fees, sales commission, placement fees and syndication fees, are recognised as the related services are performed.

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

#### *Dividends*

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

### **Property and equipment**

Property and equipment including leasehold buildings are stated at cost less subsequent accumulated depreciation and accumulated impairment losses.

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

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

### **Investment properties**

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

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

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

### **Leasing**

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

#### *The Group as lessor*

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

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

### *The Group as lessee*

Operating lease payments are recognised as an expense on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are recognised as a reduction of rental expense over the lease term on a straight-line basis.

### *Leasehold land and building*

The land and building elements of a lease of land and building are considered separately for the purpose of lease classification, unless the lease payments cannot be allocated reliably between the land and building elements, in which case, the entire lease is generally treated as a finance lease and accounted for as property and equipment. To the extent the allocation of the lease payments can be made reliably, leasehold interests in land are accounted for as operating leases and amortised 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**

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

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are recognised in profit or loss in the period in which they arise, except for exchange differences arising on a monetary item that forms part of the Bank's net investment in a foreign operation, in which case, such exchange differences are recognised in other comprehensive income and accumulated in equity and will be reclassified from equity to profit or loss on disposal of the foreign operation. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period except for differences arising on the retranslation of non-monetary items in respect of which gains and losses are recognised directly in other comprehensive income, in which cases, the exchange differences are also recognised directly in other comprehensive income.

For the purposes of presenting the consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated into the presentation currency of the Group (i.e. Hong Kong dollars) at the rate of exchange prevailing at the end of the reporting period, and their income and expenses are translated at the average exchange rates for the year, unless exchange rates fluctuate significantly during the period, in which case, the exchange rates prevailing at the dates of transactions are used. Exchange differences arising, if any, are recognised in other comprehensive income and accumulated in equity (the translation reserve). Such exchange differences are recognised in profit or loss in the period in which the foreign operation is disposal of.

### **Retirement benefit costs**

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

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

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

### **Taxation**

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

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the 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 base 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 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 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. Deferred tax is recognised in profit or loss, except when it relates to items that are recognised in other comprehensive income or directly in equity, in which case the deferred tax is also recognised in other comprehensive income or directly in equity respectively.

## **Financial instruments**

Financial assets and financial liabilities are recognised on the statement of financial position when an entity of the Group 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 or issue of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in consolidated income statement.

## **Financial assets**

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

## ***Effective interest method***

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees, 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.

## ***Financial assets at fair value through profit or loss***

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

A financial asset is classified as held for trading if:

- it has been incurred principally for the purpose of selling in the near future; or
- it is a part of an identified portfolio of financial instruments that the Group and the Bank manage 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 and the Bank's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and HKAS 39 permits the entire combined contract (asset or liability) to be designated as at fair value through profit or loss.

Financial assets at fair value through profit or loss are measured at fair value, with changes in fair value arising from remeasurement recognised directly in the consolidated income statement in the period in which they arise. The net gain or loss recognised in profit or loss exclude any dividend or interest earned on the financial assets.

#### *Loans and receivables*

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

#### *Held-to-maturity investments*

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. Subsequent to initial recognition, held-to-maturity investments are measured at amortised cost using the effective interest method, less any identified impairment losses.

#### *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 investment.

Available-for-sale financial assets are measured at fair value at the end of the reporting period. Changes in fair value are recognised in other comprehensive income and accumulated in investment revaluation reserve, until the financial asset is disposed of or is determined to be impaired, at which time, the cumulative gain or loss previously accumulated in the investment revaluation reserve is reclassified to profit or loss (see accounting policy on impairment loss on financial assets below).

For 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 and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments, they are measured at cost less any identified impairment losses at the end of the reporting period (see accounting policy on impairment loss on financial assets below).

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

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

#### **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 impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the financial assets have been impacted.

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

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

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

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

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

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

For financial assets carried at amortised cost, an impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.

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

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

## **Financial liabilities and equity**

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

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

### ***Effective interest method***

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments (including all fees, 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 has 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
- it is a part of an identified portfolio of financial instruments that the Group and the Bank manage 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 liability other than a financial liability 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 liability 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 and the Bank's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and HKAS 39 permits the entire combined contract (asset or liability) to be designated as at fair value through profit or loss.

Financial liabilities at fair value through profit or loss are measured at fair value, with changes in fair value arising on remeasurement recognised directly in profit or loss in the period in which they arise. The net gain or loss recognised in profit or loss excludes any interest paid on the financial liabilities.

#### *Other financial liabilities*

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

#### *Offsetting financial instruments*

Financial assets and liabilities are offset and the net amount reported in the statement 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 asset and settle the liability simultaneously.

#### *Equity instruments*

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

### **Derivative financial instruments and hedging**

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each reporting date. The resulting gain or loss is recognised in profit or loss immediately unless the derivative is designated and effective as a hedging instrument in which event the timing of the recognition in profit or loss depends on the nature of hedge relationship.

#### **Embedded derivatives**

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

#### **Hedge accounting**

The Group and the Bank designate certain derivatives as hedges of the fair value of available-for-sale securities (fair value hedges).

At the inception of the hedging relationship the entity documents the relationship between the hedging instrument and 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 and the Bank document whether the hedging instrument that is used in a hedging relationship is highly effective in offsetting 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 recorded in profit or loss immediately, together with any changes in the fair value of the hedged item that is attributable to the hedged risk.

Hedge accounting is discontinued when the Group and the Bank revoke the hedging relationship, the hedging instrument expires or is sold, terminated, or exercised, or 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 a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument. A financial guarantee contract issued by the Group and the Bank 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 and the Bank measure the financial guarantee contract at the higher of: (i) the amount determined in accordance with HKAS 37 “Provisions, Contingent Liabilities and Contingent Assets”; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with HKAS 18 “Revenue”.

#### **Derecognition**

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

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

#### **Provisions**

Provisions are recognised when the Group and the Bank have a present obligation as a result of a past event, and it is probable that the Group and the Bank will be required to settle that 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 is material).

#### **Impairment on non-financial assets**

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

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case, the carrying amount of the asset is increased to its recoverable amount. A reversal of an impairment loss is recognised as income immediately.

#### **Fiduciary assets**

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

## Cash and cash equivalents

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

## 5. CRITICAL ACCOUNTING JUDGEMENT AND KEY SOURCE OF ESTIMATION UNCERTAINTY

In the application of the Group's accounting policies, which are described in Note 4, management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and 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 loss in loans and advances. The allowances consist of individual impairment allowances and collective impairment allowances. The overall impairment allowances represent the aggregate amount by which management considers necessary to write down its loan portfolio in order to state it in the statement 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 for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio.

Details of the impairment allowances movements are disclosed in Note 20.

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

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

The fair values of investment in funds are determined based on the net asset values as reported by fund administrator.

Details of the assumptions used are disclosed in Note 7.

#### (c) *Estimated impairment of goodwill*

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

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

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

Details of the recoverable amount calculation are disclosed in Note 33.

### **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.

#### *Held-to-maturity investments*

The Group classified certain non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires judgement. In making this judgement, the Group evaluates its intention and ability to hold such investments to maturity. If the Group fails to keep these investments to maturity other than for the specific circumstances - for example, selling an insignificant amount close to maturity - it will be required to reclassify the entire class as available-for-sale. The investments would therefore be measured at fair value instead of amortised cost.

Details of these assets are set out in Note 19.

## **6. SEGMENT INFORMATION**

### **(a) Business segments**

The Group has adopted HKFRS 8 Operating Segments with effect from 1 January 2009. HKFRS 8 is a disclosure standard that requires operating segments to be identified on the basis of internal reports about components of the Group that are regularly reviewed by the chief operating decision maker (Executive Committee) for the purpose of allocating resources to segments and assessing their performance. In contrast, the predecessor Standard (HKAS 14 Segment Reporting) required an entity to identify two sets of segments (business and geographical), using a risks and returns approach. The adoption of HKFRS 8 has not resulted in a redesignation of the Group's reportable segments as compared with the primary reportable segments determined in accordance with HKAS 14.

The Group's operating and reportable segments under HKFRS 8, which are identified based on different business of the Group, are as follows:

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

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

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

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

(i) Segment information about these businesses for the year ended 31 December 2009 is presented below:

**Segment revenues and results**

	<b>Corporate and retail banking</b>	<b>Treasury activities</b>	<b>Securities dealing</b>	<b>Other banking- related services</b>	<b>Eliminations</b>	<b>Consolidated</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Interest income from external customers .....	686,011	496,758	2,153	—	—	1,184,922
Interest expense to external customers .....	(321,889)	(39,702)	—	—	—	(361,591)
Inter-segment interest income (note).....	146,982	—	—	—	(146,982)	—
Inter-segment interest expense (note).....	—	(146,982)	—	—	146,982	—
Net interest income .....	511,104	310,074	2,153	—	—	823,331
Fee and commission income .....	99,236	—	208,063	—	—	307,299
Fee and commission expense .....	(43,284)	—	(386)	—	—	(43,670)
Net gains on financial assets at fair value through profit or loss .....	742	75,910	—	108	—	76,760
Other operating income .....	72,184	36,300	(45)	37,783	—	146,222
Total operating income .....	639,982	422,284	209,785	37,891	—	1,309,942
Operating expenses .....	(709,280)	(25,431)	(56,040)	(10,399)	—	(801,150)
Impairment allowances on loans and advances .....	(102,289)	—	—	—	—	(102,289)
Net loss on disposal of property and equipment .....	(14)	—	—	—	—	(14)
Net gain on disposal of prepaid lease payments for land .....	362	—	—	—	—	362
Net gain on disposal of available-for-sale securities .....	—	—	—	24,810	—	24,810
Net gain on disposal of and fair value adjustments on investment properties .....	—	—	—	31,148	—	31,148
Impairment loss on available-for-sale securities .....	—	(43,571)	—	—	—	(43,571)
Impairment loss on goodwill .....	—	—	—	(10,000)	—	(10,000)
Segment profit .....	<u>(171,239)</u>	<u>353,282</u>	<u>153,745</u>	<u>73,450</u>	<u>—</u>	<u>409,238</u>
Unallocated corporate expenses .....						<u>(177,265)</u>
Profit from operations .....						231,973
Share of profits of jointly controlled entities .....				<u>32,410</u>		<u>32,410</u>
Profit before taxation .....						<u>264,383</u>

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

## Segment assets and liabilities

	Corporate and retail banking	Treasury activities	Securities dealing	Other banking- related services	Consolidated
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Assets					
Segment assets .....	37,788,842	31,059,086	304,754	402,153	69,554,835
Interests in jointly controlled entities .....				119,418	119,418
Unallocated corporate assets .....					331,273
Consolidated total assets .....					<u>70,005,526</u>
Liabilities					
Segment liabilities .....	60,987,105	2,464,100	240,003	41,854	63,733,062
Unallocated corporate liabilities .....					98,142
Consolidated total liabilities .....					<u>63,831,204</u>

## Other information

	Corporate and retail banking	Treasury activities	Securities dealing	Other banking- related services	Unallocated	Consolidated
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Capital additions .....	11,347	1,540	4,627	73	3,739	21,326
Depreciation .....	27,316	1,396	4,523	675	13,303	47,213
Release of prepaid lease payments for land .....	<u>3,416</u>	<u>73</u>	<u>457</u>	<u>—</u>	<u>2,129</u>	<u>6,075</u>



(ii) Segment information about these businesses for the year ended 31 December 2008 is presented below:

**Segment revenues and results**

	<b>Corporate and retail banking</b>	<b>Treasury activities</b>	<b>Securities dealing</b>	<b>Other banking- related services</b>	<b>Eliminations</b>	<b>Consolidated</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Interest income from external customers .....	1,102,344	1,066,191	2,801	—	—	2,171,336
Interest expense to external customers .....	(1,250,306)	(56,704)	—	—	—	(1,307,010)
Inter-segment interest income (note).....	607,244	—	—	—	(607,244)	—
Inter-segment interest expense (note).....	—	(607,244)	—	—	607,244	—
Net interest income .....	459,282	402,243	2,801	—	—	864,326
Fee and commission income.....	79,368	—	139,266	46,586	—	265,220
Fee and commission expense.....	(42,985)	—	(945)	(4,489)	—	(48,419)
Net gain (losses) on financial assets at fair value through profit or loss.....	—	(48,508)	—	209	—	(48,299)
Other operating income.....	70,788	42,985	(86)	32,879	—	146,566
Total operating income.....	566,453	396,720	141,036	75,185	—	1,179,394
Operating expenses .....	(423,857)	(28,542)	(51,788)	(22,177)	—	(526,364)
Impairment allowances on loans and advances .....	(91,334)	—	—	—	—	(91,334)
Net gain on disposal of property and equipment .....	294	—	—	—	—	294
Net gain on disposal of available-for-sale securities.....	—	—	—	108,706	—	108,706
Net gain on fair value adjustments on investment properties .....	—	—	—	39,560	—	39,560
Impairment loss on available-for-sale securities.....	—	(264,654)	—	—	—	(264,654)
Impairment loss on goodwill.....	—	—	—	(20,000)	—	(20,000)
Segment profit .....	<u>51,556</u>	<u>103,524</u>	<u>89,248</u>	<u>181,274</u>	<u>—</u>	<u>425,602</u>
Unallocated corporate expenses.....						<u>(246,067)</u>
Profit from operations.....						179,535
Share of losses of jointly controlled entities.....				<u>(90,240)</u>		<u>(90,240)</u>
Profit before taxation.....						<u>89,295</u>

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

## Segment assets and liabilities

	Corporate and retail banking	Treasury activities	Securities dealing	Other banking- related services	Consolidated
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Assets					
Segment assets .....	38,347,147	29,158,388	183,804	382,208	68,071,547
Interests in jointly controlled entities .....				82,999	82,999
Unallocated corporate assets .....					222,772
Consolidated total assets .....					<u>68,377,318</u>
Liabilities					
Segment liabilities .....	59,594,953	2,535,119	137,056	41,089	62,308,217
Unallocated corporate liabilities .....					112,477
Consolidated total liabilities .....					<u>62,420,694</u>

## Other information

	Corporate and retail banking	Treasury activities	Securities dealing	Other banking- related services	Unallocated	Consolidated
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Capital additions .....	45,467	651	2,024	4,830	14,695	67,667
Depreciation .....	25,331	1,103	4,055	792	12,644	43,925
Release of prepaid lease payments for land .....	<u>3,496</u>	<u>69</u>	<u>446</u>	<u>2,091</u>	<u>2</u>	<u>6,104</u>

## (b) Geographical information

Geographical information is analysed by the Group based on the locations of the principal operations of the branches and subsidiary companies responsible for reporting the results or booking the assets.

Details of geographical information are set out below:

2009						
	Total operating income	Profit before taxation	Total assets	Total liabilities	Total contingent liabilities and commitments	Capital expenditure during the year
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Hong Kong .....	1,275,930	246,705	68,439,215	62,917,441	15,331,875	20,682
Macau and Shantou, Mainland						
China .....	20,509	10,461	1,108,307	753,065	174,768	530
America .....	<u>13,503</u>	<u>7,217</u>	<u>458,004</u>	<u>160,698</u>	<u>79,603</u>	<u>114</u>
Total .....	<u>1,309,942</u>	<u>264,383</u>	<u>70,005,526</u>	<u>63,831,204</u>	<u>15,586,246</u>	<u>21,326</u>

	<b>Total operating income</b>	<b>Profit before taxation</b>	<b>Total assets</b>	<b>Total liabilities</b>	<b>Total contingent liabilities and commitments</b>	<b>Capital expenditure during the year</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Hong Kong .....	1,123,459	47,197	66,291,572	61,423,248	15,270,371	59,502
Macau and Shantou, Mainland						
China .....	37,725	29,980	1,195,689	798,598	224,438	8,134
America .....	18,210	12,118	890,057	198,848	62,460	31
Total .....	<u>1,179,394</u>	<u>89,295</u>	<u>68,377,318</u>	<u>62,420,694</u>	<u>15,557,269</u>	<u>67,667</u>

*Note: Total operating income consists of net interest income, net fee and commission income, net gains (losses) on financial assets at fair value through profit or loss and other operating income.*

## 7. FINANCIAL RISK MANAGEMENT

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

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

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

### Categories of financial instruments

	<b>THE GROUP</b>		<b>THE BANK</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
<b>Financial assets</b>				
Fair value through profit or loss				
- designated at fair value .....	576,590	680,567	576,590	680,567
- held for trading .....	471	542	331	429
Held-to-maturity securities .....	16,954,466	9,727,685	16,954,466	9,727,685
Loans and receivables				
(including cash and cash equivalents) .....	51,130,981	56,662,627	50,816,179	56,466,448
Available-for-sale securities .....	<u>272,649</u>	<u>196,527</u>	<u>196,464</u>	<u>150,725</u>
<b>Financial liabilities</b>				
Fair value through profit or loss				
- held for trading .....	44,413	39,303	44,413	39,303
Amortised cost .....	<u>63,759,348</u>	<u>62,370,004</u>	<u>64,235,963</u>	<u>62,891,966</u>

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

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

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

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

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

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

### Risk mitigation policies

Some specific control and mitigation measures are outlined below:

#### (a) Collateral

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

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

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

#### (b) Other risk mitigations

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

## Impairment and provisioning policies

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

The impairment allowances shown in the statements of financial position is based on the five rating grades adopted by the Hong Kong Monetary Authority, with the majority of the impairment allowances arising from the bottom three gradings.

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

	31 December 2009				
	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
Loans for use in Hong Kong					
Industrial, commercial and financial					
- Property development .....	1,516,107	7,545	—	694,641	—
- Property investment .....	7,712,459	—	1,179	6,709,546	1,773
- Financial concerns .....	1,989,693	—	—	1,236,433	—
- Stockbrokers .....	311,064	167	—	256,687	—
- Wholesale and retail trade .....	1,018,952	—	33	685,397	696
- Manufacturing .....	1,414,234	381	12,820	592,610	13,356
- Transport and transport equipment .....	641,908	—	—	131,451	—
- Recreational activities .....	1,832	8	—	1,159	—
- Information technology .....	328	38	—	118	—
- Others .....	6,318,840	23,116	2,223	2,726,628	3,341
Individuals					
- Loans for the purchase of flats in the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme .....	617,860	—	28	617,782	599
- Loans for the purchase of other residential properties .....	5,917,720	—	171	5,911,151	3,651
- Credit card advances .....	97,227	2,198	331	—	494
- Others .....	1,497,919	—	2,168	1,436,357	3,285
	29,056,143	33,453	18,953	20,999,960	27,195
Trade finance .....	692,339	20,255	5,393	231,044	10,156
Loans for use outside Hong Kong .....	3,045,097	54,388	1,559	1,595,524	16,356
	<u>32,793,579</u>	<u>108,096</u>	<u>25,905</u>	<u>22,826,528</u>	<u>53,707</u>

31 December 2008

	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
Loans for use in Hong Kong					
Industrial, commercial and financial					
- Property development .....	1,449,043	13,268	—	208,406	—
- Property investment .....	7,561,256	—	—	6,820,072	—
- Financial concerns .....	3,031,254	—	—	1,342,433	—
- Stockbrokers .....	157,647	186	523	140,359	523
- Wholesale and retail trade .....	976,687	1,265	115	685,344	115
- Manufacturing .....	2,051,389	6,960	16	1,045,633	223
- Transport and transport equipment .....	932,535	—	—	275,741	—
- Recreational activities .....	2,535	8	—	1,284	—
- Information technology .....	198	24	—	10	—
- Others .....	5,296,954	14,241	145	2,322,465	26,646
Individuals					
- Loans for the purchase of flats in the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme .....	693,850	—	382	693,468	1,607
- Loans for the purchase of other residential properties .....	5,456,764	3,503	—	5,452,820	—
- Credit card advances .....	116,180	4,225	220	—	252
- Others .....	1,557,603	2,340	2,882	1,515,209	6,785
	29,283,895	46,020	4,283	20,503,244	36,151
Trade finance .....	804,393	7,026	—	143,778	—
Loans for use outside Hong Kong .....	3,156,339	55,942	1,516	1,727,937	64,423
	<u>33,244,627</u>	<u>108,988</u>	<u>5,799</u>	<u>22,374,959</u>	<u>100,574</u>

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

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

#### Concentration of risks of financial assets with credit risk exposure

Concentration of credit risk exists when changes in geographic 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 is disclosed below:

### Geographical locations

	THE GROUP				THE BANK			
		Asia Pacific excluding Hong Kong	Others	Total		Asia Pacific excluding Hong Kong	Others	Total
	Hong Kong	Hong Kong	Others	Total	Hong Kong	Hong Kong	Others	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2009								
Short-term funds .....	8,711,251	2,402,242	3,600,282	14,713,775	8,668,785	2,402,242	3,600,283	14,671,310
Placements with banks and other financial institutions .....	36,764	1,980,987	796,815	2,814,566	36,764	1,980,987	796,815	2,814,566
Derivative financial instruments.....	331	—	—	331	331	—	—	331
Financial assets at fair value through profit or loss .....	75,855	165,197	335,538	576,590	75,855	165,197	335,538	576,590
Available-for-sale securities.....	54,948	—	38,600	93,548	54,948	—	38,600	93,548
Held-to-maturity securities.....	630,805	7,493,271	8,830,390	16,954,466	630,805	7,493,271	8,830,390	16,954,466
Advances and other accounts .....	31,396,684	692,460	1,178,591	33,267,735	31,123,939	688,637	1,177,875	32,990,451
Amounts due from subsidiaries .....	—	—	—	—	4,985	—	—	4,985
	<u>40,906,638</u>	<u>12,734,157</u>	<u>14,780,216</u>	<u>68,421,011</u>	<u>40,596,412</u>	<u>12,730,334</u>	<u>14,779,501</u>	<u>68,106,247</u>

	THE GROUP				THE BANK			
		Asia Pacific excluding Hong Kong	Others	Total		Asia Pacific excluding Hong Kong	Others	Total
	Hong Kong	Hong Kong	Others	Total	Hong Kong	Hong Kong	Others	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008								
Short-term funds .....	1,616,155	5,964,649	9,643,835	17,224,639	1,573,812	5,964,649	9,643,835	17,182,296
Placements with banks and other financial institutions .....	—	1,625,000	3,742,858	5,367,858	—	1,625,000	3,742,858	5,367,858
Derivative financial instruments.....	429	—	—	429	429	—	—	429
Financial assets at fair value through profit or loss .....	—	339,360	341,207	680,567	—	339,360	341,207	680,567
Available-for-sale securities.....	—	—	52,395	52,395	—	—	52,395	52,395
Held-to-maturity securities.....	801,190	3,523,286	5,403,209	9,727,685	801,190	3,523,286	5,403,209	9,727,685
Advances and other accounts .....	31,402,108	1,025,730	1,207,004	33,634,842	31,247,674	1,022,666	1,206,993	33,477,333
Amounts due from subsidiaries .....	—	—	—	—	3,711	—	—	3,711
	<u>33,819,882</u>	<u>12,478,025</u>	<u>20,390,508</u>	<u>66,688,415</u>	<u>33,626,816</u>	<u>12,474,961</u>	<u>20,390,497</u>	<u>66,492,274</u>

**Industry sectors**

	<b>THE GROUP</b>					
	<b>Banks and other financial institutions</b>	<b>Central government and central banks</b>	<b>Public sector entities</b>	<b>Corporate entities</b>	<b>Others</b>	<b>Total</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 31 December 2009						
Short term funds .....	10,661,232	4,052,543	—	—	—	14,713,775
Placements with banks and other financial institutions .....	2,814,566	—	—	—	—	2,814,566
Derivative financial instruments .....	177	—	—	154	—	331
Financial assets at fair value through profit or loss .....	82,389	—	—	494,201	—	576,590
Available-for-sale securities .....	37,325	—	54,947	1,276	—	93,548
Held-to-maturity securities .....	14,766,614	182,203	56,328	1,949,321	—	16,954,466
Advances and other accounts .....	83,464	117,652	160,665	23,284,220	9,621,734	33,267,735
	<u>28,445,767</u>	<u>4,352,398</u>	<u>271,940</u>	<u>25,729,172</u>	<u>9,621,734</u>	<u>68,421,011</u>
At 31 December 2008						
Short term funds .....	16,249,216	975,423	—	—	—	17,224,639
Placements with banks and other financial institutions .....	5,367,858	—	—	—	—	5,367,858
Derivative financial instruments .....	—	—	—	429	—	429
Financial assets at fair value through profit or loss .....	275,085	—	—	405,482	—	680,567
Available-for-sale securities .....	35,755	—	—	16,640	—	52,395
Held-to-maturity securities .....	8,033,861	289,181	67,547	1,337,096	—	9,727,685
Advances and other accounts .....	89,187	120,605	295,132	23,901,186	9,228,732	33,634,842
	<u>30,050,962</u>	<u>1,385,209</u>	<u>362,679</u>	<u>25,660,833</u>	<u>9,228,732</u>	<u>66,688,415</u>



**THE BANK**

	<b>Banks and other financial institutions</b>	<b>Central government and central banks</b>	<b>Public sector entities</b>	<b>Corporate entities</b>	<b>Others</b>	<b>Total</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 31 December 2009						
Short term funds .....	10,618,767	4,052,543	—	—	—	14,671,310
Placements with banks and other financial institutions .....	2,814,566	—	—	—	—	2,814,566
Derivative financial instruments .....	177	—	—	154	—	331
Financial assets at fair value through profit or loss .....	82,389	—	—	494,201	—	576,590
Available-for-sale securities .....	37,325	—	54,947	1,276	—	93,548
Held-to-maturity securities .....	14,766,614	182,203	56,328	1,949,321	—	16,954,466
Advances and other accounts .....	82,894	116,920	160,665	23,008,238	9,621,734	32,990,451
Amounts due from subsidiaries .....	—	—	—	4,985	—	4,985
	<u>28,402,732</u>	<u>4,351,666</u>	<u>271,940</u>	<u>25,458,175</u>	<u>9,621,734</u>	<u>68,106,247</u>
At 31 December 2008						
Short term funds .....	16,206,873	975,423	—	—	—	17,182,296
Placements with banks and other financial institutions .....	5,367,858	—	—	—	—	5,367,858
Derivative financial instruments .....	—	—	—	429	—	429
Financial assets at fair value through profit or loss .....	275,085	—	—	405,482	—	680,567
Available-for-sale securities .....	35,755	—	—	16,640	—	52,395
Held-to-maturity securities .....	8,033,861	289,181	67,547	1,337,096	—	9,727,685
Advances and other accounts .....	88,184	120,056	295,132	23,745,229	9,228,732	33,477,333
Amounts due from subsidiaries .....	—	—	—	3,711	—	3,711
	<u>30,007,616</u>	<u>1,384,660</u>	<u>362,679</u>	<u>25,508,587</u>	<u>9,228,732</u>	<u>66,492,274</u>

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

Credit risk exposures relating to assets on statement of financial position are as follows:

	<b>THE GROUP</b>		<b>THE BANK</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Short-term funds .....	14,713,775	17,224,639	14,671,310	17,182,296
Placements with banks and other financial institutions .....	2,814,566	5,367,858	2,814,566	5,367,858
Derivative financial instruments .....	331	429	331	429
Financial assets at fair value through profit or loss .....	576,590	680,567	576,590	680,567
Available-for-sale securities .....	93,548	52,395	93,548	52,395
Held-to-maturity securities .....	16,954,466	9,727,685	16,954,466	9,727,685
Advances and other accounts .....	33,267,735	33,634,842	32,990,451	33,477,333
Amounts due from subsidiaries .....	—	—	4,985	3,711
	<u>68,421,011</u>	<u>66,688,415</u>	<u>68,106,247</u>	<u>66,492,274</u>

Credit risk exposures relating to off-statement of financial position items are as follows:

	<b>THE GROUP</b>		<b>THE BANK</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Financial guarantee and other credit related contingent liabilities.....	1,074,429	1,014,062	1,074,429	1,014,062
Loan commitments and other credit related commitments .....	14,508,583	14,529,659	14,508,583	14,529,659
Other commitments .....	3,234	13,548	3,234	13,548
	<u>15,586,246</u>	<u>15,557,269</u>	<u>15,586,246</u>	<u>15,557,269</u>

### Credit quality

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

	<b>THE GROUP</b>	
	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Neither past due nor impaired .....	32,571,552	32,979,798
Past due but not impaired .....	168,320	164,255
Impaired .....	53,707	100,574
	<u>32,793,579</u>	<u>33,244,627</u>
Less: Allowances for impairment .....	<u>(134,001)</u>	<u>(114,787)</u>
	<u>32,659,578</u>	<u>33,129,840</u>

	<b>THE BANK</b>	
	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Neither past due nor impaired .....	32,571,552	32,979,384
Past due but not impaired .....	168,320	164,255
Impaired .....	53,707	100,574
	<u>32,793,579</u>	<u>33,244,213</u>
Less: Allowances for impairment .....	<u>(134,001)</u>	<u>(114,783)</u>
	<u>32,659,578</u>	<u>33,129,430</u>

(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.

THE GROUP									
	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 2009									
GRADES:									
Pass .....	1,266,071	15,192,196	9,149,186	5,488,452	216,415	629,905	85,157	225,307	32,252,689
Special mention .....	9,841	4,890	2,000	—	—	9,320	—	—	26,051
Substandard or below ....	2,473	21,153	120,422	144,287	—	4,477	—	—	292,812
Total .....	<u>1,278,385</u>	<u>15,218,239</u>	<u>9,271,608</u>	<u>5,632,739</u>	<u>216,415</u>	<u>643,702</u>	<u>85,157</u>	<u>225,307</u>	<u>32,571,552</u>
At 31 December 2008									
GRADES:									
Pass .....	2,112,449	14,631,407	8,970,612	5,362,572	435,557	760,580	80,786	415,828	32,769,791
Special mention .....	20,121	19,272	—	—	—	7,281	—	—	46,674
Substandard or below ....	—	15,636	—	147,697	—	—	—	—	163,333
Total .....	<u>2,132,570</u>	<u>14,666,315</u>	<u>8,970,612</u>	<u>5,510,269</u>	<u>435,557</u>	<u>767,861</u>	<u>80,786</u>	<u>415,828</u>	<u>32,979,798</u>
THE BANK									
	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 2009									
GRADES:									
Pass .....	1,266,071	15,192,196	9,149,186	5,488,452	216,415	629,905	85,157	225,307	32,252,689
Special mention .....	9,841	4,890	2,000	—	—	9,320	—	—	26,051
Substandard or below ....	2,473	21,153	120,422	144,287	—	4,477	—	—	292,812
Total .....	<u>1,278,385</u>	<u>15,218,239</u>	<u>9,271,608</u>	<u>5,632,739</u>	<u>216,415</u>	<u>643,702</u>	<u>85,157</u>	<u>225,307</u>	<u>32,571,552</u>
At 31 December 2008									
GRADES:									
Pass .....	2,112,449	14,630,993	8,970,612	5,362,572	435,557	760,580	80,786	415,828	32,769,377
Special mention .....	20,121	19,272	—	—	—	7,281	—	—	46,674
Substandard or below ....	—	15,636	—	147,697	—	—	—	—	163,333
Total .....	<u>2,132,570</u>	<u>14,665,901</u>	<u>8,970,612</u>	<u>5,510,269</u>	<u>435,557</u>	<u>767,861</u>	<u>80,786</u>	<u>415,828</u>	<u>32,979,384</u>

Collateral is mainly properties and fixed deposits.

(ii) Loans and advances past due but not impaired

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

THE GROUP AND THE BANK							
	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 2009							
Past due up to 30 days.....	6,771	10,252	—	—	—	—	17,023
Past due from 31 to 90 days .....	23,114	102,003	—	12,905	143	2,235	140,400
Past due more than 90 days .....	730	8,393	620	985	169	—	10,897
Total .....	<u>30,615</u>	<u>120,648</u>	<u>620</u>	<u>13,890</u>	<u>312</u>	<u>2,235</u>	<u>168,320</u>
Fair value of collateral .....	<u>47,860</u>	<u>291,736</u>	<u>671</u>	<u>13,323</u>	<u>2,416</u>	<u>—</u>	<u>356,006</u>
At 31 December 2008							
Past due up to 30 days.....	3,302	10,145	—	1,962	—	—	15,409
Past due from 31 to 90 days .....	7,878	94,967	5,704	19,484	280	2,925	131,238
Past due more than 90 days .....	5,296	11,644	—	668	—	—	17,608
Total .....	<u>16,476</u>	<u>116,756</u>	<u>5,704</u>	<u>22,114</u>	<u>280</u>	<u>2,925</u>	<u>164,255</u>
Fair value of collateral .....	<u>40,896</u>	<u>240,585</u>	<u>—</u>	<u>28,474</u>	<u>—</u>	<u>—</u>	<u>309,955</u>

Collateral is mainly properties and fixed deposits.

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

(iii) Loans and advances individually impaired

(a) Loans and advances to customers

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

THE GROUP AND THE BANK							
	Overdrafts	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 2009							
Individually impaired loans.....	<u>5,788</u>	<u>39,506</u>	<u>—</u>	<u>7,477</u>	<u>451</u>	<u>485</u>	<u>53,707</u>
Fair value of collateral .....	<u>33,055</u>	<u>45,395</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>78,450</u>
At 31 December 2008							
Individually impaired loans.....	<u>27,743</u>	<u>9,034</u>	<u>62,857</u>	<u>113</u>	<u>575</u>	<u>252</u>	<u>100,574</u>
Fair value of collateral .....	<u>174,295</u>	<u>11,920</u>	<u>283,958</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>470,173</u>

Collateral is mainly properties and fixed deposits.

(b) **Loans and advances to banks**

There are no individually impaired loans and advances to banks as at 31 December 2009 and 31 December 2008.

(iv) **Loans and advances renegotiated**

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

	<b>THE GROUP AND THE BANK</b>	
	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Renegotiated loans that would otherwise be past due or impaired .....	<u>50,124</u>	<u>17,017</u>

**Financial investments by rating agency designation**

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

	<b>THE GROUP AND THE BANK</b>			
	<b>Financial assets at fair value through profit or loss</b>	<b>Available for-sale securities (excluding equity securities)</b>	<b>Held-to- maturity securities</b>	<b>Total</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 31 December 2009				
Aaa.....	—	—	1,854,620	1,854,620
Aa1 to Aa3 .....	38,271	92,272	12,495,432	12,625,975
A1 to A3.....	94,123	—	2,544,102	2,638,225
Lower than A3 .....	—	—	4,544	4,544
Unrated.....	444,196	1,276	55,768	501,240
Total .....	<u>576,590</u>	<u>93,548</u>	<u>16,954,466</u>	<u>17,624,604</u>
At 31 December 2008				
Aaa.....	—	—	653,637	653,637
Aa1 to Aa3 .....	232,475	35,755	7,210,258	7,478,488
A1 to A3.....	83,985	—	1,671,001	1,754,986
Lower than A3 .....	—	—	74,529	74,529
Unrated.....	364,107	16,640	118,260	499,007
Total .....	<u>680,567</u>	<u>52,395</u>	<u>9,727,685</u>	<u>10,460,647</u>

## **Reposessed collateral**

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

<b>Nature of assets</b>	<b>THE GROUP AND THE BANK</b>	
	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Residential properties.....	6,330	12,750
Others.....	14,908	15,644
Total .....	<u>21,238</u>	<u>28,394</u>

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

## **Market risk**

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

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

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

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

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

## **Management of market risk**

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

## **Currency risk**

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

The Group and the Bank do not have any significant foreign exchange risk as foreign exchange dealing is moderate. Day-to-day foreign exchange management is performed by the Treasury Management Department within approved limits.

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

The following table indicates the concentration of currency risk at the end of each reporting dates:

THE GROUP						
	HK\$	US\$	MOP	RMB	Others	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2009						
Assets						
Cash and short-term funds .....	10,057,501	2,948,685	153,935	663,826	1,224,733	15,048,680
Placements with banks and other financial institutions .....	1,300,101	814,275	—	—	700,190	2,814,566
Derivative financial instruments..	331	—	—	—	—	331
Financial assets at fair value through profit or loss.....	494,341	82,389	—	—	—	576,730
Available-for-sale securities .....	139,767	102,082	—	28,493	2,307	272,649
Held-to-maturity securities.....	6,467,308	4,489,302	—	209,049	5,788,807	16,954,466
Advances to customers.....	31,107,491	1,464,586	8,991	109,842	102,669	32,793,579
Advances to banks and other financial institutions .....	56,450	427	—	57,806	—	114,683
Other financial assets.....	343,693	5,254	623	7,160	2,743	359,473
Total financial assets .....	49,966,983	9,907,000	163,549	1,076,176	7,821,449	68,935,157
Liabilities						
Deposits and balances of banks and other financial institutions.....	1,138,836	272,881	—	—	36,001	1,447,718
Deposits from customers.....	43,153,899	8,848,480	116,050	932,138	7,737,848	60,788,415
Derivative financial instruments..	42,728	1,685	—	—	—	44,413
Loan capital.....	(2,176)	969,375	—	—	—	967,199
Other financial liabilities .....	528,602	10,858	300	782	15,474	556,016
Total financial liabilities.....	44,861,889	10,103,279	116,350	932,920	7,789,323	63,803,761
Net position - financial assets and liabilities .....	5,105,094	(196,279)	47,199	143,256	32,126	5,131,396
THE GROUP						
	HK\$	US\$	MOP	RMB	Others	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008						
Assets						
Cash and short-term funds .....	5,521,439	7,363,797	127,061	663,657	3,983,973	17,659,927
Placements with banks and other financial institutions .....	4,285,000	782,750	—	—	300,108	5,367,858
Derivative financial instruments..	429	—	—	—	—	429
Financial assets at fair value through profit or loss.....	599,320	81,360	—	—	—	680,680
Available-for-sale securities .....	81,457	84,692	—	28,493	1,885	196,527
Held-to-maturity securities.....	4,485,688	3,366,209	—	163,432	1,712,356	9,727,685
Advances to customers.....	31,588,692	1,463,522	17,982	67,497	106,934	33,244,627
Advances to banks and other financial institutions .....	56,460	481	—	59,471	—	116,412
Other financial assets.....	98,343	161,524	590	3,415	9,931	273,803
Total financial assets .....	46,716,828	13,304,335	145,633	985,965	6,115,187	67,267,948
Liabilities						
Deposits and balances of banks and other financial institutions.....	1,114,675	332,181	—	—	78,653	1,525,509
Deposits from customers.....	40,452,603	11,944,793	96,525	870,132	6,037,607	59,401,660
Derivative financial instruments..	39,303	—	—	—	—	39,303
Loan capital.....	(3,296)	968,750	—	—	—	965,454
Other financial liabilities .....	413,159	37,181	360	2,695	23,986	477,381
Total financial liabilities.....	42,016,444	13,282,905	96,885	872,827	6,140,246	62,409,307
Net position - financial assets and liabilities .....	4,700,384	21,430	48,748	113,138	(25,059)	4,858,641

THE BANK						
	HK\$	US\$	MOP	RMB	Others	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2009						
Assets						
Cash and short-term funds .....	10,014,998	2,948,685	153,935	663,826	1,224,733	15,006,177
Placements with banks and other financial institutions .....	1,300,101	814,275	—	—	700,190	2,814,566
Derivative financial instruments..	331	—	—	—	—	331
Financial assets at fair value through profit or loss.....	494,201	82,389	—	—	—	576,590
Available-for-sale securities .....	63,582	102,082	—	28,493	2,307	196,464
Held-to-maturity securities.....	6,467,308	4,489,302	—	209,049	5,788,807	16,954,466
Advances to customers.....	31,107,491	1,464,586	8,991	109,842	102,669	32,793,579
Advances to banks and other financial institutions .....	56,450	427	—	57,806	—	114,683
Other financial assets.....	75,933	4,538	623	3,337	2,743	87,174
Total financial assets .....	49,580,395	9,906,284	163,549	1,072,353	7,821,449	68,544,030
Liabilities						
Deposits and balances of banks and other financial institutions.....	1,138,836	272,881	—	—	36,001	1,447,718
Deposits from customers.....	43,151,009	8,848,480	116,050	932,138	7,737,848	60,785,525
Derivative financial instruments..	42,728	1,685	—	—	—	44,413
Loan capital.....	(2,176)	969,375	—	—	—	967,199
Other financial liabilities .....	1,008,107	10,858	300	782	15,474	1,035,521
Total financial liabilities.....	45,338,504	10,103,279	116,350	932,920	7,789,323	64,280,376
Net position - financial assets and liabilities .....	4,241,891	(196,995)	47,199	139,433	32,126	4,263,654

THE BANK						
	HK\$	US\$	MOP	RMB	Others	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008						
Assets						
Cash and short-term funds .....	5,479,058	7,363,797	127,061	663,657	3,983,973	17,617,546
Placements with banks and other financial institutions .....	4,285,000	782,750	—	—	300,108	5,367,858
Derivative financial instruments..	429	—	—	—	—	429
Financial assets at fair value through profit or loss.....	599,207	81,360	—	—	—	680,567
Available-for-sale securities .....	35,655	84,692	—	28,493	1,885	150,725
Held-to-maturity securities.....	4,485,688	3,366,209	—	163,432	1,712,356	9,727,685
Advances to customers.....	31,588,278	1,463,522	17,982	67,497	106,934	33,244,213
Advances to banks and other financial institutions .....	56,460	481	—	59,471	—	116,412
Other financial assets.....	25,573	83,495	590	830	9,931	120,419
Total financial assets .....	46,555,348	13,226,306	145,633	983,380	6,115,187	67,025,854
Liabilities						
Deposits and balances of banks and other financial institutions.....	1,114,675	332,181	—	—	78,653	1,525,509
Deposits from customers.....	40,449,370	11,944,793	96,525	870,132	6,037,607	59,398,427
Derivative financial instruments..	39,303	—	—	—	—	39,303
Loan capital.....	(3,296)	968,750	—	—	—	965,454
Other financial liabilities .....	938,354	37,181	360	2,695	23,986	1,002,576
Total financial liabilities.....	42,538,406	13,282,905	96,885	872,827	6,140,246	62,931,269
Net position - financial assets and liabilities .....	4,016,942	(56,599)	48,748	110,553	(25,059)	4,094,585



## Foreign currency sensitivity

The Group and the Bank are mainly exposed to US dollars, Renminbi and Macau Pataca. The following table details the Group's and the Bank's sensitivity to a 1 per cent change in Hong Kong dollars against the US dollars, and 10 percent change in Hong Kong dollars against Renminbi and Macau Pataca. The respective percentages are the rates used when reporting foreign currency risk internally to key management personnel and represent management's assessment of the possible change in foreign exchange rates. The sensitivity analyses of the Group's and the Bank's exposure to foreign currency risk at the end of the reporting period has been determined by adjusting their translation at the year end.

	Change in currency rate					
	US Dollars		Renminbi		Macau Pataca	
	<i>Appreciate +1%</i>	<i>Depreciate -1%</i>	<i>Appreciate +10%</i>	<i>Depreciate -10%</i>	<i>Appreciate +10%</i>	<i>Depreciate -10%</i>
<b>THE GROUP</b>						
Hong Kong dollars equivalents (HK\$'000)						
<b>2009</b>						
Profit after tax .....	(2,345)	2,345	520	(520)	(135)	135
Other comprehensive income.....	<u>2,621</u>	<u>(2,621)</u>	<u>16,914</u>	<u>(16,914)</u>	<u>4,855</u>	<u>(4,855)</u>
<b>2008</b>						
Profit after tax .....	(2,482)	2,482	129	(129)	20	(20)
Other comprehensive income.....	<u>2,445</u>	<u>(2,445)</u>	<u>16,768</u>	<u>(16,768)</u>	<u>4,855</u>	<u>(4,855)</u>
<b>THE BANK</b>						
<b>2009</b>						
Profit after tax .....	(1,572)	1,572	138	(138)	(135)	135
Other comprehensive income.....	<u>1,841</u>	<u>(1,841)</u>	<u>14,210</u>	<u>(14,210)</u>	<u>4,855</u>	<u>(4,855)</u>
<b>2008</b>						
Profit after tax .....	(2,475)	2,475	(130)	130	20	(20)
Other comprehensive income.....	<u>1,658</u>	<u>(1,658)</u>	<u>14,193</u>	<u>(14,193)</u>	<u>4,855</u>	<u>(4,855)</u>

Numbers in bracket mean decrease.

## Interest rate risk

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

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

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

THE GROUP						
	Up to 3 months	3 - 12 months	1 - 5 years	Over 5 years	Non-interest bearing	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2009						
Assets						
Cash and short-term funds .....	14,528,955	169,926	—	—	349,799	15,048,680
Placements with banks and other financial institutions .....	652,017	2,162,549	—	—	—	2,814,566
Derivative financial instruments..	—	—	—	—	331	331
Financial assets at fair value through profit or loss.....	468,916	—	25,285	—	82,529	576,730
Available-for-sale securities .....	92,272	—	—	—	180,377	272,649
Held-to-maturity securities.....	10,206,384	2,653,126	4,092,956	—	2,000	16,954,466
Advances to customers.....	32,292,508	393,591	55,196	2,776	49,508	32,793,579
Advances to banks and other financial institutions .....	75,710	38,000	—	—	973	114,683
Other financial assets.....	—	—	—	—	359,473	359,473
Total financial assets .....	58,316,762	5,417,192	4,173,437	2,776	1,024,990	68,935,157
Liabilities						
Deposits and balances of banks and other financial institutions.....	1,437,745	—	—	—	9,973	1,447,718
Deposits from customers.....	51,352,821	4,488,710	156,051	—	4,790,833	60,788,415
Derivative financial instruments..	—	—	—	—	44,413	44,413
Loan capital.....	967,199	—	—	—	—	967,199
Other financial liabilities .....	—	—	—	—	556,016	556,016
Total financial liabilities .....	53,757,765	4,488,710	156,051	—	5,401,235	63,803,761
Net position - financial assets and liabilities .....	4,558,997	928,482	4,017,386	2,776	(4,376,245)	5,131,396

THE GROUP						
	Up to 3 months	3 - 12 months	1 - 5 years	Over 5 years	Non-interest bearing	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008						
Assets						
Cash and short-term funds .....	16,941,384	271,937	—	—	446,606	17,659,927
Placements with banks and other financial institutions .....	4,449,267	918,591	—	—	—	5,367,858
Derivative financial instruments..	—	—	—	—	429	429
Financial assets at fair value through profit or loss.....	599,208	—	—	—	81,472	680,680
Available-for-sale securities .....	35,754	—	—	—	160,773	196,527
Held-to-maturity securities.....	7,408,355	2,293,174	24,156	—	2,000	9,727,685
Advances to customers.....	32,309,117	737,016	58,967	3,106	136,421	33,244,627
Advances to banks and other financial institutions .....	85,063	30,408	—	—	941	116,412
Other financial assets.....	—	—	—	—	273,803	273,803
Total financial assets .....	61,828,148	4,251,126	83,123	3,106	1,102,445	67,267,948
Liabilities						
Deposits and balances of banks and other financial institutions.....	1,514,356	—	—	—	11,153	1,525,509
Deposits from customers.....	52,972,817	3,416,549	4,621	—	3,007,673	59,401,660
Derivative financial instruments..	—	—	—	—	39,303	39,303
Loan capital.....	965,454	—	—	—	—	965,454
Other financial liabilities .....	—	—	—	—	477,381	477,381
Total financial liabilities .....	55,452,627	3,416,549	4,621	—	3,535,510	62,409,307
Net position - financial assets and liabilities .....	6,375,521	834,577	78,502	3,106	(2,433,065)	4,858,641

THE BANK						
	Up to 3 months	3 - 12 months	1 - 5 years	Over 5 years	Non-interest bearing	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2009						
Assets						
Cash and short-term funds .....	14,468,006	169,926	—	—	368,245	15,006,177
Placements with banks and other financial institutions .....	652,017	2,162,549	—	—	—	2,814,566
Derivative financial instruments..	—	—	—	—	331	331
Financial assets at fair value through profit or loss.....	468,916	—	25,285	—	82,389	576,590
Available-for-sale securities .....	92,272	—	—	—	104,192	196,464
Held-to-maturity securities.....	10,206,384	2,653,126	4,092,956	—	2,000	16,954,466
Advances to customers.....	32,292,508	393,591	55,196	2,776	49,508	32,793,579
Advances to bank and other financial institutions .....	75,710	38,000	—	—	973	114,683
Other financial assets.....	—	—	—	—	87,174	87,174
Total financial assets .....	58,255,813	5,417,192	4,173,437	2,776	694,812	68,544,030
Liabilities						
Deposits and balances of banks and other financial institutions.....	1,437,745	—	—	—	9,973	1,447,718
Deposits from customers.....	51,349,931	4,488,710	156,051	—	4,790,833	60,785,525
Derivative financial instruments..	—	—	—	—	44,413	44,413
Loan capital.....	967,199	—	—	—	—	967,199
Other financial liabilities .....	735,825	20,446	—	—	279,250	1,035,521
Total financial liabilities .....	54,490,700	4,509,156	156,051	—	5,124,469	64,280,376
Net position - financial assets and liabilities .....	3,765,113	908,036	4,017,386	2,776	(4,429,657)	4,263,654

THE BANK						
	Up to 3 months	3 - 12 months	1 - 5 years	Over 5 years	Non-interest bearing	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008						
Assets						
Cash and short-term funds .....	16,882,390	271,937	—	—	463,219	17,617,546
Placements with banks and other financial institutions .....	4,449,267	918,591	—	—	—	5,367,858
Derivative financial instruments..	—	—	—	—	429	429
Financial assets at fair value through profit or loss.....	599,207	—	—	—	81,360	680,567
Available-for-sale securities .....	35,754	—	—	—	114,971	150,725
Held-to-maturity securities.....	7,408,355	2,293,174	24,156	—	2,000	9,727,685
Advances to customers.....	32,308,703	737,016	58,967	3,106	136,421	33,244,213
Advances to bank and other financial institutions .....	85,063	30,408	—	—	941	116,412
Other financial assets.....	—	—	—	—	120,419	120,419
Total financial assets .....	61,768,739	4,251,126	83,123	3,106	919,760	67,025,854
Liabilities						
Deposits and balances of banks and other financial institutions.....	1,514,356	—	—	—	11,153	1,525,509
Deposits from customers.....	52,969,584	3,416,549	4,621	—	3,007,673	59,398,427
Derivative financial instruments..	—	—	—	—	39,303	39,303
Loan capital.....	965,454	—	—	—	—	965,454
Other financial liabilities .....	697,853	—	—	—	304,723	1,002,576
Total financial liabilities .....	56,147,247	3,416,549	4,621	—	3,362,852	62,931,269
Net position - financial assets and liabilities .....	5,621,492	834,577	78,502	3,106	(2,443,092)	4,094,585

### Interest rate sensitivity

The sensitivity analyses below have been determined based on the exposure to interest rates at the reporting date and the stipulated change taking place at the beginning of the financial year and held constant throughout the reporting period. A 100 basis point change in upwards and 10 basis point 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.

	2009		2008	
	Change in basis points		Change in basis points	
	+100	-10	+100	-100
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>THE GROUP</b>				
Profit after tax .....	48,804	(4,880)	59,773	(59,773)
Other comprehensive income.....	<u>(2,293)</u>	<u>229</u>	<u>(14)</u>	<u>14</u>
<b>THE BANK</b>				
Profit after tax .....	48,222	(4,822)	59,209	(59,209)
Other comprehensive income.....	<u>(2,293)</u>	<u>229</u>	<u>(14)</u>	<u>14</u>

Numbers in bracket mean decrease.

### Price risk

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

### Price sensitivity

	2009		2008	
	Change in price		Change in price	
	+10%	-10%	+10%	-10%
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>THE GROUP</b>				
Profit after tax .....	54,740	(54,740)	31,355	(31,355)
Other comprehensive income.....	<u>23,575</u>	<u>(23,575)</u>	<u>13,356</u>	<u>(13,356)</u>
<b>THE BANK</b>				
Profit after tax .....	52,036	(52,036)	31,355	(31,355)
Other comprehensive income.....	<u>16,353</u>	<u>(16,353)</u>	<u>9,173</u>	<u>(9,173)</u>

Numbers in bracket mean decrease.

### Liquidity risk

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

### Management of liquidity risk

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

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

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

THE GROUP								
	Repayable on demand	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
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2009								
Deposits and balances of banks and other financial institutions.....	10,218	1,437,850	19	2	—	—	—	1,448,089
Deposits from customers.....	24,493,419	23,301,777	8,390,709	4,511,942	158,631	—	—	60,856,478
Loan capital.....	—	510	2,869	8,606	980,850	—	—	992,835
Other financial liabilities .....	461,497	7,263	13,015	25,938	16,059	—	—	523,772
Total undiscounted financial liabilities .....	24,965,134	24,747,400	8,406,612	4,546,488	1,155,540	—	—	63,821,174
At 31 December 2008								
Deposits and balances of banks and other financial institutions.....	71,495	1,458,584	42	203	—	—	—	1,530,324
Deposits from customers.....	16,860,684	30,128,383	9,073,136	3,427,260	54,953	—	42,445	59,586,861
Loan capital.....	—	1,228	6,905	20,716	1,023,993	—	—	1,052,842
Other financial liabilities .....	295,882	2,438	40,368	19,859	16,812	—	—	375,359
Total undiscounted financial liabilities .....	17,228,061	31,590,633	9,120,451	3,468,038	1,095,758	—	42,445	62,545,386

**THE BANK**

	<b>Repayable on demand</b>	<b>Repayable within 1 month</b>	<b>Repayable after 1 month but within 3 months</b>	<b>Repayable after 3 months but within 1 year</b>	<b>Repayable after 1 year but within 5 years</b>	<b>Repayable after 5 years</b>	<b>Undated</b>	<b>Total</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 31 December 2009								
Deposits and balances of banks and other financial institutions.....	10,218	1,437,850	19	2	—	—	—	1,448,089
Deposits from customers.....	24,493,329	23,299,216	8,390,379	4,511,942	158,631	—	—	60,853,497
Loan capital.....	—	510	2,869	8,606	980,850	—	—	992,835
Other financial liabilities .....	506,881	391,937	75,910	28,640	—	—	—	1,003,368
Total undiscounted financial liabilities .....	<u>25,010,428</u>	<u>25,129,513</u>	<u>8,469,177</u>	<u>4,549,190</u>	<u>1,139,481</u>	<u>—</u>	<u>—</u>	<u>64,297,789</u>
At 31 December 2008								
Deposits and balances of banks and other financial institutions.....	71,495	1,458,584	42	203	—	—	—	1,530,324
Deposits from customers.....	16,860,585	30,126,228	9,072,058	3,427,260	54,953	—	42,445	59,583,529
Loan capital.....	—	1,228	6,905	20,716	1,023,993	—	—	1,052,842
Other financial liabilities .....	443,049	390,800	62,101	4,703	—	—	—	900,653
Total undiscounted financial liabilities .....	<u>17,375,129</u>	<u>31,976,840</u>	<u>9,141,106</u>	<u>3,452,882</u>	<u>1,078,946</u>	<u>—</u>	<u>42,445</u>	<u>63,067,348</u>

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

**THE GROUP AND THE BANK**

	<b>Less than 1 month</b>	<b>1 - 3 months</b>	<b>3 months to 1 year</b>	<b>1 - 5 years</b>	<b>Over 5 years</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 31 December 2009					
Derivatives settled net Interest rate contracts.....	<u>(666)</u>	<u>401</u>	<u>(495)</u>	<u>(55,002)</u>	<u>—</u>
Derivatives settled gross					
Exchange rate contracts					
- inflow.....	7,053	49,762	1,015	—	—
- outflow .....	<u>(6,945)</u>	<u>(49,674)</u>	<u>(978)</u>	<u>—</u>	<u>—</u>
	<u>108</u>	<u>88</u>	<u>37</u>	<u>—</u>	<u>—</u>
At 31 December 2008					
Derivatives settled net					
Interest rate contracts.....	<u>(46)</u>	<u>1,361</u>	<u>(26,122)</u>	<u>(28,943)</u>	<u>—</u>
Derivatives settled gross					
Exchange rate contracts					
- inflow.....	28,090	8,146	158,239	—	—
- outflow .....	<u>(28,360)</u>	<u>(7,936)</u>	<u>(158,354)</u>	<u>—</u>	<u>—</u>
	<u>(270)</u>	<u>210</u>	<u>(115)</u>	<u>—</u>	<u>—</u>

## Off-statement of financial position

The dates of the contractual amounts of the Group's and the Bank's off-statement of financial position financial instruments that commit it to extending credit to customers and other facilities and financial guarantees are summarised in the table below:

THE GROUP				
	No later than 1 year	1-5 years	Over 5 years	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2009				
Loan commitments .....	14,508,583	—	—	14,508,583
Guarantee, acceptances and other financial facilities .....	1,074,429	—	—	1,074,429
Total .....	<u>15,583,012</u>	<u>—</u>	<u>—</u>	<u>15,583,012</u>
At 31 December 2008				
Loan commitments .....	14,529,659	—	—	14,529,659
Guarantee, acceptances and other financial facilities .....	1,014,062	—	—	1,014,062
Total .....	<u>15,543,721</u>	<u>—</u>	<u>—</u>	<u>15,543,721</u>
THE BANK				
	No later than 1 year	1-5 years	Over 5 years	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2009				
Loan commitments .....	14,508,583	—	—	14,508,583
Guarantee, acceptances and other financial facilities .....	1,074,429	—	—	1,074,429
Total .....	<u>15,583,012</u>	<u>—</u>	<u>—</u>	<u>15,583,012</u>
At 31 December 2008				
Loan commitments .....	14,529,659	—	—	14,529,659
Guarantee, acceptances and other financial facilities .....	1,014,062	—	—	1,014,062
Total .....	<u>15,543,721</u>	<u>—</u>	<u>—</u>	<u>15,543,721</u>

## Analysis of assets and liabilities by remaining maturity

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

THE GROUP								
	Repayable on demand	Repayable within 1 month (except those repayable on demand)	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
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2009								
Assets								
Cash and short-term funds .....	4,204,022	10,409,504	235,383	199,771	—	—	—	15,048,680
Placements with banks and other financial institutions .....	—	—	652,017	2,162,549	—	—	—	2,814,566
Derivative financial instruments .....	—	175	119	37	—	—	—	331
Financial assets at fair value through profit or loss								
- Held for trading .....	—	—	—	—	—	—	140	140
- Designated at fair value.	—	—	—	88,276	488,314	—	—	576,590
Available-for-sale securities ..	—	—	—	—	92,272	1,276	179,101	272,649
Held-to-maturity securities .....	—	4,142,804	1,431,063	4,141,778	7,238,821	—	—	16,954,466
Advances to customers .....	1,456,020	2,234,769	1,501,287	4,773,751	13,014,912	9,628,458	184,382	32,793,579
Advances to banks and other financial institutions .....	9,958	60,466	30,961	13,298	—	—	—	114,683
Other financial assets .....	341,785	86,790	22,146	35,886	703	—	(127,837)	359,473
Total financial assets .....	6,011,785	16,934,508	3,872,976	11,415,346	20,835,022	9,629,734	235,786	68,935,157
Liabilities								
Deposits and balances of banks and other financial institutions .....	10,218	1,437,500	—	—	—	—	—	1,447,718
Deposits from customers .....	24,492,361	23,282,401	8,369,759	4,487,837	156,057	—	—	60,788,415
Derivative financial instruments .....	—	296	20	1,373	42,724	—	—	44,413
Loan capital .....	—	—	—	—	—	967,199	—	967,199
Other financial liabilities .....	462,336	20,846	23,489	32,962	16,383	—	—	556,016
Total financial liabilities .....	24,964,915	24,741,043	8,393,268	4,522,172	215,164	967,199	—	63,803,761
Net position - financial assets and liabilities .....	(18,953,130)	(7,806,535)	(4,520,292)	6,893,174	20,619,858	8,662,535	235,786	5,131,396
Of which certificates of deposit included in:								
Held-to-maturity securities .....	—	—	—	67,510	280,000	—	—	347,510
Of which debt securities included in:								
Financial assets at fair value through profit or loss								
- Designated at fair value .....	—	—	—	88,276	488,314	—	—	576,590
Available-for-sale securities .....	—	—	—	—	92,272	1,276	—	93,548
Held-to-maturity securities .....	—	4,142,804	1,431,063	4,141,778	7,238,821	—	—	16,954,466
	—	4,142,804	1,431,063	4,230,054	7,819,407	1,276	—	17,624,604



THE GROUP

	Repayable on demand	Repayable within 1 month (except those repayable on demand)	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
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008								
Assets								
Cash and short-term funds ....	4,162,520	13,214,714	53,110	229,583	—	—	—	17,659,927
Placements with banks and other financial institutions .....	—	—	4,449,267	918,591	—	—	—	5,367,858
Derivative financial instruments .....	—	—	—	—	—	—	429	429
Financial assets at fair value through profit or loss								
- Held for trading .....	—	—	—	—	—	—	113	113
- Designated at fair value.	—	—	49,349	295,228	335,990	—	—	680,567
Available-for-sale securities ..	—	—	—	—	35,755	16,640	144,132	196,527
Held-to-maturity securities.....	—	1,201,359	1,349,389	3,295,114	3,876,303	3,520	2,000	9,727,685
Advances to customers .....	2,506,692	2,858,274	1,613,321	4,868,474	11,571,972	9,549,718	276,176	33,244,627
Advances to banks and other financial institutions .....	26,380	30,424	9,608	50,000	—	—	—	116,412
Other financial assets.....	178,911	115,575	42,484	39,503	6,691	—	(109,361)	273,803
Total financial assets .....	6,874,503	17,420,346	7,566,528	9,696,493	15,826,711	9,569,878	313,489	67,267,948
Liabilities								
Deposits and balances of banks and other financial institutions .....	71,494	1,454,015	—	—	—	—	—	1,525,509
Deposits from customers.....	16,859,032	30,054,751	9,023,831	3,370,024	51,577	—	42,445	59,401,660
Derivative financial instruments .....	—	—	—	—	—	—	39,303	39,303
Loan capital.....	—	—	—	—	—	965,454	—	965,454
Other financial liabilities .....	297,326	62,987	63,948	36,138	16,982	—	—	477,381
Total financial liabilities.....	17,227,852	31,571,753	9,087,779	3,406,162	68,559	965,454	81,748	62,409,307
Net position - financial assets and liabilities.....	(10,353,349)	(14,151,407)	(1,521,251)	6,290,331	15,758,152	8,604,424	231,741	4,858,641
Of which certificates of deposit included in:								
Held-to-maturity securities....	—	—	—	467,970	90,750	—	—	558,720
Of which debt securities included in:								
Financial assets at fair value through profit or loss								
- Designated at fair value .....	—	—	49,349	295,228	335,990	—	—	680,567
Available-for-sale securities.....	—	—	—	—	35,755	16,640	—	52,395
Held-to-maturity securities .....	—	1,201,359	1,349,389	3,295,114	3,876,303	3,520	2,000	9,727,685
	—	1,201,359	1,398,738	3,590,342	4,248,048	20,160	2,000	10,460,647

THE BANK

	Repayable on demand	Repayable within 1 month (except those repayable on demand)	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
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2009								
Assets								
Cash and short-term funds ....	4,198,892	10,372,131	235,383	199,771	—	—	—	15,006,177
Placements with banks and other financial institutions .....	—	—	652,017	2,162,549	—	—	—	2,814,566
Derivative financial instruments .....	—	175	119	37	—	—	—	331
Financial assets at fair value through profit or loss								
- Designated at fair value.	—	—	—	88,276	488,314	—	—	576,590
Available-for-sale securities ..	—	—	—	—	92,272	1,276	102,916	196,464
Held-to-maturity securities.....	—	4,142,804	1,431,063	4,141,778	7,238,821	—	—	16,954,466
Advances to customers .....	1,456,020	2,234,769	1,501,287	4,773,751	13,014,912	9,628,458	184,382	32,793,579
Advances to banks and other financial institutions .....	9,958	60,466	30,961	13,298	—	—	—	114,683
Other financial assets.....	72,936	89,068	21,392	33,239	703	—	(130,164)	87,174
Total financial assets .....	5,737,806	16,899,413	3,872,222	11,412,699	20,835,022	9,629,734	157,134	68,544,030
Liabilities								
Deposits and balances of banks and other financial institutions .....	10,218	1,437,500	—	—	—	—	—	1,447,718
Deposits from customers.....	24,492,362	23,279,840	8,369,429	4,487,837	156,057	—	—	60,785,525
Derivative financial instruments .....	—	296	20	1,373	42,724	—	—	44,413
Loan capital.....	—	—	—	—	—	967,199	—	967,199
Other financial liabilities .....	507,629	405,520	86,384	35,664	324	—	—	1,035,521
Total financial liabilities.....	25,010,209	25,123,156	8,455,833	4,524,874	199,105	967,199	—	64,280,376
Net position - financial assets and liabilities.....	(19,272,403)	(8,223,743)	(4,583,611)	6,887,825	20,635,917	8,662,535	157,134	4,263,654
Of which certificates of deposit included in:								
Held-to-maturity securities....	—	—	—	67,510	280,000	—	—	347,510
Of which debt securities included in:								
Financial assets at fair value through profit or loss								
- Designated at fair value .....	—	—	—	88,276	488,314	—	—	576,590
Available-for-sale securities.....	—	—	—	—	92,272	1,276	—	93,548
Held-to-maturity securities .....	—	4,142,804	1,431,063	4,141,778	7,238,821	—	—	16,954,466
	—	4,142,804	1,431,063	4,230,054	7,819,407	1,276	—	17,624,604

THE BANK

	Repayable on demand	Repayable within 1 month (except those repayable on demand)	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
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008								
Assets								
Cash and short-term funds ....	4,157,401	13,177,451	53,111	229,583	—	—	—	17,617,546
Placements with banks and other financial institutions .....	—	—	4,449,267	918,591	—	—	—	5,367,858
Derivative financial instruments .....	—	—	—	—	—	—	429	429
Financial assets at fair value through profit or loss								
- Designated at fair value.	—	—	49,349	295,228	335,990	—	—	680,567
Available-for-sale securities ..	—	—	—	—	35,755	16,640	98,330	150,725
Held-to-maturity securities.....	—	1,201,359	1,349,389	3,295,114	3,876,303	3,520	2,000	9,727,685
Advances to customers .....	2,506,692	2,858,264	1,613,301	4,868,383	11,571,679	9,549,718	276,176	33,244,213
Advances to banks and other financial institutions .....	26,380	30,424	9,608	50,000	—	—	—	116,412
Other financial assets.....	31,124	114,216	42,213	37,813	6,691	—	(111,638)	120,419
Total financial assets .....	6,721,597	17,381,714	7,566,238	9,694,712	15,826,418	9,569,878	265,297	67,025,854
Liabilities								
Deposits and balances of banks and other financial institutions .....	71,494	1,454,015	—	—	—	—	—	1,525,509
Deposits from customers.....	16,859,032	30,052,596	9,022,753	3,370,024	51,577	—	42,445	59,398,427
Derivative financial instruments .....	—	—	—	—	—	—	39,303	39,303
Loan capital.....	—	—	—	—	—	965,454	—	965,454
Other financial liabilities .....	444,394	451,349	85,681	20,982	170	—	—	1,002,576
Total financial liabilities.....	17,374,920	31,957,960	9,108,434	3,391,006	51,747	965,454	81,748	62,931,269
Net position - financial assets and liabilities.....	(10,653,323)	(14,576,246)	(1,542,196)	6,303,706	15,774,671	8,604,424	183,549	4,094,585
Of which certificates of deposit included in:								
Held-to-maturity securities....	—	—	—	467,970	90,750	—	—	558,720
Of which debt securities included in:								
Financial assets at fair value through profit or loss								
- Designated at fair value .....	—	—	49,349	295,228	335,990	—	—	680,567
Available-for-sale securities.....	—	—	—	—	35,755	16,640	—	52,395
Held-to-maturity securities .....	—	1,201,359	1,349,389	3,295,114	3,876,303	3,520	2,000	9,727,685
	—	1,201,359	1,398,738	3,590,342	4,248,048	20,160	2,000	10,460,647

## Fair value of financial assets and liabilities

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

THE GROUP AND THE BANK				
	Carrying value		Fair value	
	2009	2008	2009	2008
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Financial assets				
- Held-to-maturity securities .....	<u>16,954,466</u>	<u>9,727,685</u>	<u>16,975,145</u>	<u>9,658,947</u>
Financial liabilities				
- Loan capital .....	<u>967,199</u>	<u>965,454</u>	<u>872,438</u>	<u>775,000</u>

The fair value is based on quoted market prices provided by pricing service providers and market dealers.

## Fair value measurements recognised in the statement of financial position

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value 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).

THE GROUP				
	Fair value hierarchy			
	Level 1	Level 2	Level 3	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Financial assets held for trading .....	140	—	—	140
Financial assets designated at fair value through profit or loss.....	444,196	—	132,394	576,590
Available-for-sale securities .....	197,147	—	75,502	272,649
Derivative financial instruments not used for hedging .....	—	(43,954)	—	(43,954)
Derivative financial instruments used for hedging .....	—	(128)	—	(128)
Total .....	<u>641,483</u>	<u>(44,082)</u>	<u>207,896</u>	<u>805,297</u>

THE BANK				
	Fair value hierarchy			
	Level 1	Level 2	Level 3	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Financial assets held for trading .....	—	—	—	—
Financial assets designated at fair value through profit or loss.....	444,196	—	132,394	576,590
Available-for-sale securities .....	124,930	—	71,534	196,464
Derivative financial instruments not used for hedging .....	—	(43,954)	—	(43,954)
Derivative financial instruments used for hedging .....	—	(128)	—	(128)
Total .....	<u>569,126</u>	<u>(44,082)</u>	<u>203,928</u>	<u>728,972</u>

**Reconciliation of Level 3 fair value measurements of financial assets:**

	THE GROUP			THE BANK		
	Financial assets designated at fair value through profit or loss	Available- for-sale securities	Total	Financial assets designated at fair value through profit or loss	Available- for-sale securities	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Balance at 1 January 2009 .....	316,460	115,360	431,820	316,460	111,392	427,852
Total net gains / (losses) recognised in profit or loss .....	15,885	(43,571)	(27,686)	15,885	(43,571)	(27,686)
Total net gains / (losses) recognised in the revaluation reserve .....	—	1,570	1,570	—	1,570	1,570
Purchases .....	—	2,195	2,195	—	2,195	2,195
Disposals .....	(200,000)	—	(200,000)	(200,000)	—	(200,000)
Net transfers out of Level 3 .....	—	—	—	—	—	—
Foreign exchange rate movements...	49	(52)	(3)	49	(52)	(3)
Balance at 31 December 2009 .....	<u>132,394</u>	<u>75,502</u>	<u>207,896</u>	<u>132,394</u>	<u>71,534</u>	<u>203,928</u>

The majority of the Group's and the Bank's investments are valued based on quoted market information or observable market data. A small percentage (0.3%) of total assets recorded at fair value, are based on estimates and recorded as Level 3 investments. Whilst such valuations are sensitive to estimates, it is believed that changing one or more of the assumptions to reasonably possible alternative assumptions would not have a material impact on the Group's and Bank's financial position.

Of the total net losses for the year included in profit or loss, HK\$53,790,000 related to investments held at the end of the reporting period.

**8. NET INTEREST INCOME**

	2009	2008
	HK\$'000	HK\$'000
Interest income		
Short term funds and placements .....	168,991	606,587
Investments in securities .....	333,591	476,408
Loans and advances .....	<u>682,340</u>	<u>1,088,341</u>
	<u>1,184,922</u>	<u>2,171,336</u>
Interest expense		
Deposits and balances from banks and customers .....	(341,855)	(1,264,888)
Loan capital in issue .....	<u>(19,736)</u>	<u>(42,122)</u>
	<u>(361,591)</u>	<u>(1,307,010)</u>
Net interest income .....	<u>823,331</u>	<u>864,326</u>
Included within interest income		
Interest income on impaired loans and advances .....	<u>3,676</u>	<u>4,415</u>

Included within interest income and interest expense are HK\$1,180,125,000 (2008: HK\$2,156,946,000) and HK\$361,591,000 (2008: HK\$1,307,010,000) for financial assets and financial liabilities that are not at fair value through profit or loss, respectively.

## 9. NET FEE AND COMMISSION INCOME

	2009	2008
	HK\$'000	HK\$'000
Fees and commission income		
Securities dealings .....	208,063	139,266
Credit lines .....	12,683	8,034
Trade finance .....	11,290	14,409
Credit card services .....	47,560	49,214
Agency services .....	18,933	46,586
Others .....	8,770	7,711
Total fees and commission income .....	307,299	265,220
Less: Fees and commission expense .....	(43,670)	(48,419)
Net fees and commission income .....	<u>263,629</u>	<u>216,801</u>
of which:		
Net fee income, other than amounts included in determining the effective interest rate, arising from financial assets or financial liabilities that are not held for trading nor designated at fair value through profit or loss		
- fee income .....	75,099	73,911
- fee expense .....	(41,953)	(42,648)
	<u>33,146</u>	<u>31,263</u>

## 10. NET GAINS (LOSSES) ON FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

	2009	2008
	HK\$'000	HK\$'000
Net gains (losses) on financial assets at fair value through profit or loss		
- designated at fair value through profit or loss .....	76,827	(123,908)
- held for trading .....	51	75,609
Net losses on fair value hedge .....	(118)	—
	<u>76,760</u>	<u>(48,299)</u>

## 11. OTHER OPERATING INCOME

	2009	2008
	HK\$'000	HK\$'000
Dividend income		
Listed investments .....	4,585	9,773
Unlisted investments .....	3,482	3,080
Net gains on dealing in foreign currencies .....	36,300	42,985
Gross rents from investment properties .....	14,105	13,035
Less: Outgoings .....	(1,210)	(948)
Net rental income .....	12,895	12,087
Safe deposit box rentals .....	26,415	25,702
Insurance underwriting profit .....	11,857	8,336
Other banking services income .....	41,983	41,508
Others .....	8,705	3,095
	<u>146,222</u>	<u>146,566</u>

## 12. OPERATING EXPENSES

	2009	2008
	HK\$'000	HK\$'000
Actuarial loss on retirement scheme .....	—	21,862
Release of prepaid lease payments for land .....	6,075	6,104
Auditor's remuneration .....	3,935	3,678
Staff costs (including directors' emoluments)		
Salaries and other costs .....	376,887	393,953
Retirement benefits scheme contributions .....	19,586	29,779
Total staff costs .....	396,473	423,732
Depreciation .....	47,213	43,925
Premises and equipment expenses, excluding		
Depreciation and amortisation		
Rentals and rates for premises .....	42,724	38,896
Others .....	20,698	22,247
Expenses relating to Minibonds Repurchase Scheme* .....	287,717	—
Other operating expenses .....	173,580	211,987
	<u>978,415</u>	<u>772,431</u>

Included in the premises and equipment expenses are minimum lease payments under operating lease of HK\$37,335,000 (2008: HK\$34,655,000).

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\* The Bank announced on 22 July 2009 that it had, without admission of any liability, entered into an agreement ("Repurchase Scheme") with the Securities and Futures Commission, the Hong Kong Monetary Authority and fifteen other distributing banks in relation to the repurchase of the Lehman Brothers Minibonds ("Minibonds"). The amount paid to repurchase the Minibonds together with other expenses under the Repurchase Scheme, amounting to HK\$287,717,000 in 2009, represents expenses incurred by the Bank to compensate its customers who had suffered from the collapse of the Lehman Brothers Group.

### 13. DIRECTORS' AND EMPLOYEES' EMOLUMENTS

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

	2009				2008			
	Fees	Salaries and other benefits	Contribution to retirement benefits scheme	Total	Fees	Salaries and other benefits	Contribution to retirement benefits scheme	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Executive directors								
Liu Lit Man.....	108	5,085	188	5,381	120	5,437	350	5,907
Liu Lit Mo .....	75	487	26	588	70	487	45	602
Liu Lit Chi.....	70	5,293	143	5,506	70	5,536	259	5,865
Don Tit Shing Liu .....	70	2,728	142	2,940	70	2,484	244	2,798
Lau Wai Man.....	70	2,224	128	2,422	70	2,328	232	2,630
Wilfred Chun Ning Liu.....	70	2,140	92	2,302	70	2,345	167	2,582
Tsang Chiu Wing .....	70	2,041	114	2,225	70	2,118	188	2,376
Wong Har Kar .....	70	1,950	104	2,124	70	2,020	155	2,245
Frank Shui Sang Jin .....	—	—	—	—	44	1,354	135	1,533
Total executive directors' emoluments .....	603	21,948	937	23,488	654	24,109	1,775	26,538
Non-executive directors								
Timothy George Freshwater.....	130	80	—	210	100	80	—	180
Wang Xiaoming .....	70	—	—	70	58	—	—	58
Andrew Liu .....	70	30	—	100	70	29	—	99
Eiichi Yoshikawa .....	70	—	—	70	70	—	—	70
Christopher Kwun Shing Liu .....	70	—	—	70	70	—	—	70
Alfred Cheuk Yu Chow.....	130	—	—	130	100	—	—	100
Meng Qinghui .....	70	—	—	70	58	—	—	58
Xu Minjie.....	—	—	—	—	12	—	—	12
Wang Zhi.....	—	—	—	—	12	—	—	12
Total non-executive directors' emoluments..	610	110	—	720	550	109	—	659
Independent non-executive directors								
Robin Yau Hing Chan.....	130	—	—	130	100	—	—	100
Wanchai Chiranakhorn.....	130	—	—	130	100	—	—	100
Cheng Yuk Wo.....	130	—	—	130	100	—	—	100
Andrew Chiu Cheung Ma .....	130	—	—	130	100	—	—	100
Total independent non-executive directors' emoluments.....	520	—	—	520	400	—	—	400
Total.....	1,733	22,058	937	24,728	1,604	24,218	1,775	27,597

The five highest paid individuals in the Group in 2009 and 2008 were all directors of the Bank and details of their emoluments are included in above. No directors waived any emoluments in the years ended 31 December 2009 and 31 December 2008.



## 14. TAXATION

	2009	2008
	HK\$'000	HK\$'000
The tax charge comprises:		
Hong Kong Profits Tax		
— current year .....	37,056	11,254
— (over)underprovision in prior years .....	(1,352)	325
	35,704	11,579
Overseas taxation.....	1,898	6,027
Deferred tax ( <i>note 30</i> ) .....	(4,967)	11,069
	<u>32,635</u>	<u>28,675</u>

Hong Kong Profits Tax is calculated at 16.5% (2008: 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:

	2009	2008
	HK\$'000	HK\$'000
Profit before taxation .....	264,383	89,295
Tax at the domestic income tax rate of 16.5% (2008: 16.5%).....	43,624	14,734
Tax effect of share of (profit) loss of jointly controlled entities.....	(5,126)	14,890
Tax effect of expenses not deductible for tax purpose .....	7,271	20,044
Tax effect of income not taxable for tax purpose .....	(11,700)	(21,746)
(Over)under provision in prior years .....	(1,595)	1,258
Effect of different tax rates of subsidiaries operating in other jurisdictions.....	161	(550)
Effect of changes in tax rates of deferred tax.....	—	45
Tax charge for the year .....	<u>32,635</u>	<u>28,675</u>

## 15. DIVIDENDS

	2009	2008
	HK\$'000	HK\$'000
Dividends recognised as distribution during the year:		
2009 Interim - HK\$0.08 (2008: 2008 Interim - HK\$0.15) per share .....	34,800	65,250
2008 Final - HK\$0.05 (2008: 2007 Final - HK\$0.44) per share.....	21,750	191,400
	<u>56,550</u>	<u>256,650</u>

The final dividend of HK\$0.20 per share in respect of the current financial year (2008: HK\$0.05) has been proposed by the directors and is subject to approval by the shareholders in the next annual general meeting.

## 16. EARNINGS PER SHARE

The calculation of basic earnings per share is based on the profit attributable to shareholders of the Bank of HK\$231,748,000 (2008: HK\$60,620,000) and on 435,000,000 (2008: 435,000,000) ordinary shares in issue during the year.

There was no dilution of earnings per share as no potential ordinary shares were in issue for the year ended 31 December 2009 (2008: nil).

## 17. CASH AND SHORT-TERM FUNDS

	THE GROUP		THE BANK	
	2009	2008	2009	2008
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Cash and balances with banks and other financial institutions.....	4,427,240	4,087,415	4,422,110	4,082,297
Money at call and short notice.....	6,704,160	13,180,425	6,666,787	13,143,162
Exchange fund bills .....	3,917,280	392,087	3,917,280	392,087
	<u>15,048,680</u>	<u>17,659,927</u>	<u>15,006,177</u>	<u>17,617,546</u>

## 18. DERIVATIVE FINANCIAL INSTRUMENTS

THE GROUP AND THE BANK						
	2009			2008		
	Notional amount	Fair values		Notional amount	Fair values	
		Assets	Liabilities		Assets	Liabilities
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Derivatives held for trading						
- Foreign currency related contracts.....	57,830	331	131	194,475	429	460
- Interest rate swaps .....	535,100	—	44,154	990,750	—	38,843
Derivatives held for hedging						
- Interest rate swaps .....	54,285	—	128	—	—	—
		<u>331</u>	<u>44,413</u>		<u>429</u>	<u>39,303</u>

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

THE GROUP AND THE BANK						
	2009			2008		
	Notional amount	Replacement cost	Credit risk weighted amount	Notional amount	Replacement cost	Credit risk weighted amount
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Exchange rate contracts .....	57,830	331	535	194,475	429	876
Interest rate contracts.....	589,385	—	1,004	990,750	—	730
		<u>331</u>	<u>1,539</u>		<u>429</u>	<u>1,606</u>

The derivative financial instruments including exchange rate contracts and interest rate contracts have been recognised on statements of financial position at fair value.

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

During the year, the Group designates two interest rate swaps as fair value hedges of the fair value of available-for-sale securities. The purpose is to minimise its exposure to fair value changes of its fixed-rate bonds by swapping fixed-rate bonds from fixed rates to floating rates. The interest rate swaps and the corresponding fixed-rate bonds have the same terms and management of the Group considers that the interest rate swaps are highly effective hedging instruments.

During the year, the hedge was effective in hedging the fair value exposure to interest rate movements and as a result both the change in fair value of the bonds and the fair value of the interest rate swaps were included in profit and loss.

The fair value of the interest rate swaps are measured at the present value of future cash flows estimated and discounted based on the applicable yield curves derived from quoted interest rates.

Apart from the above two interest rate swaps designated as fair value hedges, all other derivative financial instruments do not qualify for hedge accounting for financial reporting but are managed in conjunction with the financial instruments designated at fair value through profit or loss.

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

## 19. INVESTMENTS IN SECURITIES

	THE GROUP					THE BANK				
	Financial assets at fair value through profit or loss					Financial assets at fair value through profit or loss				
	Held for trading	Designated at fair value	Available-for-sale securities	Held-to-maturity securities	Total	Held for trading	Designated at fair value	Available-for-sale securities	Held-to-maturity securities	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
2009										
Equity securities:										
Listed in Hong Kong.....	140	—	135,287	—	135,427	—	—	63,070	—	63,070
Listed overseas.....	—	—	6,912	—	6,912	—	—	6,912	—	6,912
	140	—	142,199	—	142,339	—	—	69,982	—	69,982
Unlisted .....	—	—	36,902	—	36,902	—	—	32,934	—	32,934
	140	—	179,101	—	179,241	—	—	102,916	—	102,916
Debt securities:										
Certificates of deposit.....	—	—	—	347,510	347,510	—	—	—	347,510	347,510
Structured products .....	—	576,590	—	—	576,590	—	576,590	—	—	576,590
Other debt securities - Unlisted .....	—	—	93,548	16,606,956	16,700,504	—	—	93,548	16,606,956	16,700,504
	—	576,590	93,548	16,954,466	17,624,604	—	576,590	93,548	16,954,466	17,624,604
Total:										
Listed in Hong Kong.....	140	—	135,287	—	135,427	—	—	63,070	—	63,070
Listed overseas.....	—	—	6,912	—	6,912	—	—	6,912	—	6,912
Unlisted .....	—	576,590	130,450	16,954,466	17,661,506	—	576,590	126,482	16,954,466	17,657,538
	140	576,590	272,649	16,954,466	17,803,845	—	576,590	196,464	16,954,466	17,727,520
Market value of listed securities:										
Listed in Hong Kong.....	140	—	135,287	—	135,427	—	—	63,070	—	63,070
Listed overseas.....	—	—	6,912	—	6,912	—	—	6,912	—	6,912
	140	—	142,199	—	142,339	—	—	69,982	—	69,982
As analysed by issuing entities:										
Central government and central banks.....	—	—	—	182,203	182,203	—	—	—	182,203	182,203
Public sector entities.....	—	—	54,947	56,328	111,275	—	—	54,947	56,328	111,275
Banks and other financial institutions.....	45	82,389	54,067	14,766,614	14,903,115	—	82,389	39,425	14,766,614	14,888,428
Corporate entities.....	95	494,201	155,225	1,949,321	2,598,842	—	494,201	97,650	1,949,321	2,541,172
Others .....	—	—	8,410	—	8,410	—	—	4,442	—	4,442
	140	576,590	272,649	16,954,466	17,803,845	—	576,590	196,464	16,954,466	17,727,520

Included in available-for-sale securities are financial instruments issued by structured investment vehicles with gross investment cost of approximately HK\$116,294,000 (2008: HK\$116,219,000). Impairment losses of HK\$115,018,000 (2008: HK\$99,579,000) has been recognised for these investments. All other available-for-sale securities and investments in securities are neither past due nor impaired.

Certain held-to-maturity certificates of deposit of approximately HK\$15,510,000 (2008: HK\$15,500,000) held by the San Francisco Branch of the Bank have been pledged to the State of California of the United States of America in compliance with the requirements of the California Financial Code.

	THE GROUP					THE BANK				
	Financial assets at fair value through profit or loss					Financial assets at fair value through profit or loss				
	Held for trading	Designated at fair value	Available-for-sale securities	Held-to-maturity securities	Total	Held for trading	Designated at fair value	Available-for-sale securities	Held-to-maturity securities	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
2008										
Equity securities:										
Listed in Hong Kong.....	113	—	76,976	—	77,089	—	—	35,142	—	35,142
Listed overseas.....	—	—	4,191	—	4,191	—	—	4,191	—	4,191
	113	—	81,167	—	81,280	—	—	39,333	—	39,333
Unlisted .....	—	—	62,965	—	62,965	—	—	58,997	—	58,997
	113	—	144,132	—	144,245	—	—	98,330	—	98,330
Debt securities:										
Certificates of deposit .....	—	—	—	558,720	558,720	—	—	—	558,720	558,720
Structured products .....	—	680,567	—	—	680,567	—	680,567	—	—	680,567
Other debt securities - Unlisted .....	—	—	52,395	9,168,965	9,221,360	—	—	52,395	9,168,965	9,221,360
	—	680,567	52,395	9,727,685	10,460,647	—	680,567	52,395	9,727,685	10,460,647
Total:										
Listed in Hong Kong.....	113	—	76,976	—	77,089	—	—	35,142	—	35,142
Listed overseas.....	—	—	4,191	—	4,191	—	—	4,191	—	4,191
Unlisted .....	—	680,567	115,360	9,727,685	10,523,612	—	680,567	111,392	9,727,685	10,519,644
	113	680,567	196,527	9,727,685	10,604,892	—	680,567	150,725	9,727,685	10,558,977
Market value of listed securities:										
Listed in Hong Kong.....	113	—	76,976	—	77,089	—	—	35,142	—	35,142
Listed overseas.....	—	—	4,191	—	4,191	—	—	4,191	—	4,191
	113	—	81,167	—	81,280	—	—	39,333	—	39,333
As analysed by issuing entities:										
Central government and central banks .....	—	—	—	289,181	289,181	—	—	—	289,181	289,181
Public sector entities .....	—	—	—	67,547	67,547	—	—	—	67,547	67,547
Banks and other financial institutions.....	—	275,085	42,615	8,033,861	8,351,561	—	275,085	35,755	8,033,861	8,344,701
Corporate entities.....	113	405,482	119,439	1,337,096	1,862,130	—	405,482	84,465	1,337,096	1,827,043
Others .....	—	—	34,473	—	34,473	—	—	30,505	—	30,505
	113	680,567	196,527	9,727,685	10,604,892	—	680,567	150,725	9,727,685	10,558,977

## 20. ADVANCES AND OTHER ACCOUNTS

	THE GROUP		THE BANK	
	2009	2008	2009	2008
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Advances to customers				
Bills receivable.....	302,986	334,215	302,986	334,215
Trade bills .....	118,258	165,293	118,258	165,293
Other advances to customers.....	32,372,335	32,745,119	32,372,335	32,744,705
	32,793,579	33,244,627	32,793,579	33,244,213
Interest receivable.....	90,429	138,721	90,410	138,452
Impairment allowances				
- Individually assessed.....	(25,905)	(5,799)	(25,905)	(5,799)
- Collectively assessed.....	(108,096)	(108,988)	(108,096)	(108,984)
	32,750,007	33,268,561	32,749,988	33,267,882
Advances to banks and other financial institutions .....	114,683	116,412	114,683	116,412
	32,864,690	33,384,973	32,864,671	33,384,294
Other accounts .....	403,045	249,869	125,780	93,039
	<u>33,267,735</u>	<u>33,634,842</u>	<u>32,990,451</u>	<u>33,477,333</u>

Included in the “Advances to banks and other financial institutions” of the Group and the Bank is an amount of approximately HK\$114,683,000 (2008: HK\$116,412,000) placed as reserve funds with the financial institutions in the People’s Republic of China by the Shantou Branch of the Bank in compliance with the requirements of Regulations Governing Foreign Financial Institutions of the People’s Republic of China.

Impairment allowances on advances:

	THE GROUP			THE BANK		
	Individual assessment	Collective assessment	Total	Individual assessment	Collective assessment	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Balance at 1 January 2009 .....	5,799	108,988	114,787	5,799	108,984	114,783
Increase in impairment allowances..	116,880	—	116,880	116,880	—	116,880
Amounts reversed .....	(13,694)	(897)	(14,591)	(13,694)	(893)	(14,587)
Amounts written off.....	(91,538)	—	(91,538)	(91,538)	—	(91,538)
Recoveries of advances written off in previous years .....	12,134	—	12,134	12,134	—	12,134
Unwinding effect of discount rate...	(3,676)	—	(3,676)	(3,676)	—	(3,676)
Exchange difference.....	—	5	5	—	5	5
Balance at 31 December 2009 .....	<u>25,905</u>	<u>108,096</u>	<u>134,001</u>	<u>25,905</u>	<u>108,096</u>	<u>134,001</u>

	THE GROUP			THE BANK		
	Individual assessment	Collective assessment	Total	Individual assessment	Collective assessment	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Balance at 1 January 2008 .....	17,876	116,720	134,596	17,876	116,714	134,590
Increase in impairment allowances ..	144,819	—	144,819	144,819	—	144,819
Amounts reversed .....	(45,795)	(7,690)	(53,485)	(45,795)	(7,688)	(53,483)
Amounts written off .....	(141,853)	—	(141,853)	(141,853)	—	(141,853)
Recoveries of advances written off in previous years .....	35,167	—	35,167	35,167	—	35,167
Unwinding effect of discount rate ...	(4,415)	—	(4,415)	(4,415)	—	(4,415)
Exchange difference .....	—	(42)	(42)	—	(42)	(42)
Balance at 31 December 2008 .....	<u>5,799</u>	<u>108,988</u>	<u>114,787</u>	<u>5,799</u>	<u>108,984</u>	<u>114,783</u>

Details of the impaired loans are as follows:

	THE GROUP AND THE BANK	
	2009	2008
	HK\$'000	HK\$'000
Gross impaired loans .....	53,707	100,574
Less: Impairment allowances under individual assessment .....	(25,905)	(5,799)
Net impaired loans .....	<u>27,802</u>	<u>94,775</u>
Gross impaired loans as a percentage of gross advances to customers .....	<u>0.16%</u>	<u>0.30%</u>
Market value of collateral pledged .....	<u>103,950</u>	<u>470,173</u>

## 21. INVESTMENTS IN SUBSIDIARIES

(i)

	2009	2008
	HK\$'000	HK\$'000
Unlisted shares, at cost .....	<u>338,323</u>	<u>348,323</u>

Details of the principal subsidiaries as at 31 December 2009 are as follows:

Name of company	Place of incorporation / operation	Issued and fully paid ordinary share capital	Percentage of issued share capital held	Principal activities
Chong Hing (Nominees) Limited .....	Hong Kong	HK\$100,000	100%	Provision of nominee services
Chong Hing Finance Limited .....	Hong Kong	HK\$25,000,000	100%	Deposit-taking and lending
Chong Hing Information Technology Limited .....	Hong Kong	HK\$100,000	100%	Provision of electronic data processing services
Liu Chong Hing Banking Corporation, Cayman .....	Cayman Islands / Hong Kong	US\$10,000,000	100%	General merchant banking
Chong Hing Securities Limited .....	Hong Kong	HK\$10,000,000	100%	Stockbroking
Chong Hing Commodities and Futures Limited .....	Hong Kong	HK\$5,000,000	100%	Investment holding and commodities and futures broking
Gallbraith Limited .....	Hong Kong	HK\$16,550,000	100%	Property investment
Card Alliance Company Limited .....	Hong Kong	HK\$18,000,000	100%	Credit card management
Chong Hing Insurance Company Limited .....	Hong Kong	HK\$85,000,000	100%	Insurance underwriting

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

(ii) Amounts due from subsidiaries

	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Amounts due from subsidiaries .....	<u>4,985</u>	<u>3,711</u>

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

## 22. INTERESTS IN JOINTLY CONTROLLED ENTITIES

	<b>THE GROUP</b>		<b>THE BANK</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Unlisted shares, at cost .....	—	—	21,500	21,500
Share of increases in net assets, net of dividends received .....	<u>119,418</u>	<u>82,999</u>	<u>—</u>	<u>—</u>
	<u>119,418</u>	<u>82,999</u>	<u>21,500</u>	<u>21,500</u>

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

As at 31 December 2009, the Group had interests in the following jointly controlled entities:

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

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

	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Assets .....	741,582	624,244
Liabilities .....	(622,164)	(541,245)
Income .....	66,028	61,602
Expense .....	<u>(33,618)</u>	<u>(151,842)</u>

## 23. INVESTMENT PROPERTIES

All of the 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.

	THE GROUP		THE BANK	
	2009	2008	2009	2008
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 1 January .....	129,801	60,241	104,050	35,900
Addition .....	—	30,000	—	30,000
Net increase in fair value recognised in the income statement.....	5,148	39,560	4,110	38,150
Disposals .....	(32,000)	—	(32,000)	—
Exchange adjustments .....	250	—	—	—
At 31 December.....	<u>103,199</u>	<u>129,801</u>	<u>76,160</u>	<u>104,050</u>

Net gain on disposal of fair value adjustments on investment properties:

	THE GROUP	
	2009	2008
	<i>HK\$'000</i>	<i>HK\$'000</i>
Net gain on disposal of investment properties .....	26,000	—
Net gain on fair value adjustments on investment properties .....	<u>5,148</u>	<u>39,560</u>
	<u>31,148</u>	<u>39,560</u>

Investment properties owned by the Group and by the Bank were revalued at 31 December 2009 on an open market value basis by Vigers Hong Kong Limited, independent professionally qualified valuers. The fair value is mainly arrived at by reference to comparable market transactions for similar properties.

The investment properties are rented out under operating leases.

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

	THE GROUP		THE BANK	
	2009	2008	2009	2008
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Leasehold properties				
Held in Hong Kong on long-term lease (over 50 years unexpired) .....	1,060	32,550	1,060	32,550
Held in Hong Kong on medium-term lease (10 - 50 years unexpired) .....	75,100	71,500	75,100	71,500
Held outside Hong Kong on medium-term lease (10 - 50 years unexpired) .....	<u>27,039</u>	<u>25,751</u>	<u>—</u>	<u>—</u>
	<u>103,199</u>	<u>129,801</u>	<u>76,160</u>	<u>104,050</u>



## 24. PROPERTY AND EQUIPMENT

	THE GROUP			THE BANK		
	Buildings	Equipment	Total	Buildings	Equipment	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>COST</b>						
At 1 January 2009 .....	316,883	477,734	794,617	313,083	428,659	741,742
Additions .....	—	21,326	21,326	—	13,125	13,125
Disposals .....	(220)	(344)	(564)	(220)	(274)	(494)
Exchange adjustments .....	—	4	4	—	4	4
At 31 December 2009 .....	316,663	498,720	815,383	312,863	441,514	754,377
<b>ACCUMULATED DEPRECIATION</b>						
At 1 January 2009 .....	34,204	290,689	324,893	34,100	258,570	292,670
Provided for the year .....	6,624	40,589	47,213	6,528	35,025	41,553
Eliminated on disposals .....	(82)	(329)	(411)	(82)	(262)	(344)
At 31 December 2009 .....	40,746	330,949	371,695	40,546	293,333	333,879
<b>CARRYING AMOUNTS</b>						
At 31 December 2009 .....	275,917	167,771	443,688	272,317	148,181	420,498
At 1 January 2009 .....	282,679	187,045	469,724	278,983	170,089	449,072

	THE GROUP			THE BANK		
	Buildings	Equipment	Total	Buildings	Equipment	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>COST</b>						
At 1 January 2008 .....	308,345	425,175	733,520	304,545	378,551	683,096
Additions .....	8,538	59,129	67,667	8,538	54,649	63,187
Disposals .....	—	(6,567)	(6,567)	—	(4,538)	(4,538)
Exchange adjustments .....	—	(3)	(3)	—	(3)	(3)
At 31 December 2008 .....	316,883	477,734	794,617	313,083	428,659	741,742
<b>ACCUMULATED DEPRECIATION</b>						
At 1 January 2008 .....	27,641	259,006	286,647	27,634	229,863	257,497
Provided for the year .....	6,563	37,362	43,925	6,466	32,366	38,832
Eliminated on disposals .....	—	(5,676)	(5,676)	—	(3,656)	(3,656)
Exchange adjustments .....	—	(3)	(3)	—	(3)	(3)
At 31 December 2008 .....	34,204	290,689	324,893	34,100	258,570	292,670
<b>CARRYING AMOUNTS</b>						
At 31 December 2008 .....	282,679	187,045	469,724	278,983	170,089	449,072
At 1 January 2008 .....	280,704	166,169	446,873	276,911	148,688	425,599

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

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

The carrying amount of buildings shown above comprise:

	THE GROUP		THE BANK	
	2009	2008	2009	2008
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Leasehold properties				
Held in Hong Kong on long-term lease (over 50 years unexpired) .....	207,380	211,918	207,380	211,918
Held in Hong Kong on medium-term lease (10-50 years unexpired) .....	61,556	63,498	57,956	59,802
Held outside Hong Kong on medium-term lease (10-50 years unexpired) .....	6,981	7,263	6,981	7,263
	<u>275,917</u>	<u>282,679</u>	<u>272,317</u>	<u>278,983</u>

## 25. PREPAID LEASE PAYMENTS FOR LAND

The Group's prepaid lease payments comprise:

	THE GROUP		THE BANK	
	2009	2008	2009	2008
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
COST				
In Hong Kong held on:				
Leases of over 50 years .....	124,800	125,212	648,869	649,908
Leases of between 10 to 50 years .....	193,145	198,932	182,630	188,136
Outside Hong Kong held on:				
Leases of between 10 to 50 years .....	3,588	3,983	3,588	3,983
	<u>321,533</u>	<u>328,127</u>	<u>835,087</u>	<u>842,027</u>
Net book value at 1 January .....	328,127	334,231	842,027	848,465
Disposals .....	(519)	—	(519)	—
Release of prepaid operating lease payments .....	(6,075)	(6,104)	(6,421)	(6,438)
Net book value at 31 December .....	<u>321,533</u>	<u>328,127</u>	<u>835,087</u>	<u>842,027</u>
Analysed as:				
Current portion .....	6,075	6,104	6,421	6,438
Non-current portion .....	315,458	322,023	828,666	835,589
Total .....	<u>321,533</u>	<u>328,127</u>	<u>835,087</u>	<u>842,027</u>

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

## 26. DEPOSITS FROM CUSTOMERS

	THE GROUP		THE BANK	
	2009	2008	2009	2008
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Demand deposits and current accounts .....	4,790,745	3,004,761	4,790,745	3,004,761
Savings deposits .....	19,644,533	13,835,350	19,644,533	13,835,350
Time, call and notice deposits .....	36,353,137	42,561,549	36,350,247	42,558,316
	<u>60,788,415</u>	<u>59,401,660</u>	<u>60,785,525</u>	<u>59,398,427</u>

Included in the balances is an aggregate amount of approximately HK\$59,749,000 (2008: HK\$147,110,000) representing deposits of companies and their subsidiaries having significant influence on the Group.

## 27. LOAN CAPITAL

	<b>THE GROUP AND THE BANK</b>	
	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
US\$125 million callable floating rate subordinated notes due 2016 .....	<u>967,199</u>	<u>965,454</u>

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

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

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

## 28. SHARE CAPITAL

	<b>2009 &amp; 2008</b>
	<i>HK\$'000</i>
Authorised:	
600,000,000 shares of HK\$0.50 each .....	<u>300,000</u>
Issued and fully paid:	
435,000,000 shares of HK\$0.50 each .....	<u>217,500</u>

## 29. RESERVES

	<b>Share premium</b>	<b>Investment revaluation reserve</b>	<b>General reserve</b>	<b>Translation reserve</b>	<b>Regulatory reserve</b>	<b>Retained profits</b>	<b>Total</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
<b>THE BANK</b>							
At 1 January 2009 .....	1,542,817	(3,199)	1,378,500	8,060	307,000	2,440,689	5,673,867
Profit for the year .....	—	—	—	—	—	119,647	119,647
Other comprehensive income for the year .....	—	27,812	—	223	—	—	28,035
Total comprehensive income for the year .....	—	27,812	—	223	—	119,647	147,682
Interim dividend paid .....	—	—	—	—	—	(34,800)	(34,800)
Final dividend paid .....	—	—	—	—	—	(21,750)	(21,750)
Earmark of retained profits as regulatory reserve .....	—	—	—	—	(20,000)	20,000	—
At 31 December 2009 .....	<u>1,542,817</u>	<u>24,613</u>	<u>1,378,500</u>	<u>8,283</u>	<u>287,000</u>	<u>2,523,786</u>	<u>5,764,999</u>
At 1 January 2008 .....	1,542,817	50,512	1,378,500	335	356,000	2,557,334	5,885,498
Profit for the year .....	—	—	—	—	—	91,005	91,005
Other comprehensive income (expense) for the year .....	—	(53,711)	—	7,725	—	—	(45,986)
Total comprehensive income (expense) for the year .....	—	(53,711)	—	7,725	—	91,005	45,019
Interim dividend paid .....	—	—	—	—	—	(65,250)	(65,250)
Final dividend paid .....	—	—	—	—	—	(191,400)	(191,400)
Earmark of retained profits as regulatory reserve .....	—	—	—	—	(49,000)	49,000	—
At 31 December 2008 .....	<u>1,542,817</u>	<u>(3,199)</u>	<u>1,378,500</u>	<u>8,060</u>	<u>307,000</u>	<u>2,440,689</u>	<u>5,673,867</u>

The Bank's reserves available for distribution to shareholders as at 31 December 2009 comprised retained profits of HK\$2,523,786,000 (2008: HK\$2,440,689,000) and general reserve of HK\$1,378,500,000 (2008: HK\$1,378,500,000).

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

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

### 30. DEFERRED TAXATION

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

	Accelerated tax depreciation	Collectively assessed impairment allowance	Investment properties	Revaluation of available- for-sale securities	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>THE GROUP</b>					
At 1 January 2009 .....	15,645	(18,428)	12,557	(3,491)	6,283
Charge to consolidated income statement for the year ( <i>Note 14</i> ) .....	(112)	(1,217)	(3,638)	—	(4,967)
Credit to other comprehensive income for the year .....	—	—	—	10,456	10,456
At 31 December 2009 .....	<u>15,533</u>	<u>(19,645)</u>	<u>8,919</u>	<u>6,965</u>	<u>11,772</u>
At 1 January 2008 .....	12,282	(19,726)	6,149	16,569	15,274
Charge to consolidated income statement for the year ( <i>Note 14</i> ) .....	3,363	1,298	6,408	—	11,069
Credit to other comprehensive income for the year .....	—	—	—	(20,060)	(20,060)
At 31 December 2008 .....	<u>15,645</u>	<u>(18,428)</u>	<u>12,557</u>	<u>(3,491)</u>	<u>6,283</u>
<b>THE BANK</b>					
At 1 January 2009 .....	12,794	(18,427)	10,243	(866)	3,744
Charge to income statement for the year .....	(601)	(1,218)	(3,117)	—	(4,936)
Credit to other comprehensive income for the year .....	—	—	—	4,961	4,961
At 31 December 2009 .....	<u>12,193</u>	<u>(19,645)</u>	<u>7,126</u>	<u>4,095</u>	<u>3,769</u>
At 1 January 2008 .....	9,283	(19,725)	4,188	4,177	(2,077)
Charge to income statement for the year .....	3,511	1,298	6,055	—	10,864
Credit to other comprehensive income for the year .....	—	—	—	(5,043)	(5,043)
At 31 December 2008 .....	<u>12,794</u>	<u>(18,427)</u>	<u>10,243</u>	<u>(866)</u>	<u>3,744</u>

### 31. SHARE OPTION SCHEME

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

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

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

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

### 32. LOANS TO OFFICERS

The aggregate relevant loans to officers, included in "advances to customers" in Note 20, and disclosure pursuant to Section 161B of the Companies Ordinance are as follows:

	<b>THE GROUP AND THE BANK</b>	
	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Aggregate balance of all relevant loans outstanding at the reporting date.....	<u>54,004</u>	<u>91,177</u>
Maximum aggregate balance of relevant loans during the year.....	<u>124,770</u>	<u>114,996</u>

The loans have no fixed repayment terms and the applicable interest rate ranges from 0% to prime rate plus 10%. Included in the loans to officers are loans of HK\$53,138,000 (2008: HK\$90,053,000) with collateral.

### 33. IMPAIRMENT LOSS ON GOODWILL

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

For the year ended 31 December 2009, management has reviewed goodwill for impairment. The review comprised a comparison of the carrying amount and value in use of an acquired subsidiary (the smallest cash-generating unit) to which the goodwill has been allocated. The acquired subsidiary is involved in insurance business.

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

Value in use is derived at by discounting the expected future cash flows at 12% discount rate. Management's financial model assumes a flat growth in underwriting profit. A goodwill impairment loss of HK\$10,000,000 (2008: HK\$20,000,000), representing the excess of the carrying amount above the value in use, has been recognised for the year ended 31 December 2009.

### 34. CONTINGENT LIABILITIES AND COMMITMENTS

	THE GROUP		THE BANK	
	2009	2008	2009	2008
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Contingent liabilities and commitments				
- contractual amounts				
Direct credit substitutes .....	790,690	647,442	790,690	647,442
Trade-related contingencies .....	283,739	366,620	283,739	366,620
Forward asset purchases .....	3,234	13,548	3,234	13,548
Other commitments:				
- Which are unconditionally cancellable without prior notice ...	4,969,184	4,703,352	4,969,184	4,703,352
- With an original maturity of one year and under .....	7,717,628	8,105,056	7,717,628	8,105,056
- With an original maturity of over one year .....	1,821,771	1,721,251	1,821,771	1,721,251
Lease commitments .....	72,846	73,506	67,706	70,398
	<u>15,659,092</u>	<u>15,630,775</u>	<u>15,653,952</u>	<u>15,627,667</u>

Most of contingent liabilities and commitments are denominated in Hong Kong dollars.

At the end of the reporting period, the Group had commitments for future minimum lease payments under these non-cancellable operating leases which fall due as follows:

	THE GROUP		THE BANK	
	2009	2008	2009	2008
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Within one year .....	30,034	28,532	27,832	26,941
In the second to fifth years inclusive .....	42,480	36,874	39,542	35,413
Over five years .....	332	1,043	332	1,043
	<u>72,846</u>	<u>66,449</u>	<u>67,706</u>	<u>63,397</u>

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

Capital commitments outstanding at the end of the reporting period are as follows:

	THE GROUP AND THE BANK	
	2009	2008
	HK\$'000	HK\$'000
Capital expenditure contracted for but not provided in the consolidated financial statements in respect of property and equipment .....	<u>3,234</u>	<u>13,548</u>

The credit risk weighted amount of contingent liabilities and commitments is HK\$2,906,189,000 (2008: HK\$2,990,733,000).

At the end of the reporting period, the Group and the Bank as lessor had contracted with tenants for the following future minimum lease payments:

	<b>THE GROUP AND THE BANK</b>	
	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Within one year .....	3,890	1,148
In the second to fifth years inclusive .....	4,135	38
	<u>8,025</u>	<u>1,186</u>

### 35. RETIREMENT BENEFITS SCHEME

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

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

The most recent actuarial valuation of the ORSO (Defined benefit) Scheme was carried out as at 31 December 2008 by the qualified actuaries of Watson Wyatt Hong Kong Limited. The accrued liabilities and future costs were measured using the Projected Unit Credit method.

At the date of the latest formal independent actuarial valuation made on 31 December 2008, the net retirement asset of the ORSO (Defined benefit) Scheme was HK\$52,000.

Net benefit cost:

	<b>2008</b>
	<i>HK\$'000</i>
Current service cost.....	(94)
Interest cost on benefit obligation .....	(838)
Expected return on plan assets .....	2,292
Actuarial loss recognised in the year.....	<u>(23,222)</u>
Net benefit cost.....	<u>(21,862)</u>

The amount included in the consolidated statement of financial position arising from Group’s defined benefit retirement benefit plan is as follows:

	<b>2008</b>
	<i>HK\$'000</i>
Present value of defined benefit obligation.....	(25,450)
Fair value of plan assets.....	<u>25,502</u>
Retirement benefit asset .....	<u>52</u>

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

	<b>2008</b>
	<i>HK\$'000</i>
Opening defined benefit obligation .....	25,121
Interest cost .....	94
Current service cost.....	838
Actuarial gains on obligations .....	(2,456)
Benefits forfeited .....	1,853
Closing defined benefit obligation .....	<u>25,450</u>

Changes in fair value of plan assets are as follows:

	<b>2008</b>
	<i>HK\$'000</i>
Opening fair value of plan assets .....	47,035
Expected return .....	2,292
Actuarial losses on plan assets .....	(21,369)
Benefits paid .....	(2,456)
Closing fair value of plan assets.....	<u>25,502</u>

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

	<b>2008</b>
	<i>%</i>
Cash.....	47
Equities.....	53

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

The actual return on plan assets for 2008 was HK\$19,077,000.

The amounts of assets of the Scheme invested in the Bank's own deposit account as at 31 December 2008 were:

	<b>2008</b>
	<i>HK\$'000</i>
Deposits with the Bank .....	11,756

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

	<b>2008</b>
	<i>%</i>
Discount rate.....	2.8
Expected rate of return on plan assets .....	5.0
Expected rate of salary increase .....	3.0



### 36. RELATED PARTY TRANSACTIONS

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

	Interest, commission and rental income		Interest and rental expenses	
	2009	2008	2009	2008
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Investing enterprises having significant influence on the Bank and its subsidiaries .....	7,733	7,030	23,271	26,567
Jointly controlled entities.....	12,154	18,788	2,725	6,624
Directors and their associates.....	11,926	24,046	6,040	14,202

The above transactions were carried out at market rates.

At the end of reporting period, the Group and the Bank had the following material outstanding balances with related parties:

	Amounts due from related parties		Amounts due to related parties	
	2009	2008	2009	2008
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Investing enterprises having significant influence on the Bank and its subsidiaries .....	—	—	59,749	147,110
Jointly controlled entities.....	53,790	59,743	96,034	148,992
Directors and their associates.....	1,434,806	1,695,469	530,733	621,189

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

Amounts due from related parties are included in advances and other accounts on statement of financial position.

Amounts due to related parties are included in deposit from customers on statement of financial position.

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

	Interest, commission and rental income		Interest and rental expenses		Computer service expense		Dividend income	
	2009	2008	2009	2008	2009	2008	2009	2008
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Subsidiaries .....	6,856	7,802	11,287	18,222	24,105	26,676	60,000	48,000

The above transactions were carried out at market rates.

At the end of reporting period, the Bank had the following material outstanding balances with subsidiaries:

	Amounts due from		Amounts due to	
	2009	2008	2009	2008
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Subsidiaries .....	4,985	3,711	763,072	704,828

The above outstanding balances are unsecured, bear interest at market rates and are repayable within one year.

## Compensation of key management personnel

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

	<b>THE GROUP AND THE BANK</b>	
	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Short-term benefits .....	52,749	54,769
Post employment benefits .....	2,460	3,996
	<u>55,209</u>	<u>58,765</u>

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

## 37. CAPITAL MANAGEMENT

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

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

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

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

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

### Capital Adequacy Ratio

	<b>2009</b>	<b>2008</b>
	<i>%</i>	<i>%</i>
Capital adequacy ratio .....	15.95	15.64
Core capital ratio .....	12.72	12.55

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

## Capital base

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

	<b>2009</b>	<b>2008</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Core capital		
Paid-up ordinary share capital.....	217,500	217,500
Share premium.....	1,542,817	1,542,817
Published reserves .....	3,491,579	3,346,050
Profit and loss account .....	(87,537)	78,501
Less: Net deferred tax assets .....	—	(1)
Total core capital.....	5,164,359	5,184,867
Other deductions from core capital .....	(122,809)	(143,357)
Core capital after deductions.....	<u>5,041,550</u>	<u>5,041,510</u>
Supplementary capital		
Reserves attributable to fair value gains on revaluation of holdings of land and buildings ....	5,502	5,755
Collective impairment allowances .....	108,096	108,988
Regulatory reserve for general banking risks .....	287,000	307,000
Reserves attributable to fair value gains on revaluation of holdings of available-for-sale equities and debt securities.....	13,611	—
Unrealised fair value gains arising from holdings of equities and debt securities designated at fair value through profit or loss.....	24,206	—
Term subordinated debt.....	<u>967,199</u>	<u>965,454</u>
Total supplementary capital.....	1,405,614	1,387,197
Other deductions from supplementary capital .....	(122,809)	(143,357)
Supplementary capital after deductions .....	<u>1,282,805</u>	<u>1,243,840</u>
Total capital base after deductions .....	<u><u>6,324,355</u></u>	<u><u>6,285,350</u></u>

Deductions from total capital base mainly include investments in subsidiaries of which their risk-weighted assets have not been consolidated into the total risk-weighted assets of the Group, which mainly conduct non-banking related business. Those subsidiaries are Chong Hing Commodities and Futures Limited, Chong Hing Insurance Company Limited, Chong Hing (Management) Limited, Chong Hing (Nominees) Limited and Chong Hing Securities Limited.

## INDEPENDENT AUDITOR'S REPORT

**Deloitte.**

**德勤**

### **TO THE MEMBERS OF CHONG HING BANK LIMITED**

*(incorporated in Hong Kong with limited liability)*

We have audited the consolidated financial statements of Chong Hing Bank Limited (the “Bank”) and its subsidiaries (collectively referred to as the “Group”) set out on pages F-103 to F-178, which comprise the consolidated and the Bank balance sheets as at 31 December 2008, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

### **Directors’ responsibility for the consolidated financial statements**

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

### **Auditor’s responsibility**

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

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

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

### **Opinion**

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Bank and of the Group as at 31 December 2008 and of the Group’s profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

**Deloitte Touche Tohmatsu**  
*Certified Public Accountants*  
Hong Kong

4 March 2009

**CONSOLIDATED INCOME STATEMENT**  
**FOR THE YEAR ENDED 31 DECEMBER 2008**

	<b>NOTES</b>	<b>2008</b>	<b>2007</b>
		<i>HK\$'000</i>	<i>HK\$'000</i>
Interest income .....		2,171,336	3,310,484
Interest expense .....		(1,307,010)	(2,339,871)
Net interest income .....	8	864,326	970,613
Fee and commission income .....		265,220	326,641
Fee and commission expense .....		(48,419)	(43,229)
Net fee and commission income .....	9	216,801	283,412
Net (losses) gains on financial assets designated at fair value through profit or loss .....	10	(48,299)	10,372
Other operating income .....	11	146,566	156,297
Operating expenses .....	12	(772,431)	(642,894)
		406,963	777,800
Impairment allowances on loans and advances .....	20	(91,334)	(82,922)
Net gain (loss) on disposal of property and equipment .....		294	(64)
Net gain on disposal of land .....		—	2,591
Net gain on disposal of investment properties .....		—	14,420
Net gain on disposal of available-for-sale securities .....		108,706	177,351
Fair value adjustment on investment properties .....	23	39,560	14,391
Impairment loss on available-for-sale securities .....		(264,654)	(369,627)
Impairment loss on goodwill .....	33	(20,000)	(30,000)
Profit from operations .....		179,535	503,940
Share of (loss) profit of jointly controlled entities .....		(90,240)	66,074
Profit before taxation .....		89,295	570,014
Taxation .....	14	(28,675)	(64,982)
Profit for the year .....		60,620	505,032
Dividends .....	15	256,650	282,750
Earnings per share, basic and diluted .....	16	HK\$0.14	HK\$1.16

**CONSOLIDATED BALANCE SHEET**  
**AS AT 31 DECEMBER 2008**

	NOTES	2008 HK\$'000	2007 HK\$'000
<b>Assets</b>			
Cash and short-term funds .....	17	17,659,927	14,763,977
Placements with banks and other financial institutions maturing between one to twelve months .....		5,367,858	3,084,147
Derivative financial instruments .....	18	429	60
Financial assets at fair value through profit or loss .....	19	680,680	1,134,422
Available-for-sale securities .....	19	196,527	876,661
Held-to-maturity securities .....	19	9,727,685	15,607,980
Advances and other accounts .....	20	33,634,842	32,495,890
Tax recoverable .....		38,113	19,816
Interests in jointly controlled entities .....	22(i)	82,999	142,230
Loan to a jointly controlled entity .....	22(ii)	—	5,267
Investment properties .....	23	129,801	60,241
Property and equipment .....	24	469,724	446,873
Prepaid lease payments for land .....	25	328,127	334,231
Goodwill .....	33	60,606	80,606
<b>Total assets</b> .....		<u>68,377,318</u>	<u>69,052,401</u>
<b>Liabilities</b>			
Deposits and balances of banks and other financial institutions .....		1,525,509	456,858
Deposits from customers .....	26	59,401,660	60,327,437
Derivative financial instruments .....	18	39,303	114,546
Other accounts and accruals .....		477,381	861,619
Current tax liabilities .....		5,104	35,008
Loan capital .....	27	965,454	970,871
Deferred tax liabilities .....	30	6,283	15,274
<b>Total liabilities</b> .....		<u>62,420,694</u>	<u>62,781,613</u>
<b>Shareholders' equity</b>			
Share capital .....	28	217,500	217,500
Reserves .....		5,739,124	6,053,288
<b>Shareholders' funds</b> .....		<u>5,956,624</u>	<u>6,270,788</u>
<b>Total liabilities and shareholders' equity</b> .....		<u>68,377,318</u>	<u>69,052,401</u>

The consolidated financial statements on pages F-103 to F-178 were approved and authorised for issue by the Board of Directors on 4 March 2009 and signed on its behalf by:

**Liu Lit Man**, *Executive Chairman*

**Liu Lit Mo**, *Vice Chairman-Executive Director*

**Lau Wai Man**, *Executive Director and Deputy Chief Executive Officer*

**Michael K W Yeung**, *Company Secretary*

**BALANCE SHEET**  
AS AT 31 DECEMBER 2008

	NOTES	2008 HK\$'000	2007 HK\$'000
<b>Assets</b>			
Cash and short-term funds .....	17	17,617,546	14,713,472
Placements with banks and other financial institutions maturing between one to twelve months .....		5,367,858	3,084,147
Derivative financial instruments .....	18	429	60
Financial assets at fair value through profit or loss .....	19	680,567	1,134,158
Available-for-sale securities .....	19	150,725	724,187
Held-to-maturity securities .....	19	9,727,685	15,607,980
Advances and other accounts .....	20	33,477,333	32,093,440
Tax recoverable .....		37,976	19,816
Investments in subsidiaries .....	21(i)	348,323	333,323
Amounts due from subsidiaries .....	21(ii)	3,711	3,407
Interests in jointly controlled entities .....	22(i)	21,500	56,500
Loan to a jointly controlled entity .....	22(ii)	—	5,267
Investment properties .....	23	104,050	35,900
Property and equipment .....	24	449,072	425,599
Prepaid lease payments for land .....	25	842,027	848,465
Deferred tax assets .....	30	—	2,077
<b>Total assets</b> .....		<u>68,828,802</u>	<u>69,087,798</u>
<b>Liabilities</b>			
Deposits and balances of banks and other financial institutions .....		1,525,509	456,858
Deposits from customers .....	26	59,398,427	60,323,598
Amounts due to subsidiaries .....	36	704,828	658,146
Derivative financial instruments .....	18	39,303	114,546
Other accounts and accruals .....		297,748	457,448
Current tax liabilities .....		2,422	3,333
Loan capital .....	27	965,454	970,871
Deferred tax liabilities .....	30	3,744	—
<b>Total liabilities</b> .....		<u>62,937,435</u>	<u>62,984,800</u>
<b>Shareholders' equity</b>			
Share capital .....	28	217,500	217,500
Reserves .....	29	5,673,867	5,885,498
<b>Shareholders' funds</b> .....		<u>5,891,367</u>	<u>6,102,998</u>
<b>Total liabilities and shareholders' equity</b> .....		<u>68,828,802</u>	<u>69,087,798</u>

Approved and authorised for issue by the Board of Directors on 4 March 2009 and signed on its behalf by:

**Liu Lit Man**, *Executive Chairman*

**Liu Lit Mo**, *Vice Chairman-Executive Director*

**Lau Wai Man**, *Executive Director and Deputy Chief Executive Officer*

**Michael K W Yeung**, *Company Secretary*

**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**  
**FOR THE YEAR ENDED 31 DECEMBER 2008**

	Notes	Share capital	Share premium	Goodwill	Investment revaluation reserve	General reserve	Translation reserve	Regulatory reserve	Retained profits	Total
		HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 1 January 2008 .....		217,500	1,542,817	(182)	138,680	1,388,500	330	356,000	2,627,143	6,270,788
Revaluation losses, net .....		—	—	—	(300,495)	—	—	—	—	(300,495)
Exchange differences arising from translation of foreign operations ..		—	—	—	—	—	7,194	—	—	7,194
Deferred taxation arising from revaluation movement .....	30	—	—	—	20,060	—	—	—	—	20,060
Share of reserves of a jointly-controlled entity .....		—	—	—	(841)	—	—	—	—	(841)
Net income (expense) recognised directly in equity .....		—	—	—	(281,276)	—	7,194	—	—	(274,082)
Profit for the year .....		—	—	—	—	—	—	—	60,620	60,620
Reversal of reserve upon impairment .....		—	—	—	264,654	—	—	—	—	264,654
Reversal of reserve upon disposal .....		—	—	—	(108,706)	—	—	—	—	(108,706)
Total recognised income (expense) for the year .....		—	—	—	(125,328)	—	7,194	—	60,620	(57,514)
Interim dividend paid for financial year 2008 .....	15	—	—	—	—	—	—	—	(65,250)	(65,250)
Final dividend paid for financial year 2007 .....	15	—	—	—	—	—	—	—	(191,400)	(191,400)
Earmark of retained profits as regulatory reserve .....		—	—	—	—	—	—	(49,000)	49,000	—
At 31 December 2008 ..		<u>217,500</u>	<u>1,542,817</u>	<u>(182)</u>	<u>13,352</u>	<u>1,388,500</u>	<u>7,524</u>	<u>307,000</u>	<u>2,480,113</u>	<u>5,956,624</u>



**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**  
**FOR THE YEAR ENDED 31 DECEMBER 2008**

	Notes	Share capital	Share premium	Goodwill	Investment revaluation reserve	General reserve	Translation reserve	Regulatory reserve	Retained profits	Total
		HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 1 January 2007 .....		217,500	1,542,817	(182)	142,386	1,388,500	(152)	165,000	2,595,861	6,051,730
Revaluation losses, net .....		—	—	—	(206,538)	—	—	—	—	(206,538)
Exchange differences arising from translation of foreign operations ..		—	—	—	—	—	482	—	—	482
Deferred taxation arising from revaluation movement .....	30	—	—	—	10,556	—	—	—	—	10,556
Net income (expense) recognised directly in equity .....		—	—	—	(195,982)	—	482	—	—	(195,500)
Profit for the year.....		—	—	—	—	—	—	—	505,032	505,032
Reversal of reserve upon impairment.....		—	—	—	369,627	—	—	—	—	369,627
Reversal of reserve upon disposal.....		—	—	—	(177,351)	—	—	—	—	(177,351)
Total recognised income (expense) for the year .....		—	—	—	(3,706)	—	482	—	505,032	501,808
Interim dividend paid for financial year 2007 .....	15	—	—	—	—	—	—	—	(91,350)	(91,350)
Final dividend paid for financial year 2006 .....	15	—	—	—	—	—	—	—	(191,400)	(191,400)
Earmark of retained profits as regulatory reserve .....		—	—	—	—	—	—	191,000	(191,000)	—
At 31 December 2007..		<u>217,500</u>	<u>1,542,817</u>	<u>(182)</u>	<u>138,680</u>	<u>1,388,500</u>	<u>330</u>	<u>356,000</u>	<u>2,627,143</u>	<u>6,270,788</u>

The retained profits of the Group included accumulated loss of HK\$28,876,000 (2007: accumulated profits of HK\$64,514,000) retained by the jointly controlled entities of the Group.

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

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

**CONSOLIDATED CASH FLOW STATEMENT**  
**FOR THE YEAR ENDED 31 DECEMBER 2008**

	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
<b>OPERATING ACTIVITIES</b>		
Profit before taxation .....	89,295	570,014
Adjustments for:		
Net (gain) loss on disposal of property and equipment .....	(294)	64
Net gain on disposal of investment properties .....	—	(14,420)
Net gain on disposal of land .....	—	(2,591)
Net gain on disposal of available-for-sale securities .....	(108,706)	(177,351)
Impairment allowances on loans and advances .....	91,334	82,922
Impairment loss on goodwill .....	20,000	30,000
Impairment loss on available-for-sale securities .....	264,654	369,627
Dividend income from equity securities .....	(12,853)	(11,859)
Share of loss (profit) of jointly controlled entities .....	90,240	(66,074)
Fair value adjustment on investment properties .....	(39,560)	(14,391)
Depreciation .....	43,925	36,846
Amortisation of prepaid lease payments for land .....	6,104	5,710
Interest income from held-to-maturity securities and available-for-sale securities .....	(462,018)	(702,669)
Interest expense on loan capital .....	42,122	63,971
Exchange adjustments .....	615	2,871
Operating cash flows before movements in operating assets and liabilities .....	24,858	172,670
Decrease (increase) in interest receivable and other accounts .....	381,973	(153,985)
(Decrease) increase in other accounts and accruals .....	(383,060)	107,551
Increase in placements with banks and other financial institutions with original maturity over three months .....	(303,466)	(850,625)
Decrease in exchange fund bills with original maturity over three months .....	47,155	155,580
Decrease in money at call and short notice with original maturity over three months .....	690,017	624,478
Decrease (increase) in bills receivable .....	175,514	(25,354)
Increase in trade bills .....	(736)	(26,220)
Increase in other advances to customers .....	(1,808,623)	(4,880,739)
(Increase) decrease in advances to banks and other financial institutions .....	(59,328)	341
Decrease in deposits and balances of banks and other financial institutions with original maturity over three months .....	(1,841)	(79,162)
Decrease (increase) in financial assets at fair value through profit or loss .....	453,742	(523,611)
(Increase) decrease in derivative assets .....	(369)	117,732
Decrease in derivative liabilities .....	(75,243)	—
(Decrease) increase in deposits from customers .....	(925,777)	5,652,205
Cash (generated from) used in operations .....	(1,785,184)	290,861
Hong Kong Profits Tax paid .....	(58,868)	(71,290)
Overseas tax paid .....	(6,939)	(2,972)
<b>NET CASH (USED IN) GENERATED FROM OPERATING ACTIVITIES .....</b>	<b>(1,850,991)</b>	<b>216,599</b>

	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
<b>INVESTING ACTIVITIES</b>		
Interest received on held-to-maturity securities and available-for-sale securities .....	542,974	706,817
Dividends received on investments .....	12,853	11,859
Dividend income from jointly controlled entities .....	3,150	23,100
Capital investment in jointly controlled entities .....	(35,000)	—
Purchase of held-to-maturity securities .....	(24,380,625)	(26,184,962)
Purchase of available-for-sale securities .....	(42,160)	(364,551)
Purchase of property and equipment .....	(67,667)	(103,050)
Purchase of prepaid lease payments for land .....	—	(28,171)
Proceeds from redemption of held-to-maturity securities .....	30,260,920	24,480,155
Proceeds from sale and redemption of available-for-sale securities ...	421,799	379,493
Proceeds from disposal of property and equipment .....	1,185	95
Proceeds from disposal of land .....	—	7,356
Purchases of investment properties .....	(30,000)	—
Proceeds from disposal of investment properties .....	—	50,820
Repayment of loan from a jointly controlled entity .....	5,267	25,733
<b>NET CASH FROM (USED IN) INVESTING ACTIVITIES .....</b>	<u>6,692,696</u>	<u>(995,306)</u>
<b>CASH USED IN FINANCING ACTIVITIES</b>		
Interest paid on loan capital .....	(42,180)	(63,333)
Dividends paid .....	(256,650)	(282,750)
<b>NET CASH USED IN FINANCING ACTIVITIES .....</b>	<u>(298,830)</u>	<u>(346,083)</u>
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS .....</b>	4,542,875	(1,124,790)
<b>CASH AND CASH EQUIVALENTS AT 1 JANUARY .....</b>	<u>12,990,424</u>	<u>14,115,214</u>
<b>CASH AND CASH EQUIVALENTS AT 31 DECEMBER,</b> represented by		
Cash and balances with banks and other financial institutions .....	4,087,415	1,833,309
Money at call and short notice .....	13,180,425	9,776,851
Exchange fund bills .....	392,087	3,153,817
Placements with banks and other financial institutions maturing between one to twelve months .....	5,367,858	3,084,147
Deposits and balances of banks and other financial institutions .....	(1,525,509)	(456,858)
Less: Amounts with original maturity over three months .....	(3,968,977)	(4,400,842)
	<u><u>17,533,299</u></u>	<u><u>12,990,424</u></u>

# NOTES TO THE FINANCIAL STATEMENTS

## FOR THE YEAR ENDED 31 DECEMBER 2008

### 1. GENERAL

The Bank is a public limited company incorporated in Hong Kong and its shares are listed on the Stock Exchange of Hong Kong Limited. The Bank is engaged in the provision of banking and related financial services. The address of the registered office and principal place of business of the Bank is disclosed in the Annual Report.

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

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

In the current year, the Group and the Bank have applied the following amendments and interpretations (“new HKFRSs”) issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”) which are or have become effective.

HKAS 39 & HKFRS 7 (Amendments)	Reclassification of financial assets
HK(IFRIC) - INT 11	HKFRS 2: Group and treasury share transactions
HK(IFRIC) - INT 12	Service concession arrangements
HK(IFRIC) - INT 14	HKAS 19 - The limit on a defined benefit asset, minimum funding requirements and their interaction

The adoption of the new HKFRSs had no material effect on how the results and financial position for the current or prior accounting periods have been prepared and presented. Accordingly, no prior period adjustment has been required.

### 3. NEW AND REVISED HKFRSS ISSUED BUT NOT YET EFFECTIVE

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

HKFRSs (Amendments)	Improvements to HKFRSs <sup>1</sup>
HKAS 1 (Revised)	Presentation of financial statements <sup>2</sup>
HKAS 23 (Revised)	Borrowing costs <sup>2</sup>
HKAS 27 (Revised)	Consolidated and separate financial statements <sup>3</sup>
HKAS 32 & 1 (Amendments)	Puttable financial instruments and obligations arising on liquidation <sup>2</sup>
HKAS 39 (Amendment)	Eligible hedged items <sup>3</sup>
HKFRS 1 & HKAS 27 (Amendments)	Cost of an investment in a subsidiary, jointly controlled entity or associate <sup>2</sup>
HKFRS 2 (Amendment)	Vesting conditions and cancellations <sup>2</sup>
HKFRS 3 (Revised)	Business combinations <sup>3</sup>
HKFRS 8	Operating segments <sup>2</sup>
HK(IFRIC) - INT 13	Customer loyalty programmes <sup>4</sup>
HK(IFRIC) - INT 15	Agreements for the construction of real estate <sup>2</sup>
HK(IFRIC) - INT 16	Hedges of a net investment in a foreign operation <sup>5</sup>
HK(IFRIC) - INT 17	Distribution of non-cash assets to owners <sup>3</sup>
HK(IFRIC) - INT 18	Transfer of assets from customers <sup>6</sup>

<sup>1</sup> Effective for annual periods beginning on or after 1 January 2009 except the amendments to HKFRS 5, effective for annual periods beginning on or after 1 July 2009.

<sup>2</sup> Effective for annual periods beginning on or after 1 January 2009.

<sup>3</sup> Effective for annual periods beginning on or after 1 July 2009.

<sup>4</sup> Effective for annual periods beginning on or after 1 July 2008.

<sup>5</sup> Effective for annual periods beginning on or after 1 October 2008.

<sup>6</sup> Effective for transfers on or after 1 July 2009.

#### 4. SIGNIFICANT ACCOUNTING POLICIES

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

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

##### **Basis of consolidation**

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

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

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

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

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

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

##### **Goodwill**

###### ***Goodwill arising on acquisitions prior to 1 January 2005***

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

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

###### ***Goodwill arising on acquisitions on or after 1 January 2005***

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

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

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

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

### **Interests in jointly controlled entities**

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

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

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

### **Revenue recognition**

#### ***Interest income and expenses***

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

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

#### ***Fees and commission income***

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

Other fees and commission income, including account servicing fees, investment management fees, sales commission, placement fees and syndication fees, are recognised as the related services are performed.

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

#### ***Dividends***

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

### **Property and equipment**

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

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

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

## **Investment properties**

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

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

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

## **Leasing**

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

### ***The Group as lessor***

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

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

### ***The Group as lessee***

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

### ***Prepaid lease payments for land***

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

## **Foreign currencies**

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

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

For the purposes of presenting the consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated into the presentation currency of the Group (i.e. Hong Kong dollars) at the rate of exchange prevailing at the balance sheet date, and their income and expenses are translated at the average exchange rates for the year, unless

exchange rates fluctuate significantly during the period, in which case, the exchange rates prevailing at the dates of transactions are used. Exchange differences arising, if any, are recognised as a separate component of equity (the translation reserve). Such exchange differences are recognised in the consolidated income statement in the period in which the foreign operation is disposed of.

### **Retirement benefit costs**

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

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

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

### **Taxation**

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

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

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

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

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

### **Financial instruments**

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

### **Financial assets**

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



### *Effective interest method*

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

### *Financial assets at fair value through profit or loss*

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

A financial asset is classified as held for trading if:

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

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

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

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

### *Loans and receivables*

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

### *Held-to-maturity investments*

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

### *Available-for-sale financial assets*

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

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

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

### **Impairment of financial assets**

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

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

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

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

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

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

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

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

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

### **Financial liabilities and equity**

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

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

### *Effective interest method*

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

Interest expense is recognised on an effective interest basis.

### *Financial liabilities at fair value through profit or loss*

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

### *Other financial liabilities*

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

### *Offsetting financial instruments*

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

### *Equity instruments*

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

## **Derivative financial instruments**

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

## **Embedded derivatives**

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

## **Financial guarantee contracts**

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

## **Derecognition**

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

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

## **Impairment on non-financial assets**

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

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

## **Fiduciary assets**

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

## **Cash and cash equivalents**

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

## **5. CRITICAL ACCOUNTING JUDGEMENT AND KEY SOURCE OF ESTIMATION UNCERTAINTY**

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

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

### **Key sources of estimation uncertainty**

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

#### **(a) *Impairment allowances on loans and advances***

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

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

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

Details of the impairment allowances movements are disclosed in Note 20.

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

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

The fair values of investment in funds are determined based on the net asset values as reported by fund administrator.

Details of the assumptions used are disclosed in Note 7.

(c) ***Impairment of available-for-sale investments***

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

(d) ***Estimated impairment of goodwill***

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

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

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

Details of the recoverable amount calculation are disclosed in Note 33.

**Critical judgements in applying the entity's accounting policies**

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

***Held-to-maturity investments***

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

Details of these assets are set out in Note 19.

## **6. BUSINESS AND GEOGRAPHICAL SEGMENTS**

### **(a) Business segments**

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

Principal activities are as follows:

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

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

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

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

(i) Segment information about these businesses for the year ended 31 December 2008 is presented below:

# INCOME STATEMENT

	Corporate and retail banking	Treasury activities	Securities dealing	Other banking- related services	Eliminations	Consolidated
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Interest income from external customers .....	1,102,344	1,066,191	2,801	—	—	2,171,336
Interest expense to external customers .....	(1,250,306)	(56,704)	—	—	—	(1,307,010)
Inter-segment interest income (note).....	607,244	—	—	—	(607,244)	—
Inter-segment interest expense (note).....	—	(607,244)	—	—	607,244	—
Net interest income.....	459,282	402,243	2,801	—	—	864,326
Fee and commission income.....	79,368	—	139,266	46,586	—	265,220
Fee and commission expense.....	(42,985)	—	(945)	(4,489)	—	(48,419)
Net gains (losses) on financial assets designated at fair value through profit or loss .....	—	(48,508)	—	209	—	(48,299)
Other operating income.....	70,788	42,985	(86)	32,879	—	146,566
Total operating income.....	566,453	396,720	141,036	75,185	—	1,179,394
Operating expenses .....	(423,857)	(28,542)	(51,788)	(22,177)	—	(526,364)
Impairment allowances on loans and advances .....	(91,334)	—	—	—	—	(91,334)
Net gain on disposal of property and equipment .....	294	—	—	—	—	294
Net gain on disposal of available-for-sale securities .....	—	—	—	108,706	—	108,706
Fair value adjustment on investment properties .....	—	—	—	39,560	—	39,560
Impairment loss on available-for-sale securities .....	—	(264,654)	—	—	—	(264,654)
Impairment loss on goodwill.....	—	—	—	(20,000)	—	(20,000)
Segment profit .....	<u>51,556</u>	<u>103,524</u>	<u>89,248</u>	<u>181,274</u>	<u>—</u>	<u>425,602</u>
Unallocated corporate expenses.....						<u>(246,067)</u>
Profit from operations.....						179,535
Share of losses of jointly controlled entities.....				<u>(90,240)</u>		<u>(90,240)</u>
Profit before taxation.....						89,295
Taxation.....						<u>(28,675)</u>
Profit for the year.....						<u>60,620</u>

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

(i) Segment information about these businesses as at 31 December 2008 is presented below:

## BALANCE SHEET

	Corporate and retail banking	Treasury activities	Securities dealing	Other banking- related services	Consolidated
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
<b>Assets</b>					
Segment assets .....	38,347,147	29,158,388	183,804	382,208	68,071,547
Interests in jointly controlled entities .....	—	—	—	82,999	82,999
Unallocated corporate assets .....					<u>222,772</u>
Consolidated total assets .....					<u><u>68,377,318</u></u>
<b>Liabilities</b>					
Segment liabilities .....	59,594,953	2,535,119	137,056	41,089	62,308,217
Unallocated corporate liabilities .....					<u>112,477</u>
Consolidated total liabilities .....					<u><u>62,420,694</u></u>

## OTHER INFORMATION

	Corporate and retail banking	Treasury activities	Securities dealing	Other banking- related services	Unallocated	Consolidated
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Capital additions .....	45,467	651	2,024	4,830	14,695	67,667
Depreciation .....	<u>25,331</u>	<u>1,103</u>	<u>4,055</u>	<u>792</u>	<u>12,644</u>	<u>43,925</u>



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

# INCOME STATEMENT

	Corporate and retail banking	Treasury activities	Securities dealing	Other banking- related services	Eliminations	Consolidated
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Interest income from external customers ...	1,626,540	1,675,038	8,906	—	—	3,310,484
Interest expense to external customers .....	(2,228,507)	(111,364)	—	—	—	(2,339,871)
Inter-segment interest income ( <i>note</i> ) .....	1,156,760	—	—	—	(1,156,760)	—
Inter-segment interest expense ( <i>note</i> ) .....	—	(1,156,760)	—	—	1,156,760	—
Net interest income .....	554,793	406,914	8,906	—	—	970,613
Fee and commission income .....	76,659	—	202,794	47,188	—	326,641
Fee and commission expense .....	(37,162)	—	(1,672)	(4,395)	—	(43,229)
Net gains (losses) in financial assets designated at fair value through profit or loss .....	—	(12,019)	—	22,391	—	10,372
Other operating income .....	91,384	29,859	(60)	35,114	—	156,297
Total operating income .....	685,674	424,754	209,968	100,298	—	1,420,694
Operating expenses .....	(366,304)	(27,222)	(51,471)	(21,919)	—	(466,916)
Impairment allowances on loans and advances .....	(82,922)	—	—	—	—	(82,922)
Net loss on disposal of property and equipment .....	(64)	—	—	—	—	(64)
Net gain on disposal of land .....	2,591	—	—	—	—	2,591
Net gain on disposal of investment properties .....	—	—	—	14,420	—	14,420
Net gain on disposal of available-for-sale securities .....	—	—	—	177,351	—	177,351
Fair value adjustment on investment properties .....	—	—	—	14,391	—	14,391
Impairment loss on available-for-sale securities .....	—	(369,627)	—	—	—	(369,627)
Impairment loss on goodwill .....	—	—	—	(30,000)	—	(30,000)
Segment profit .....	<u>238,975</u>	<u>27,905</u>	<u>158,497</u>	<u>254,541</u>	<u>—</u>	<u>679,918</u>
Unallocated corporate expenses .....						<u>(175,978)</u>
Profit from operations .....						503,940
Share of profits of jointly controlled entities .....				<u>66,074</u>		<u>66,074</u>
Profit before taxation .....						570,014
Taxation .....						<u>(64,982)</u>
Profit for the year .....						<u>505,032</u>

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

(ii) Segment information about these businesses as at 31 December 2007 is presented below:

## BALANCE SHEET

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

## OTHER INFORMATION

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

(b) **Geographical segments**

Geographical segmentation is analysed by the Group based on the locations of the principal operations of the branches and subsidiary companies responsible for reporting the results or booking the assets. For both years 2007 and 2008, more than 90% of the Group's revenue were generated by customers located in Hong Kong and profit before taxation were generated by assets booked by the principal operations of the branches and subsidiary companies located in Hong Kong. More than 90% of assets were located in Hong Kong and the remaining assets were extended to branches outside Hong Kong, mainly in the Mainland China and America.

Details of geographical segmentation are set out below:

<b>2008</b>						
	<b>Total operating income</b>	<b>Profit before taxation</b>	<b>Total assets</b>	<b>Total liabilities</b>	<b>Total contingent liabilities and commitments</b>	<b>Capital expenditure during the year</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Hong Kong .....	1,123,459	47,197	66,291,572	61,423,248	15,270,371	59,502
Asia Pacific (excluding Hong Kong) .....	37,725	29,980	1,195,689	798,598	224,438	8,134
America .....	18,210	12,118	890,057	198,848	62,460	31
Total .....	<u>1,179,394</u>	<u>89,295</u>	<u>68,377,318</u>	<u>62,420,694</u>	<u>15,557,269</u>	<u>67,667</u>
<b>2007</b>						
	<b>Total operating income</b>	<b>Profit before taxation</b>	<b>Total assets</b>	<b>Total liabilities</b>	<b>Total contingent liabilities and commitments</b>	<b>Capital expenditure during the year</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Hong Kong .....	1,358,206	485,868	67,041,552	61,410,227	17,442,739	122,962
Asia Pacific (excluding Hong Kong) .....	39,243	67,039	1,541,043	1,134,006	325,076	8,231
America .....	23,245	17,107	469,806	237,380	176,433	28
Total .....	<u>1,420,694</u>	<u>570,014</u>	<u>69,052,401</u>	<u>62,781,613</u>	<u>17,944,248</u>	<u>131,221</u>

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

## **7. FINANCIAL RISK MANAGEMENT**

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

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

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

## Categories of financial instruments

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>Financial assets</b>				
Fair value through profit or loss .....	680,680	1,134,422	680,567	1,134,158
Held-to-maturity investments .....	9,727,685	15,607,980	9,727,685	15,607,980
Loans and receivables (including cash and cash equivalents) .....	56,662,627	50,344,014	56,462,737	49,891,059
Available-for-sale investments.....	<u>196,527</u>	<u>876,661</u>	<u>150,725</u>	<u>724,187</u>
<b>Financial liabilities</b>				
Fair value through profit or loss .....	474,384	960,546	300,653	561,132
Amortised cost.....	<u>60,927,169</u>	<u>60,784,295</u>	<u>60,923,936</u>	<u>60,780,456</u>

## Credit risk

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

## Management of credit risk

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

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

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

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

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

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

## **Risk mitigation policies**

Some specific control and mitigation measures are outlined below.

### **(a) Collateral**

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

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

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

### **(b) Other risk mitigations**

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

## **Impairment and provisioning policies**

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

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

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

<b>31 December 2008</b>					
	<b>Gross loans and advances</b>	<b>Collective impairment allowances</b>	<b>Individual impairment allowances</b>	<b>Loans and advances secured by collateral</b>	<b>Gross impaired advances</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Loans for use in Hong Kong					
Industrial, commercial and financial					
- Property development.....	1,449,043	13,268	—	208,406	—
- Property investment .....	7,561,256	—	—	6,820,072	—
- Financial concerns .....	3,031,254	—	—	1,342,433	—
- Stockbrokers .....	157,647	186	523	140,359	523
- Wholesale and retail trade.....	976,687	1,265	115	685,344	115
- Manufacturing.....	2,051,389	6,960	16	1,045,633	223
- Transport and transport equipment .....	932,535	—	—	275,741	—
- Recreational activities .....	2,535	8	—	1,284	—
- Information technology .....	198	24	—	10	—
- Others .....	5,296,954	14,241	145	2,322,465	26,646
Individuals					
- Loans for the purchase of flats in the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme.....	693,850	—	382	693,468	1,607
- Loans for the purchase of other residential properties .....	5,456,764	3,503	—	5,452,820	—
- Credit card advances .....	116,180	4,225	220	—	252
- Others .....	1,557,603	2,340	2,882	1,515,209	6,785
	29,283,895	46,020	4,283	20,503,244	36,151
Trade finance.....	804,393	7,026	—	143,778	—
Loans for use outside Hong Kong.....	3,156,339	55,942	1,516	1,727,937	64,423
	<u>33,244,627</u>	<u>108,988</u>	<u>5,799</u>	<u>22,374,959</u>	<u>100,574</u>

31 December 2007

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

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

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

#### Concentration of risks of financial assets with credit risk exposure

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

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

#### Geographical locations

	THE GROUP				THE BANK			
	Hong Kong	Asia Pacific excluding Hong Kong	Others	Total	Hong Kong	Asia Pacific excluding Hong Kong	Others	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008								
Short-term funds .....	1,616,155	5,964,649	9,643,835	17,224,639	1,573,812	5,964,649	9,643,835	17,182,296
Placements with banks and other financial institutions..	—	1,625,000	3,742,858	5,367,858	—	1,625,000	3,742,858	5,367,858
Derivative financial instruments .....	429	—	—	429	429	—	—	429
Financial assets at fair value through profit or loss .....	—	339,360	341,207	680,567	—	339,360	341,207	680,567
Available-for-sale securities....	—	—	52,395	52,395	—	—	52,395	52,395
Held-to-maturity securities .....	801,190	3,523,286	5,403,209	9,727,685	801,190	3,523,286	5,403,209	9,727,685
Advances and other accounts..	31,402,108	1,025,730	1,207,004	33,634,842	31,247,674	1,022,666	1,206,993	33,477,333
Amounts due from subsidiaries .....	—	—	—	—	3,711	—	—	3,711
	<u>33,819,882</u>	<u>12,478,025</u>	<u>20,390,508</u>	<u>66,688,415</u>	<u>33,626,816</u>	<u>12,474,961</u>	<u>20,390,497</u>	<u>66,492,274</u>

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



**Industry sectors**

	<b>THE GROUP</b>					
	<b>Financial institutions</b>	<b>Central government and central banks</b>	<b>Public sector entities</b>	<b>Corporate entities</b>	<b>Others</b>	<b>Total</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 31 December 2008						
Short term funds .....	16,249,216	975,423	—	—	—	17,224,639
Placements with banks and other financial institutions .....	5,367,858	—	—	—	—	5,367,858
Derivative financial instruments .....	—	—	—	429	—	429
Financial assets at fair value through profit or loss .....	275,085	—	—	405,482	—	680,567
Available-for-sale securities .....	35,755	—	—	16,640	—	52,395
Held-to-maturity securities .....	8,033,861	289,181	67,547	1,337,096	—	9,727,685
Advances and other accounts .....	89,187	120,605	295,132	23,901,186	9,228,732	33,634,842
	<u>30,050,962</u>	<u>1,385,209</u>	<u>362,679</u>	<u>25,660,833</u>	<u>9,228,732</u>	<u>66,688,415</u>
At 31 December 2007						
Short term funds .....	11,303,164	3,153,817	—	—	—	14,456,981
Placements with banks and other financial institutions .....	3,084,147	—	—	—	—	3,084,147
Derivative financial instruments .....	—	—	—	60	—	60
Financial assets at fair value through profit or loss .....	475,282	118,393	—	535,484	4,999	1,134,158
Available-for-sale securities .....	208,436	—	—	30,606	—	239,042
Held-to-maturity securities .....	15,060,293	534,442	11,245	2,000	—	15,607,980
Advances and other accounts .....	2,928,236	—	—	20,196,779	9,370,875	32,495,890
Loan to a jointly controlled entity .....	5,267	—	—	—	—	5,267
	<u>33,064,825</u>	<u>3,806,652</u>	<u>11,245</u>	<u>20,764,929</u>	<u>9,375,874</u>	<u>67,023,525</u>

**THE BANK**

		Central government and central banks	Public sector entities	Corporate entities	Others	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008						
Short term funds.....	16,206,873	975,423	—	—	—	17,182,296
Placements with banks and other financial institutions .....	5,367,858	—	—	—	—	5,367,858
Derivative financial instruments.....	—	—	—	429	—	429
Financial assets at fair value through profit or loss .....	275,085	—	—	405,482	—	680,567
Available-for-sale securities .....	35,755	—	—	16,640	—	52,395
Held-to-maturity securities.....	8,033,861	289,181	67,547	1,337,096	—	9,727,685
Advances and other accounts .....	88,184	120,056	295,132	23,745,229	9,228,732	33,477,333
Amounts due from subsidiaries .....	—	—	—	3,711	—	3,711
	<u>30,007,616</u>	<u>1,384,660</u>	<u>362,679</u>	<u>25,508,587</u>	<u>9,228,732</u>	<u>66,492,274</u>
At 31 December 2007						
Short term funds.....	11,252,696	3,153,817	—	—	—	14,406,513
Placements with banks and other financial institutions .....	3,084,147	—	—	—	—	3,084,147
Derivative financial instruments.....	—	—	—	60	—	60
Financial assets at fair value through profit or loss .....	475,282	118,393	—	535,484	4,999	1,134,158
Available-for-sale securities .....	208,436	—	—	30,606	—	239,042
Held-to-maturity securities.....	15,060,293	534,442	11,245	2,000	—	15,607,980
Advances and other accounts .....	2,928,236	—	—	19,794,853	9,370,351	32,093,440
Amounts due from subsidiaries .....	2,680	—	—	727	—	3,407
Loan to a jointly controlled entity.....	5,267	—	—	—	—	5,267
	<u>33,017,037</u>	<u>3,806,652</u>	<u>11,245</u>	<u>20,363,730</u>	<u>9,375,350</u>	<u>66,574,014</u>

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

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

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Short-term funds .....	17,224,639	14,456,981	17,182,296	14,406,513
Placements with banks and other financial institutions .....	5,367,858	3,084,147	5,367,858	3,084,147
Derivative financial instruments .....	429	60	429	60
Financial assets at fair value through profit or loss .....	680,567	1,134,158	680,567	1,134,158
Available-for-sale securities .....	52,395	239,042	52,395	239,042
Held-to-maturity securities .....	9,727,685	15,607,980	9,727,685	15,607,980
Advances and other accounts .....	33,634,842	32,495,890	33,477,333	32,093,440
Amounts due from subsidiaries .....	—	—	3,711	3,407
Loan to a jointly controlled entity .....	—	5,267	—	5,267
	<u>66,688,415</u>	<u>67,023,525</u>	<u>66,492,274</u>	<u>66,574,014</u>

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

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Financial guarantee and other credit related contingent liabilities .....	1,014,062	1,239,142	1,014,062	1,239,142
Loan commitments and other credit related commitments .	14,529,659	16,606,916	14,529,659	16,606,916
Other commitments .....	87,054	98,190	83,946	95,514
	<u>15,630,775</u>	<u>17,944,248</u>	<u>15,627,667</u>	<u>17,941,572</u>

#### Credit quality

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

	THE GROUP	
	31 December 2008	31 December 2007
	<i>HK\$'000</i>	<i>HK\$'000</i>
Neither past due nor impaired .....	33,234,931	31,626,817
Past due but not impaired.....	164,255	222,517
Impaired.....	<u>100,574</u>	<u>215,820</u>
	33,499,760	32,065,154
Less: allowances for impairment .....	<u>(114,787)</u>	<u>(134,596)</u>
	<u>33,384,973</u>	<u>31,930,558</u>

	THE BANK	
	31 December 2008	31 December 2007
	<i>HK\$'000</i>	<i>HK\$'000</i>
Neither past due nor impaired .....	33,234,248	31,625,904
Past due but not impaired.....	164,255	222,517
Impaired.....	<u>100,574</u>	<u>215,820</u>
	33,499,077	32,064,241
Less: allowances for impairment .....	<u>(114,783)</u>	<u>(134,590)</u>
	<u>33,384,294</u>	<u>31,929,651</u>

(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.

THE GROUP									
	Overdrafts	Instalment loans	Term loans	Syndication loans	Foreign currency loans	Trade finance	Personal loans/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 2008									
GRADES:									
Pass .....	2,112,448	14,889,393	8,975,212	5,362,572	435,557	760,580	121,027	368,136	33,024,925
Special mention .....	20,121	19,272	—	—	—	7,281	—	—	46,674
Substandard or below ....	—	15,635	—	147,697	—	—	—	—	163,332
Total .....	<u>2,132,569</u>	<u>14,924,300</u>	<u>8,975,212</u>	<u>5,510,269</u>	<u>435,557</u>	<u>767,861</u>	<u>121,027</u>	<u>368,136</u>	<u>33,234,931</u>
At 31 December 2007									
GRADES:									
Pass .....	2,482,893	12,881,686	8,631,073	5,478,920	384,865	829,442	73,648	473,598	31,236,125
Special mention .....	12,884	186,542	3,000	—	—	3,992	—	—	206,418
Substandard or below ....	—	12,552	—	171,722	—	—	—	—	184,274
Total .....	<u>2,495,777</u>	<u>13,080,780</u>	<u>8,634,073</u>	<u>5,650,642</u>	<u>384,865</u>	<u>833,434</u>	<u>73,648</u>	<u>473,598</u>	<u>31,626,817</u>
THE BANK									
	Overdrafts	Instalment loans	Term loans	Syndication loans	Foreign currency loans	Trade finance	Personal loans/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 2008									
GRADES:									
Pass .....	2,112,448	14,888,979	8,975,212	5,362,572	435,557	760,580	121,027	367,867	33,024,242
Special mention .....	20,121	19,272	—	—	—	7,281	—	—	46,674
Substandard or below ....	—	15,635	—	147,697	—	—	—	—	163,332
Total .....	<u>2,132,569</u>	<u>14,923,886</u>	<u>8,975,212</u>	<u>5,510,269</u>	<u>435,557</u>	<u>767,861</u>	<u>121,027</u>	<u>367,867</u>	<u>33,234,248</u>
At 31 December 2007									
GRADES:									
Pass .....	2,482,893	12,881,157	8,631,073	5,478,920	384,865	829,442	73,648	473,214	31,235,212
Special mention .....	12,884	186,542	3,000	—	—	3,992	—	—	206,418
Substandard or below ....	—	12,552	—	171,722	—	—	—	—	184,274
Total .....	<u>2,495,777</u>	<u>13,080,251</u>	<u>8,634,073</u>	<u>5,650,642</u>	<u>384,865</u>	<u>833,434</u>	<u>73,648</u>	<u>473,214</u>	<u>31,625,904</u>

(ii) Loans and advances past due but not impaired

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

THE GROUP AND THE BANK								
	Overdrafts	Instalment loans	Term loans	Syndication loans	Trade finance	Personal loans/tax loans	Others	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008								
Past due up to 30 days.....	3,302	10,145	—	—	1,962	—	—	15,409
Past due from 31 to 90 days .....	7,878	94,967	5,704	—	19,484	280	2,925	131,238
Past due more than 90 days.....	5,296	11,644	—	—	668	—	—	17,608
Total .....	16,476	116,756	5,704	—	22,114	280	2,925	164,255
Fair value of collateral.....	40,896	240,585	—	—	28,474	—	—	309,955
At 31 December 2007								
Past due up to 30 days.....	2,074	8,380	—	—	13,363	67	—	23,884
Past due from 31 to 90 days .....	17,503	56,550	1,460	—	35,548	302	2,919	114,282
Past due more than 90 days.....	15,779	57,468	—	—	11,104	—	—	84,351
Total .....	35,356	122,398	1,460	—	60,015	369	2,919	222,517
Fair value of collateral.....	110,490	347,862	362	—	42,737	—	—	501,451

Collateral is mainly properties and fixed deposits.

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

(iii) Loans and advances individually impaired

(a) Loans and advances to customers

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

THE GROUP AND THE BANK								
	Overdrafts	Instalment loans	Term loans	Syndication loans	Trade finance	Personal loans/tax loans	Others	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008								
Individually impaired loans.....	27,743	9,034	62,857	—	113	575	252	100,574
Fair value of collateral.....	174,295	11,920	283,958	—	—	—	—	470,173
At 31 December 2007								
Individually impaired loans.....	57,863	18,496	121,816	12,910	3,633	749	353	215,820
Fair value of collateral.....	176,991	22,871	289,241	26,000	4,400	—	—	519,503

Collaterals are mainly properties and fixed deposits.

(b) Loans and advances to banks

There are no individually impaired loans and advances to banks as at 31 December 2008 and 31 December 2007.

(iv) Loans and advances renegotiated

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

	THE GROUP AND THE BANK	
	2008	2007
	HK\$'000	HK\$'000
Renegotiated loans that would otherwise be past due or impaired.....	<u>17,017</u>	<u>918</u>

**Debt securities**

**Financial investments by rating agency designation**

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

	THE GROUP AND THE BANK			
	Financial asset at fair value through profit or loss	Available- for-sale securities (excluding equity securities)	Held-to- maturity securities	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008				
Aaa.....	—	—	653,637	653,637
Aa1 to Aa3 .....	232,475	35,755	7,210,258	7,478,488
A1 to A3.....	83,985	—	1,671,001	1,754,986
Lower than A3 .....	—	—	74,529	74,529
Unrated.....	<u>364,107</u>	<u>16,640</u>	<u>118,260</u>	<u>499,007</u>
Total .....	<u>680,567</u>	<u>52,395</u>	<u>9,727,685</u>	<u>10,460,647</u>
At 31 December 2007				
Aaa.....	71,211	—	1,244,723	1,315,934
Aa1 to Aa3 .....	499,575	39,012	11,842,288	12,380,875
A1 to A3.....	39,012	—	1,859,745	1,898,757
Lower than A3 .....	—	100,831	296,937	397,768
Unrated.....	<u>524,360</u>	<u>99,199</u>	<u>364,287</u>	<u>987,846</u>
Total .....	<u>1,134,158</u>	<u>239,042</u>	<u>15,607,980</u>	<u>16,981,180</u>

## Reposessed collateral

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

Nature of assets	THE GROUP AND THE BANK	
	2008	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>
Residential properties .....	12,750	63,070
Others .....	<u>15,644</u>	<u>39,700</u>

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

## Market risk

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

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

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

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

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

## Management of market risk

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

## Foreign exchange risk

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

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

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

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

	THE GROUP					
	HK\$	US\$	MOP	RMB	Others	Total
Hong Kong dollars equivalents (HK\$'000)						
At 31 December 2008						
Assets						
Cash and short-term funds.....	5,521,439	7,363,797	127,061	663,657	3,983,973	17,659,927
Placements with banks and other financial institutions .....	4,285,000	782,750	—	—	300,108	5,367,858
Derivative financial instruments .....	429	—	—	—	—	429
Financial assets at fair value through profit or loss .....	599,320	81,360	—	—	—	680,680
Available-for-sale securities.....	81,457	84,692	—	28,493	1,885	196,527
Held-to-maturity securities .....	4,485,688	3,366,209	—	163,432	1,712,356	9,727,685
Advances to customers .....	31,588,692	1,463,522	17,982	67,497	106,934	33,244,627
Advances to banks and other financial institutions .....	56,460	481	—	59,471	—	116,412
Other assets.....	1,174,185	161,829	590	36,638	9,931	1,383,173
Total assets.....	47,792,670	13,304,640	145,633	1,019,188	6,115,187	68,377,318
Liabilities						
Deposits and balances of banks and other financial institutions .....	1,114,675	332,181	—	—	78,653	1,525,509
Deposits from customers .....	40,452,603	11,944,793	96,525	870,132	6,037,607	59,401,660
Derivative financial instruments .....	39,303	—	—	—	—	39,303
Loan capital .....	(3,296)	968,750	—	—	—	965,454
Other liabilities .....	419,539	37,181	2,782	5,280	23,986	488,768
Total liabilities .....	42,022,824	13,282,905	99,307	875,412	6,140,246	62,420,694
Net on-balance sheet position .....	5,769,846	21,735	46,326	143,776	(25,059)	5,956,624



	THE GROUP					
	HK\$	US\$	MOP	RMB	Others	Total
Hong Kong dollars equivalents (HK\$'000)						
At 31 December 2007						
Assets						
Cash and short-term funds.....	9,814,179	3,269,551	85,227	460,829	1,134,191	14,763,977
Placements with banks and other financial institutions .....	959,999	1,630,681	—	—	493,467	3,084,147
Derivative financial instruments .....	60	—	—	—	—	60
Financial assets at fair value through profit or loss .....	807,088	327,334	—	—	—	1,134,422
Available-for-sale securities.....	224,822	647,823	—	—	4,016	876,661
Held-to-maturity securities .....	6,061,007	6,128,323	—	69,700	3,348,950	15,607,980
Advances to customers .....	30,256,331	1,248,302	26,973	—	190,277	31,721,883
Advances to banks and other financial institutions .....	56,670	414	—	—	—	57,084
Other assets.....	1,584,552	196,331	170	10,444	14,690	1,806,187
Total assets.....	49,764,708	13,448,759	112,370	540,973	5,185,591	69,052,401
Liabilities						
Deposits and balances of banks and other financial institutions .....	3,116	277,707	—	—	176,035	456,858
Deposits from customers .....	42,301,866	12,389,216	62,443	434,323	5,139,589	60,327,437
Derivative financial instruments .....	114,546	—	—	—	—	114,546
Loan capital .....	(4,417)	975,288	—	—	—	970,871
Other liabilities .....	799,007	77,984	3,843	7,679	23,388	911,901
Total liabilities .....	43,214,118	13,720,195	66,286	442,002	5,339,012	62,781,613
Net on-balance sheet position .....	6,550,590	(271,436)	46,084	98,971	(153,421)	6,270,788

	THE BANK					
	<i>HK\$</i>	<i>US\$</i>	<i>MOP</i>	<i>RMB</i>	<i>Others</i>	<i>Total</i>
Hong Kong dollars equivalents (HK\$'000)						
At 31 December 2008						
Assets						
Cash and short-term funds.....	5,479,058	7,363,797	127,061	663,657	3,983,973	17,617,546
Placements with banks and other financial institutions .....	4,285,000	782,750	—	—	300,108	5,367,858
Derivative financial instruments .....	429	—	—	—	—	429
Financial assets at fair value through profit or loss .....	599,207	81,360	—	—	—	680,567
Available-for-sale securities.....	35,655	84,692	—	28,493	1,885	150,725
Held-to-maturity securities .....	4,485,688	3,366,209	—	163,432	1,712,356	9,727,685
Advances to customers .....	31,588,278	1,463,522	17,982	67,497	106,934	33,244,213
Advances to banks and other financial institutions .....	56,460	481	—	59,471	—	116,412
Other assets.....	1,742,715	161,829	590	8,302	9,931	1,923,367
Total assets.....	48,272,490	13,304,640	145,633	990,852	6,115,187	68,828,802
Liabilities						
Deposits and balances of banks and other financial institutions.....	1,114,675	332,181	—	—	78,653	1,525,509
Deposits from customers .....	40,449,370	11,944,793	96,525	870,132	6,037,607	59,398,427
Derivative financial instruments .....	39,303	—	—	—	—	39,303
Loan capital .....	(3,296)	968,750	—	—	—	965,454
Other liabilities .....	942,098	37,181	2,782	2,695	23,986	1,008,742
Total liabilities .....	42,542,150	13,282,905	99,307	872,827	6,140,246	62,937,435
Net on-balance sheet position .....	5,730,340	21,735	46,326	118,025	(25,059)	5,891,367

	THE BANK					
	HK\$	US\$	MOP	RMB	Others	Total
Hong Kong dollars equivalents (HK\$'000)						
At 31 December 2007						
Assets						
Cash and short-term funds.....	9,763,674	3,269,551	85,227	460,829	1,134,191	14,713,472
Placements with banks and other financial institutions .....	959,999	1,630,681	—	—	493,467	3,084,147
Derivative financial instruments .....	60	—	—	—	—	60
Financial assets at fair value through profit or loss .....	806,824	327,334	—	—	—	1,134,158
Available-for-sale securities.....	72,348	647,823	—	—	4,016	724,187
Held-to-maturity securities .....	6,061,007	6,128,323	—	69,700	3,348,950	15,607,980
Advances to customers .....	30,255,802	1,248,302	26,973	—	190,277	31,721,354
Advances to banks and other financial institutions .....	56,670	414	—	—	—	57,084
Other assets.....	1,825,867	196,331	170	8,298	14,690	2,045,356
Total assets.....	49,802,251	13,448,759	112,370	538,827	5,185,591	69,087,798
Liabilities						
Deposits and balances of banks and other financial institutions .....	3,116	277,707	—	—	176,035	456,858
Deposits from customers .....	42,298,027	12,389,216	62,443	434,323	5,139,589	60,323,598
Derivative financial instruments .....	114,546	—	—	—	—	114,546
Loan capital .....	(4,417)	975,288	—	—	—	970,871
Other liabilities .....	1,008,179	77,984	3,843	5,533	23,388	1,118,927
Total liabilities .....	43,419,451	13,720,195	66,286	439,856	5,339,012	62,984,800
Net on-balance sheet position .....	6,382,800	(271,436)	46,084	98,971	(153,421)	6,102,998

#### Foreign currency sensitivity

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

	Change in currency rate					
	US Dollars		Renminbi		Macau Pataca	
	Appreciate	Depreciate	Appreciate	Depreciate	Appreciate	Depreciate
	+1%	- 1%	+10%	- 10%	+10%	- 10%
<b>THE GROUP</b>						
Hong Kong dollars equivalents (HK\$'000)						
2008						
Profit before tax.....	(903)	903	14,536	(14,536)	4,633	(4,633)
Other equity .....	23	(23)	—	—	—	—
	<u>23</u>	<u>(23)</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>
2007						
Profit before tax.....	(2,855)	2,855	9,818	(9,818)	4,608	(4,608)
Other equity .....	46	(46)	—	—	—	—
	<u>46</u>	<u>(46)</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>
<b>THE BANK</b>						
2008						
Profit before tax.....	(903)	903	11,961	(11,961)	4,633	(4,633)
Other equity .....	23	(23)	—	—	—	—
	<u>23</u>	<u>(23)</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>
2007						
Profit before tax.....	(2,855)	2,855	9,818	(9,818)	4,608	(4,608)
Other equity .....	46	(46)	—	—	—	—
	<u>46</u>	<u>(46)</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>

Numbers in bracket mean decrease.

#### Interest rate risk

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

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

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

	THE GROUP					
	Up to 3 months	3 - 12 months	1 - 5 years	Over 5 years	Non- interest bearing	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008						
Assets						
Cash and short-term funds .....	16,941,384	271,937	—	—	446,606	17,659,927
Placements with banks and other financial institutions .....	4,449,267	918,591	—	—	—	5,367,858
Derivative financial instruments.....	—	—	—	—	429	429
Financial assets at fair value through profit or loss .....	599,208	—	—	—	81,472	680,680
Available-for-sale securities .....	35,754	—	—	—	160,773	196,527
Held-to-maturity securities.....	7,408,355	2,293,174	24,156	—	2,000	9,727,685
Advances to customers.....	32,309,117	737,016	58,967	3,106	136,421	33,244,627
Advances to banks and other financial institutions .....	85,063	30,408	—	—	941	116,412
Other assets .....	—	—	—	—	1,383,173	1,383,173
Total assets .....	<u>61,828,148</u>	<u>4,251,126</u>	<u>83,123</u>	<u>3,106</u>	<u>2,211,815</u>	<u>68,377,318</u>
Liabilities						
Deposits and balances of banks and other financial institutions .....	1,514,356	—	—	—	11,153	1,525,509
Deposits from customers.....	52,972,817	3,416,549	4,621	—	3,007,673	59,401,660
Derivative financial instruments.....	—	—	—	—	39,303	39,303
Loan capital.....	965,454	—	—	—	—	965,454
Other liabilities.....	—	—	—	—	488,768	488,768
Total liabilities .....	<u>55,452,627</u>	<u>3,416,549</u>	<u>4,621</u>	<u>—</u>	<u>3,546,897</u>	<u>62,420,694</u>
Total interest sensitivity gap .....	<u>6,375,521</u>	<u>834,577</u>	<u>78,502</u>	<u>3,106</u>	<u>(1,335,082)</u>	<u>5,956,624</u>

**THE GROUP**

	<b>Up to 3 months</b>	<b>3 - 12 months</b>	<b>1 - 5 years</b>	<b>Over 5 years</b>	<b>Non- interest bearing</b>	<b>Total</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 31 December 2007						
<b>Assets</b>						
Cash and short-term funds .....	14,361,137	51,052	—	—	351,788	14,763,977
Placements with banks and other financial institutions .....	2,684,574	399,573	—	—	—	3,084,147
Derivative financial instruments.....	—	—	—	—	60	60
Financial assets at fair value through profit or loss .....	861,059	—	78,023	—	195,340	1,134,422
Available-for-sale securities .....	239,042	—	—	—	637,619	876,661
Held-to-maturity securities.....	12,871,862	2,655,195	78,923	—	2,000	15,607,980
Advances to customers.....	30,561,808	822,886	50,875	2,846	283,468	31,721,883
Advances to banks and other financial institutions .....	9,733	20,620	26,731	—	—	57,084
Other assets .....	—	—	—	—	1,806,187	1,806,187
<b>Total assets .....</b>	<b>61,589,215</b>	<b>3,949,326</b>	<b>234,552</b>	<b>2,846</b>	<b>3,276,462</b>	<b>69,052,401</b>
<b>Liabilities</b>						
Deposits and balances of banks and other financial institutions .....	437,555	—	—	—	19,303	456,858
Deposits from customers.....	54,953,819	2,355,240	13,216	—	3,005,162	60,327,437
Derivative financial instruments.....	—	—	—	—	114,546	114,546
Loan capital.....	970,871	—	—	—	—	970,871
Other liabilities.....	—	—	—	—	911,901	911,901
<b>Total liabilities .....</b>	<b>56,362,245</b>	<b>2,355,240</b>	<b>13,216</b>	<b>—</b>	<b>4,050,912</b>	<b>62,781,613</b>
<b>Total interest sensitivity gap .....</b>	<b>5,226,970</b>	<b>1,594,086</b>	<b>221,336</b>	<b>2,846</b>	<b>(774,450)</b>	<b>6,270,788</b>

THE BANK						
	Up to 3 months	3 - 12 months	1 - 5 years	Over 5 years	Non- interest bearing	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008						
Assets						
Cash and short-term funds .....	16,882,390	271,937	—	—	463,219	17,617,546
Placements with banks and other financial institutions .....	4,449,267	918,591	—	—	—	5,367,858
Derivative financial instruments.....	—	—	—	—	429	429
Financial assets at fair value through profit or loss .....	599,207	—	—	—	81,360	680,567
Available-for-sale securities .....	35,754	—	—	—	114,971	150,725
Held-to-maturity securities.....	7,408,355	2,293,174	24,156	—	2,000	9,727,685
Advances to customers.....	32,308,703	737,016	58,967	3,106	136,421	33,244,213
Advances to bank and other financial institutions.....	85,063	30,408	—	—	941	116,412
Other assets .....	—	—	—	—	1,923,367	1,923,367
Total assets .....	<u>61,768,739</u>	<u>4,251,126</u>	<u>83,123</u>	<u>3,106</u>	<u>2,722,708</u>	<u>68,828,802</u>
Liabilities						
Deposits and balances of banks and other financial institutions .....	1,514,356	—	—	—	11,153	1,525,509
Deposits from customers.....	52,969,584	3,416,549	4,621	—	3,007,673	59,398,427
Derivative financial instruments.....	—	—	—	—	39,303	39,303
Loan capital.....	965,454	—	—	—	—	965,454
Other liabilities.....	697,853	—	—	—	310,889	1,008,742
Total liabilities .....	<u>56,147,247</u>	<u>3,416,549</u>	<u>4,621</u>	<u>—</u>	<u>3,369,018</u>	<u>62,937,435</u>
Total interest sensitivity gap .....	<u>5,621,492</u>	<u>834,577</u>	<u>78,502</u>	<u>3,106</u>	<u>(646,310)</u>	<u>5,891,367</u>

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

#### Interest rate sensitivity

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

	2008		2007	
	Change in basis points		Change in basis points	
	+100	- 100	+100	- 100
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>THE GROUP</b>				
Profit before tax .....	59,773	(59,773)	45,970	(45,970)
Other equity.....	<u>(14)</u>	<u>14</u>	<u>(771)</u>	<u>771</u>
<b>THE BANK</b>				
Profit before tax .....	59,209	(59,209)	45,437	(45,437)
Other equity.....	<u>(14)</u>	<u>14</u>	<u>(771)</u>	<u>771</u>

Numbers in bracket mean decrease.



## Price risk

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

### Price sensitivity

	2008		2007	
	Change in price		Change in price	
	+10%	- 10%	+10%	- 10%
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>THE GROUP</b>				
Profit before tax .....	31,355	(31,355)	52,977	(52,977)
Other equity .....	<u>13,356</u>	<u>(13,356)</u>	<u>39,606</u>	<u>(39,606)</u>
<b>THE BANK</b>				
Profit before tax .....	31,355	(31,355)	52,977	(52,977)
Other equity .....	<u>9,173</u>	<u>(9,173)</u>	<u>24,627</u>	<u>(24,627)</u>

Numbers in bracket mean decrease.

## Liquidity risk

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

### Management of liquidity risk

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

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

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

**THE GROUP**

	<b>Repayable on demand</b>	<b>Repayable within 3 months</b>	<b>Repayable after 3 months but within 1 year</b>	<b>Repayable after 1 year but within 5 years</b>	<b>Repayable after 5 years</b>	<b>Undated</b>	<b>Total</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 31 December 2008							
Deposits and balances of banks and other financial institutions	71,607	1,458,473	245	—	—	—	1,530,325
Deposits from customers.....	16,859,622	39,202,581	3,427,260	54,953	—	42,445	59,586,861
Loan capital.....	—	7,059	20,716	1,023,993	—	—	1,051,768
Other liabilities .....	296,833	41,857	24,962	23,095	—	—	386,747
Total undiscounted financial liabilities .....	<u>17,228,062</u>	<u>40,709,970</u>	<u>3,473,183</u>	<u>1,102,041</u>	<u>—</u>	<u>42,445</u>	<u>62,555,701</u>
At 31 December 2007							
Deposits and balances of banks and other financial institutions	27,205	435,689	—	—	—	—	462,894
Deposits from customers.....	15,600,482	42,888,552	2,165,694	33,069	—	7,627	60,695,424
Loan capital.....	—	14,596	43,307	1,146,271	—	—	1,204,174
Other liabilities .....	592,339	23,734	54,454	29,193	—	1,960	701,680
Total undiscounted financial liabilities .....	<u>16,220,026</u>	<u>43,362,571</u>	<u>2,263,455</u>	<u>1,208,533</u>	<u>—</u>	<u>9,587</u>	<u>63,064,172</u>

**THE BANK**

	<b>Repayable on demand</b>	<b>Repayable within 3 months</b>	<b>Repayable after 3 months but within 1 year</b>	<b>Repayable after 1 year but within 5 years</b>	<b>Repayable after 5 years</b>	<b>Undated</b>	<b>Total</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 31 December 2008							
Deposits and balances of banks and other financial institutions	71,607	1,458,473	245	—	—	—	1,530,325
Deposits from customers.....	16,859,523	39,199,348	3,427,260	54,953	—	42,445	59,583,529
Loan capital.....	—	7,059	20,716	1,023,993	—	—	1,051,768
Other liabilities .....	444,000	451,952	7,124	3,744	—	—	906,820
Total undiscounted financial liabilities .....	<u>17,375,130</u>	<u>41,116,832</u>	<u>3,455,345</u>	<u>1,082,690</u>	<u>—</u>	<u>42,445</u>	<u>63,072,442</u>
At 31 December 2007							
Deposits and balances of banks and other financial institutions	27,205	435,689	—	—	—	—	462,894
Deposits from customers.....	15,600,381	42,884,712	2,165,694	33,069	—	7,627	60,691,483
Loan capital.....	—	14,596	43,307	1,146,271	—	—	1,204,174
Other liabilities .....	514,998	387,863	5,947	—	—	—	908,808
Total undiscounted financial liabilities .....	<u>16,142,584</u>	<u>43,722,860</u>	<u>2,214,948</u>	<u>1,179,340</u>	<u>—</u>	<u>7,627</u>	<u>63,267,359</u>

The following tables detail the Group's and the Bank'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 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 reporting date.

**THE GROUP AND THE BANK**

	<b>Less than 1 month</b>	<b>1 - 3 months</b>	<b>3 months to 1 year</b>	<b>1 - 5 years</b>	<b>Over 5 years</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 31 December 2008					
Derivatives settled net					
Interest rate contracts .....	<u>(46)</u>	<u>1,361</u>	<u>(26,122)</u>	<u>(28,943)</u>	<u>—</u>
Derivatives settled gross					
Exchange rate contracts					
- inflow .....	28,090	8,146	158,239	—	—
- outflow .....	<u>(28,360)</u>	<u>(7,936)</u>	<u>(158,354)</u>	<u>—</u>	<u>—</u>
	<u>(270)</u>	<u>210</u>	<u>(115)</u>	<u>—</u>	<u>—</u>
At 31 December 2007					
Derivatives settled net					
Interest rate contracts .....	<u>5,244</u>	<u>3,743</u>	<u>5,040</u>	<u>(15,283)</u>	<u>—</u>
Derivatives settled gross					
Exchange rate contracts					
- inflow .....	24,223	4,625	62,808	—	—
- outflow .....	<u>(24,286)</u>	<u>(3,946)</u>	<u>(64,127)</u>	<u>—</u>	<u>—</u>
	<u>(63)</u>	<u>679</u>	<u>(1,319)</u>	<u>—</u>	<u>—</u>

## Off-balance sheet items

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

THE GROUP				
	No later than 1 year	1 - 5 years	Over 5 years	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008				
Loan commitments .....	14,529,659	—	—	14,529,659
Guarantee, acceptances and other financial facilities .....	1,014,062	—	—	1,014,062
Operating lease commitments .....	39,714	33,792	—	73,506
Capital commitments .....	13,548	—	—	13,548
Total .....	<u>15,596,983</u>	<u>33,792</u>	<u>—</u>	<u>15,630,775</u>
At 31 December 2007				
Loan commitments .....	16,606,916	—	—	16,606,916
Guarantee, acceptances and other financial facilities .....	1,239,142	—	—	1,239,142
Operating lease commitments .....	28,150	36,839	275	65,264
Capital commitments .....	32,926	—	—	32,926
Total .....	<u>17,907,134</u>	<u>36,839</u>	<u>275</u>	<u>17,944,248</u>
THE BANK				
	No later than 1 year	1-5 years	Over 5 years	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008				
Loan commitments .....	14,529,659	—	—	14,529,659
Guarantee, acceptances and other financial facilities .....	1,014,062	—	—	1,014,062
Operating lease commitments .....	38,066	32,332	—	70,398
Capital commitments .....	13,548	—	—	13,548
Total .....	<u>15,595,335</u>	<u>32,332</u>	<u>—</u>	<u>15,627,667</u>
At 31 December 2007				
Loan commitments .....	16,606,916	—	—	16,606,916
Guarantee, acceptances and other financial facilities .....	1,239,142	—	—	1,239,142
Operating lease commitments .....	26,288	36,025	275	62,588
Capital commitments .....	32,926	—	—	32,926
Total .....	<u>17,905,272</u>	<u>36,025</u>	<u>275</u>	<u>17,941,572</u>

## Analysis of assets and liabilities by remaining maturity

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

	THE GROUP						
	Repayable on demand	Repayable within 3 months or less (except those repayable on demand)	Repayable after 3 months but within 1 year	Repayable after 1 year but within 5 years	Repayable after 5 years	Undated	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008							
Assets							
Cash and short-term funds.....	4,162,520	13,267,824	229,583	—	—	—	17,659,927
Placements with banks and other financial institutions .....	—	4,449,267	918,591	—	—	—	5,367,858
Derivative financial assets.....	—	—	—	—	—	429	429
Financial assets at fair value through profit or loss .....	—	49,350	295,228	335,990	—	112	680,680
Available-for-sale securities.....	—	—	—	35,755	16,640	144,132	196,527
Held-to-maturity securities .....	—	2,550,748	3,295,114	3,876,303	3,520	2,000	9,727,685
Advances to customers .....	2,506,692	4,471,595	4,868,474	11,571,972	9,549,718	276,176	33,244,627
Advances to banks and other financial institutions .....	26,380	40,032	50,000	—	—	—	116,412
Total other assets .....	183,817	164,435	77,616	6,691	—	950,614	1,383,173
Total assets .....	6,879,409	24,993,251	9,734,606	15,826,711	9,569,878	1,373,463	68,377,318
Liabilities							
Deposits and balances of banks and other financial institutions .....	71,494	1,454,015	—	—	—	—	1,525,509
Deposits from customers .....	16,859,032	39,078,582	3,370,024	51,577	—	42,445	59,401,660
Derivative financial liabilities .....	—	—	—	—	—	39,303	39,303
Loan capital .....	—	—	—	—	965,454	—	965,454
Other liabilities .....	297,326	126,935	41,242	23,265	—	—	488,768
Total liabilities.....	17,227,852	40,659,532	3,411,266	74,842	965,454	81,748	62,420,694
Net liquidity gap.....	(10,348,443)	(15,666,281)	6,323,340	15,751,869	8,604,424	1,291,715	5,956,624

THE GROUP

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

THE BANK

	Repayable on demand	Repayable within 3 months or less (except those repayable on demand)	Repayable after 3 months but within 1 year	Repayable after 1 year but within 5 years	Repayable after 5 years	Undated	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2008							
Assets							
Cash and short-term funds.....	4,157,401	13,230,562	229,583	—	—	—	17,617,546
Placements with banks and other financial institutions .....	—	4,449,267	918,591	—	—	—	5,367,858
Derivative financial assets.....	—	—	—	—	—	429	429
Financial assets at fair value through profit or loss .....	—	49,349	295,228	335,990	—	—	680,567
Available-for-sale securities.....	—	—	—	35,755	16,640	98,330	150,725
Held-to-maturity securities .....	—	2,550,748	3,295,114	3,876,303	3,520	2,000	9,727,685
Advances to customers .....	2,506,692	4,471,565	4,868,383	11,571,679	9,549,718	276,176	33,244,213
Advances to banks and other financial institutions .....	26,380	40,032	50,000	—	—	—	116,412
Other assets.....	36,029	162,806	75,789	6,691	—	1,642,052	1,923,367
Total assets .....	6,726,502	24,954,329	9,732,688	15,826,418	9,569,878	2,018,987	68,828,802
Liabilities							
Deposits and balances of banks and other financial institutions .....	71,494	1,454,015	—	—	—	—	1,525,509
Deposits from customers .....	16,859,032	39,075,349	3,370,024	51,577	—	42,445	59,398,427
Derivative financial instruments .....	—	—	—	—	—	39,303	39,303
Loan capital .....	—	—	—	—	965,454	—	965,454
Other liabilities .....	444,394	537,030	23,404	3,914	—	—	1,008,742
Total liabilities.....	17,374,920	41,066,394	3,393,428	55,491	965,454	81,748	62,937,435
Net liquidity gap.....	(10,648,418)	(16,112,065)	6,339,260	15,770,927	8,604,424	1,937,239	5,891,367

**THE BANK**

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

**Fair value of financial assets and liabilities**

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

	<b>THE GROUP AND THE BANK</b>			
	<b>Carrying value</b>		<b>Fair value</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
<b>Financial assets</b>				
- Held-to-maturity securities .....	<u>9,727,685</u>	<u>15,607,980</u>	<u>9,658,947</u>	<u>15,144,333</u>
<b>Financial liabilities</b>				
- Loan capital .....	<u>965,454</u>	<u>970,871</u>	<u>775,000</u>	<u>944,523</u>



The fair value of financial assets and financial liabilities are determined as follows:

- the fair value of financial assets and financial liabilities (including derivative instruments) with standard terms and conditions and traded in active liquid markets are determined with reference to quoted market bid prices and ask prices respectively;
- the fair value of investment in funds are determined based on the net asset values as reported by the fund administrator; and
- the fair value of derivative instruments is calculated using quoted prices. Where such prices are not available, use is made of discounted cash flow analysis using the applicable yield curve for the duration of the instruments for non-optional derivatives, and option pricing models for optional derivatives.

### Capital management

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

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

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

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

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

### Capital Adequacy Ratio

	2008	2007
	%	%
Capital adequacy ratio.....	15.64	14.22
Core capital ratio .....	12.55	11.52

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

## Capital base

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

	2008	2007
	HK\$'000	HK\$'000
Core capital		
Paid-up ordinary share capital .....	217,500	217,500
Share premium .....	1,542,817	1,542,817
Published reserves .....	3,348,465	3,231,676
Profit and loss account .....	78,501	56,732
Less: Net deferred tax assets .....	(1)	(2,079)
Total core capital .....	5,187,282	5,046,646
Other deductions from core capital .....	(143,357)	(418,739)
Core capital after deductions .....	5,043,925	4,627,907
Supplementary capital		
Reserves attributable to fair value gains on revaluation of holdings of land and buildings .....	5,755	5,755
Collective impairment allowances .....	108,988	116,720
Regulatory reserve for general banking risks .....	307,000	356,000
Reserves attributable to fair value gains on revaluation of holdings of available-for-sale equities and debt securities .....	(2,415)	10,062
Unrealised fair value gains arising from holdings of equities and debt securities designated at fair value through profit or loss .....	—	45,807
Term subordinated debt .....	965,454	970,871
Total supplementary capital .....	1,384,782	1,505,215
Other deductions from supplementary capital .....	(143,357)	(418,740)
Supplementary capital after deductions .....	1,241,425	1,086,475
Total capital base after deductions .....	6,285,350	5,714,382

Deductions from total capital base mainly include investments in subsidiaries of which their risk-weighted assets have not been consolidated into the total risk-weighted assets of the Group, which mainly conduct non-banking related business. Those subsidiaries are Chong Hing Commodities and Futures Limited, Chong Hing Insurance Company Limited, Chong Hing (Management) Limited, Chong Hing (Nominees) Limited and Chong Hing Securities Limited.

## 8. NET INTEREST INCOME

	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Interest income		
Short term funds and placements.....	606,587	978,648
Investments in securities .....	476,408	718,519
Loans and advances .....	1,088,341	1,613,317
	<u>2,171,336</u>	<u>3,310,484</u>
Interest expense .....		
Deposits and balances from banks and customers.....	(1,264,888)	(2,275,900)
Loan capital in issue .....	(42,122)	(63,971)
	<u>(1,307,010)</u>	<u>(2,339,871)</u>
Net interest income .....	<u>864,326</u>	<u>970,613</u>
Included within interest income		
Interest income on impaired loans and advances .....	<u>4,415</u>	<u>19,417</u>

Included within interest income and interest expense are HK\$2,156,946,000 (2007: HK\$3,294,634,000) and HK\$1,307,010,000 (2007: HK\$2,339,871,000) for financial assets and financial liabilities that are not at fair value through profit or loss, respectively.

## 9. NET FEE AND COMMISSION INCOME

	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Fees and commission income		
Securities dealings .....	139,266	202,794
Credit lines .....	8,034	7,618
Trade finance .....	14,409	15,397
Credit card services .....	49,214	42,106
Agency services .....	46,586	47,187
Others .....	7,711	11,539
Total fees and commission income .....	265,220	326,641
Less: Fees and commission expense .....	(48,419)	(43,229)
Net fees and commission income.....	<u>216,801</u>	<u>283,412</u>
of which:		
Net fee income, other than amounts included in determining the effective interest rate, arising from financial assets or financial liabilities that are not held for trading nor designated at fair value		
- fee income.....	73,911	70,936
- fee expense.....	(42,648)	(37,051)
	<u>31,263</u>	<u>33,885</u>

**10. NET (LOSSES) GAINS ON FINANCIAL ASSETS DESIGNATED AT FAIR VALUE THROUGH PROFIT OR LOSS**

	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Net (losses) gains on financial assets at fair value through profit or loss		
- designated at fair value through profit or loss.....	(123,908)	127,980
- deemed held for trading.....	75,609	(117,608)
	<u>(48,299)</u>	<u>10,372</u>

**11. OTHER OPERATING INCOME**

	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Dividend income		
Listed investments .....	9,773	8,979
Unlisted investments .....	3,080	2,880
Net gains on dealing in foreign currencies .....	42,985	29,859
Gross rents from investment properties.....	13,035	11,910
Less: Outgoings .....	(948)	(961)
Net rental income.....	12,087	10,949
Safe deposit box rentals .....	25,702	25,064
Insurance underwriting profit .....	8,336	10,130
Other banking services income .....	41,508	41,595
Actuarial gain on retirement scheme.....	—	21,914
Others .....	3,095	4,927
	<u>146,566</u>	<u>156,297</u>

**12. OPERATING EXPENSES**

	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Actuarial loss on retirement scheme .....	21,862	—
Amortisation of prepaid lease payments for land.....	6,104	5,710
Auditor's remuneration.....	3,678	3,579
Staff costs		
Salaries and other costs.....	393,953	355,624
Retirement benefits scheme contributions.....	29,779	26,620
Total staff costs.....	423,732	382,244
Depreciation.....	43,925	36,846
Premises and equipment expenses, excluding depreciation/amortisation		
Rentals and rates for premises.....	38,896	35,747
Others .....	22,247	17,842
Other operating expenses.....	211,987	160,926
	<u>772,431</u>	<u>642,894</u>

Included in the premises and equipment expenses are minimum lease payments under operating lease of HK\$34,655,000 (2007: HK\$31,246,000).

### 13. DIRECTORS' AND EMPLOYEES' EMOLUMENTS

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

	2008				2007			
	Contribution to Salaries and other retirement benefits scheme Total				Contribution to Salaries and other retirement benefits scheme Total			
	Fees	Salaries and other benefits	retirement benefits scheme	Total	Fees	Salaries and other benefits	retirement benefits scheme	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Executive directors (Hong Kong)								
Liu Lit Man .....	120	5,437	350	5,907	120	5,454	350	5,924
Liu Lit Mo .....	70	487	45	602	70	488	45	603
Liu Lit Chi .....	70	5,536	259	5,865	70	8,328	224	8,622
Don Tit Shing Liu .....	70	2,484	244	2,798	70	2,198	217	2,485
Lau Wai Man .....	70	2,328	232	2,630	70	2,053	205	2,328
Wilfred Chun Ning Liu .....	70	2,345	167	2,582	70	2,215	163	2,448
Tsang Chiu Wing .....	70	2,118	188	2,376	70	1,845	155	2,070
Wong Har Kar .....	70	2,020	155	2,245	70	1,827	131	2,028
Frank Shui Sang Jin .....	44	1,354	135	1,533	70	1,977	196	2,243
Total executive directors .....	654	24,109	1,775	26,538	680	26,385	1,686	28,751
Non-executive directors (Hong Kong)								
Timothy George Freshwater .....	100	80	—	180	100	80	—	180
Wang Xiaomong .....	58	—	—	58	—	—	—	—
Andrew Liu .....	70	29	—	99	70	11	—	81
Eiichi Yoshikawa .....	70	—	—	70	33	—	—	33
Christopher Kwun Shing Liu .....	70	—	—	70	70	—	—	70
Alfred Cheuk Yu Chow .....	100	—	—	100	100	—	—	100
Meng Qinghui .....	58	—	—	58	—	—	—	—
Xu Minjie .....	12	—	—	12	33	—	—	33
Wang Zhi .....	12	—	—	12	70	—	—	70
Sun Jiakang .....	—	—	—	—	37	—	—	37
Toshiaki Arai .....	—	—	—	—	37	—	—	37
Total non-executive directors .....	550	109	—	659	550	91	—	641
Independent non-executive directors (Hong Kong)								
Robin Yau Hing Chan .....	100	—	—	100	100	—	—	100
Wanchai Chiranakhorn .....	100	—	—	100	100	—	—	100
Cheng Yuk Wo .....	100	—	—	100	100	—	—	100
Andrew Chiu Cheung Ma .....	100	—	—	100	40	—	—	40
Total independent non-executive directors .....	400	—	—	400	340	—	—	340
Total .....	1,604	24,218	1,775	27,597	1,570	26,476	1,686	29,732

The five highest paid individuals in the Group in 2008 and 2007 were all directors of the Bank and details of their emoluments are included in Note 13 above.

#### 14. TAXATION

	2008	2007
	HK\$'000	HK\$'000
The tax charge comprises:		
Hong Kong Profits Tax		
- current year .....	11,254	63,824
- under (over) provision in prior years .....	325	(557)
	11,579	63,267
Overseas taxation .....	6,027	3,724
Deferred tax ( <i>Note 30</i> ) .....	11,069	(2,009)
	<u>28,675</u>	<u>64,982</u>

Hong Kong Profits Tax is calculated at 16.5% (2007: 17.5%) of the estimated assessable profit for the year. Taxation arising in other jurisdictions is calculated at the rates prevailing in the relevant jurisdictions.

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

	2008	2007
	HK\$'000	HK\$'000
Profit before taxation .....	<u>89,295</u>	<u>570,014</u>
Tax at the domestic income tax rate of 16.5% (2007: 17.5%) .....	14,734	99,752
Tax effect of share of loss (profit) of jointly controlled entities .....	14,890	(11,563)
Tax effect of expenses not deductible for tax purpose .....	20,044	6,316
Tax effect of income not taxable for tax purpose.....	(21,746)	(27,133)
Utilisation of tax losses previously not recognised .....	—	(437)
Under (over) provision in prior years .....	1,258	(557)
Effect of different tax rates of subsidiaries operating in other jurisdictions .....	(550)	(1,541)
Effect of changes in tax rates of deferred tax.....	45	—
Others .....	<u>—</u>	<u>145</u>
Tax charge for the year .....	<u>28,675</u>	<u>64,982</u>

#### 15. DIVIDENDS

	2008	2007
	HK\$'000	HK\$'000
Dividends recognised as distribution during the year:		
2008 Interim - HK\$0.15 (2007: HK\$0.21) per share.....	65,250	91,350
2007 Final - HK\$0.44 (2006: HK\$0.44) per share .....	<u>191,400</u>	<u>191,400</u>
	<u>256,650</u>	<u>282,750</u>

The final dividend of HK\$0.05 per share in respect of the current financial year (2007: HK\$0.44) has been proposed by the directors and is subject to approval by the shareholders in the next annual general meeting.

#### 16. EARNINGS PER SHARE

The calculation of basic and diluted earnings per share is based on the profit attributable to shareholders of HK\$60,620,000 (2007: HK\$505,032,000) and on 435,000,000 (2007: 435,000,000) ordinary shares in issue during the year.

## 17. CASH AND SHORT-TERM FUNDS

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Cash and balances with banks and other financial institutions .....	4,087,415	1,833,309	4,082,297	1,833,210
Money at call and short notice.....	13,180,425	9,776,851	13,143,162	9,726,445
Exchange fund bills .....	392,087	3,153,817	392,087	3,153,817
	<u>17,659,927</u>	<u>14,763,977</u>	<u>17,617,546</u>	<u>14,713,472</u>

## 18. DERIVATIVE FINANCIAL INSTRUMENTS

THE GROUP AND THE BANK						
	2008			2007		
	Notional amount	Fair values		Notional amount	Fair values	
		Assets	Liabilities		Assets	Liabilities
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Derivatives held for trading						
- Foreign currency related contracts .....	194,475	429	460	36,051	60	276
- Interest rate swaps.....	990,750	—	38,843	1,019,568	—	112,746
- Currency swaps .....	—	—	—	55,840	—	1,524
		<u>429</u>	<u>39,303</u>		<u>60</u>	<u>114,546</u>

The replacement costs and credit risk-weighted amounts of derivative exposures are as follows:

THE GROUP AND THE BANK						
	2008			2007		
	Notional amount	Replacement cost	Credit risk-weighted amount	Notional amount	Replacement cost	Credit risk-weighted amount
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Exchange rate contracts.....	194,475	429	876	91,891	60	626
Interest rate contracts.....	990,750	—	730	1,019,568	—	1,529
		<u>429</u>	<u>1,606</u>		<u>60</u>	<u>2,155</u>

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

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

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

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

## 19. INVESTMENTS IN SECURITIES

	THE GROUP					THE BANK				
	Financial assets at fair value through profit or loss					Financial assets at fair value through profit or loss				
	Held for trading	Designated at fair value	Available-for-sale securities	Held-to-maturity securities	Total	Held for trading	Designated at fair value	Available-for-sale securities	Held-to-maturity securities	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
2008										
Equity securities:										
Listed in Hong Kong.....	113	—	76,976	—	77,089	—	—	35,142	—	35,142
Listed overseas.....	—	—	4,191	—	4,191	—	—	4,191	—	4,191
	113	—	81,167	—	81,280	—	—	39,333	—	39,333
Unlisted .....	—	—	62,965	—	62,965	—	—	58,997	—	58,997
	113	—	144,132	—	144,245	—	—	98,330	—	98,330
Debt securities:										
Certificates of deposit .....	—	—	—	558,720	558,720	—	—	—	558,720	558,720
Structured products .....	—	680,567	—	—	680,567	—	680,567	—	—	680,567
Other debt securities -										
Unlisted .....	—	—	52,395	9,168,965	9,221,360	—	—	52,395	9,168,965	9,221,360
	—	680,567	52,395	9,727,685	10,460,647	—	680,567	52,395	9,727,685	10,460,647
Total:										
Listed in Hong Kong.....	113	—	76,976	—	77,089	—	—	35,142	—	35,142
Listed overseas.....	—	—	4,191	—	4,191	—	—	4,191	—	4,191
Unlisted .....	—	680,567	115,360	9,727,685	10,523,612	—	680,567	111,392	9,727,685	10,519,644
	113	680,567	196,527	9,727,685	10,604,892	—	680,567	150,725	9,727,685	10,558,977
Market value of listed securities:										
Listed in Hong Kong.....	113	—	76,976	—	77,089	—	—	35,142	—	35,142
Listed overseas.....	—	—	4,191	—	4,191	—	—	4,191	—	4,191
	113	—	81,167	—	81,280	—	—	39,333	—	39,333
As analysed by issuing entities:										
Central government and central banks.....	—	—	—	289,181	289,181	—	—	—	289,181	289,181
Public sector entities.....	—	—	—	67,547	67,547	—	—	—	67,547	67,547
Bank and other financial institutions.....	—	275,085	42,615	8,033,861	8,351,561	—	275,085	35,755	8,033,861	8,344,701
Corporate entities.....	113	405,482	119,439	1,337,096	1,862,130	—	405,482	84,465	1,337,096	1,827,043
Others .....	—	—	34,473	—	34,473	—	—	30,505	—	30,505
	113	680,567	196,527	9,727,685	10,604,892	—	680,567	150,725	9,727,685	10,558,977

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

- In 2008 and 2007, structured products which contain embedded derivatives such as options and credit default swaps that would otherwise have been separately accounted for; and
- In 2007, bond funds (classified as “other debt securities” below) are designated at fair value through profit or loss because they are managed and evaluated on a fair value basis, in accordance with investment strategy. Information about the bond funds is provided internally on that basis to the Group’s key management personnel.



Included in available-for-sale securities are financial instruments issued by structured investment vehicles with gross investment cost of approximately HK\$116,219,000 (2007: HK\$568,212,000). Impairment losses of HK\$99,579,000 (2007: HK\$369,627,000) has been recognised for these investments. All other available-for-sale securities and investments in securities are neither past due nor impaired.

Certain held-to-maturity certificates of deposit of approximately HK\$15,500,000 (2007: HK\$25,170,000) held by the San Francisco Branch of the Bank have been pledged to the State of California of the United States of America in compliance with the requirements of the California Financial Code.

	THE GROUP					THE BANK				
	Financial assets at fair value through profit or loss					Financial assets at fair value through profit or loss				
	Held for trading	Designated at fair value	Available-for-sale securities	Held-to-maturity securities	Total	Held for trading	Designated at fair value	Available-for-sale securities	Held-to-maturity securities	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
2007										
Equity securities:										
Listed in Hong Kong.....	264	—	220,255	—	220,519	—	—	70,390	—	70,390
Listed overseas.....	—	—	8,614	—	8,614	—	—	8,614	—	8,614
	264	—	228,869	—	229,133	—	—	79,004	—	79,004
Unlisted .....	—	—	408,750	—	408,750	—	—	406,141	—	406,141
	264	—	637,619	—	637,883	—	—	485,145	—	485,145
Debt securities:										
Certificates of deposit .....	—	—	—	1,484,139	1,484,139	—	—	—	1,484,139	1,484,139
Structured products .....	—	939,082	—	—	939,082	—	939,082	—	—	939,082
Other debt securities -										
Unlisted .....	—	195,076	239,042	14,123,841	14,557,959	—	195,076	239,042	14,123,841	14,557,959
	—	1,134,158	239,042	15,607,980	16,981,180	—	1,134,158	239,042	15,607,980	16,981,180
Total:										
Listed in Hong Kong.....	264	—	220,255	—	220,519	—	—	70,390	—	70,390
Listed overseas.....	—	—	8,614	—	8,614	—	—	8,614	—	8,614
Unlisted .....	—	1,134,158	647,792	15,607,980	17,389,930	—	1,134,158	645,183	15,607,980	17,387,321
	264	1,134,158	876,661	15,607,980	17,619,063	—	1,134,158	724,187	15,607,980	17,466,325
Market value of listed securities:										
Listed in Hong Kong.....	264	—	220,255	—	220,519	—	—	70,390	—	70,390
Listed overseas.....	—	—	8,614	—	8,614	—	—	8,614	—	8,614
	264	—	228,869	—	229,133	—	—	79,004	—	79,004
As analysed by issuing entities:										
Central government and central banks.....	—	118,393	—	534,442	652,835	—	118,393	—	534,442	652,835
Public sector entities .....	—	—	—	11,245	11,245	—	—	—	11,245	11,245
Bank and other financial institutions .....	56	475,282	272,315	15,060,293	15,807,946	—	475,282	210,326	15,060,293	15,745,901
Corporate entities .....	208	535,484	198,204	2,000	735,896	—	535,484	107,719	2,000	645,203
Others .....	—	4,999	406,142	—	411,141	—	4,999	406,142	—	411,141
	264	1,134,158	876,661	15,607,980	17,619,063	—	1,134,158	724,187	15,607,980	17,466,325

## 20. ADVANCES AND OTHER ACCOUNTS

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Advances to customers				
Bills receivable.....	334,215	509,729	334,215	509,729
Trade bills .....	165,293	164,557	165,293	164,557
Other advances to customers.....	32,745,119	31,047,597	32,744,705	31,047,068
	33,244,627	31,721,883	33,244,213	31,721,354
Interest receivable.....	138,721	286,187	138,452	285,803
Impairment allowances				
- Individually assessed.....	(5,799)	(17,876)	(5,799)	(17,876)
- Collectively assessed.....	(108,988)	(116,720)	(108,984)	(116,714)
	33,268,561	31,873,474	33,267,882	31,872,567
Advances to banks and other financial institutions.....	116,412	57,084	116,412	57,084
	33,384,973	31,930,558	33,384,294	31,929,651
Other accounts .....	249,869	565,332	93,039	163,789
	<u>33,634,842</u>	<u>32,495,890</u>	<u>33,477,333</u>	<u>32,093,440</u>

Included in the “Advances to banks and other financial institutions” of the Group and the Bank is an amount of approximately HK\$116,412,000 (2007: HK\$57,084,000) placed as reserve funds with the financial institutions in the People’s Republic of China by the Shantou Branch of the Bank in compliance with the requirements of Regulations Governing Foreign Financial Institutions of the People’s Republic of China.

Included in the “other accounts” of the Group and the Bank is retirement benefits scheme assets of HK\$52,000 (2007: HK\$21,914,000) due to the excess of scheme assets over defined benefit obligations, as disclosed in Note 35.

Impairment allowances on advances:

	THE GROUP			THE BANK		
	Individual assessment	Collective assessment	Total	Individual assessment	Collective assessment	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Balance at 1 January 2008 .....	17,876	116,720	134,596	17,876	116,714	134,590
Increase in impairment allowances.....	144,819	—	144,819	144,819	—	144,819
Amounts reversed .....	(45,795)	(7,690)	(53,485)	(45,795)	(7,688)	(53,483)
Amounts written off.....	(141,853)	—	(141,853)	(141,853)	—	(141,853)
Recoveries of advances written off in previous years .....	35,167	—	35,167	35,167	—	35,167
Unwinding effect of discount rate .....	(4,415)	—	(4,415)	(4,415)	—	(4,415)
Exchange difference.....	—	(42)	(42)	—	(42)	(42)
Balance at 31 December 2008.....	<u>5,799</u>	<u>108,988</u>	<u>114,787</u>	<u>5,799</u>	<u>108,984</u>	<u>114,783</u>

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

Details of the impaired loans are as follows:

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Gross impaired loans .....	100,574	215,820	100,574	215,820
Less: Impairment allowances under individual assessment	<u>(5,799)</u>	<u>(17,876)</u>	<u>(5,799)</u>	<u>(17,876)</u>
Net impaired loans .....	<u>94,775</u>	<u>197,944</u>	<u>94,775</u>	<u>197,944</u>
Gross impaired loans as a percentage of gross advances to customers .....	<u>0.30%</u>	<u>0.68%</u>	<u>0.30%</u>	<u>0.68%</u>
Market value of collateral pledged .....	<u>470,173</u>	<u>519,503</u>	<u>470,173</u>	<u>519,503</u>

## 21. INVESTMENTS IN SUBSIDIARIES

(i)

	2008	2007
	HK\$'000	HK\$'000
Unlisted shares, at cost .....	<u>348,323</u>	<u>333,323</u>

Details of the principal subsidiaries as at 31 December 2008 are as follows:

<b>Name of company</b>	<b>Place of incorporation/ operation</b>	<b>Issued and fully paid ordinary share capital</b>	<b>Percentage of issued share capital directly held</b>	<b>Principal activities</b>
Chong Hing (Nominees) Limited.....	Hong Kong	HK\$100,000	100%	Provision of nominee services
Chong Hing Finance Limited .....	Hong Kong	HK\$25,000,000	100%	Deposit-taking and lending
Chong Hing Information Technology Limited.....	Hong Kong	HK\$100,000	100%	Provision of electronic data processing services
Liu Chong Hing Banking Corporation, Cayman .....	Cayman Islands/ Hong Kong	US\$10,000,000	100%	General merchant banking
Chong Hing Securities Limited .....	Hong Kong	HK\$10,000,000	100%	Stockbroking
Chong Hing Commodities and Futures Limited.....	Hong Kong	HK\$5,000,000	100%	Investment holding and commodities and futures broking
Gallbraith Limited .....	Hong Kong	HK\$16,550,000	100%	Property investment
Card Alliance Company Limited .....	Hong Kong	HK\$18,000,000	100%	Credit card management
Chong Hing Insurance Company Limited ..	Hong Kong	HK\$85,000,000	100%	Insurance underwriting

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

(ii) Amounts due from subsidiaries

	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Amounts due from subsidiaries.....	<u>3,711</u>	<u>3,407</u>

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

## 22. INTERESTS IN JOINTLY CONTROLLED ENTITIES

(i)

	<b>THE GROUP</b>		<b>THE BANK</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Unlisted shares, at cost .....	—	—	21,500	56,500
Share of increases in net assets, net of dividends received	<u>82,999</u>	<u>142,230</u>	<u>—</u>	<u>—</u>
	<u>82,999</u>	<u>142,230</u>	<u>21,500</u>	<u>56,500</u>

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

As at 31 December 2008, the Group had interests in the following jointly controlled entities:

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

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

	2008	2007
	HK\$'000	HK\$'000
Assets .....	624,244	573,233
Liabilities.....	(541,245)	(431,003)
Income .....	61,602	105,521
Expense.....	<u>(151,842)</u>	<u>(39,447)</u>

(ii) Loan to a jointly controlled entity

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Loan to a jointly controlled entity.....	<u>—</u>	<u>5,267</u>	<u>—</u>	<u>5,267</u>

## 23. INVESTMENT PROPERTIES

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.

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 1 January .....	60,241	82,250	35,900	64,250
Addition .....	30,000	—	30,000	—
Net increase in fair value recognised in the income statement .....	39,560	14,391	38,150	8,050
Disposals .....	<u>—</u>	<u>(36,400)</u>	<u>—</u>	<u>(36,400)</u>
At 31 December.....	<u>129,801</u>	<u>60,241</u>	<u>104,050</u>	<u>35,900</u>

Investment properties owned by the Group and by the Bank were revalued at 31 December 2008 on an open market value basis by Vigers Hong Kong Limited, independent professionally qualified valuers. The fair value is mainly arrived at by reference to comparable market transactions for similar properties.

The investment properties are rented out under operating leases.

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

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Leasehold properties				
Held in Hong Kong on long-term lease (over 50 years unexpired) .....	32,550	14,500	32,550	14,500
Held in Hong Kong on medium-term lease (10 - 50 years unexpired) .....	71,500	21,400	71,500	21,400
Held outside Hong Kong on medium-term lease (10 - 50 years unexpired) .....	25,751	24,341	—	—
	<u>129,801</u>	<u>60,241</u>	<u>104,050</u>	<u>35,900</u>

## 24. PROPERTY AND EQUIPMENT

	THE GROUP			THE BANK		
	Buildings	Equipment	Total	Buildings	Equipment	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>COST</b>						
At 1 January 2008 .....	308,345	425,175	733,520	304,545	378,551	683,096
Additions .....	8,538	59,129	67,667	8,538	54,649	63,187
Disposals .....	—	(6,567)	(6,567)	—	(4,538)	(4,538)
Exchange adjustments .....	—	(3)	(3)	—	(3)	(3)
At 31 December 2008 .....	<u>316,883</u>	<u>477,734</u>	<u>794,617</u>	<u>313,083</u>	<u>428,659</u>	<u>741,742</u>
<b>ACCUMULATED DEPRECIATION</b>						
At 1 January 2008 .....	27,641	259,006	286,647	27,634	229,863	257,497
Provided for the year .....	6,563	37,362	43,925	6,466	32,366	38,832
Eliminated on disposals .....	—	(5,676)	(5,676)	—	(3,656)	(3,656)
Exchange adjustments .....	—	(3)	(3)	—	(3)	(3)
At 31 December 2008 .....	<u>34,204</u>	<u>290,689</u>	<u>324,893</u>	<u>34,100</u>	<u>258,570</u>	<u>292,670</u>
<b>CARRYING AMOUNTS</b>						
At 31 December 2008 .....	<u>282,679</u>	<u>187,045</u>	<u>469,724</u>	<u>278,983</u>	<u>170,089</u>	<u>449,072</u>

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

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

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

The carrying amount of buildings shown above comprise:

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Leasehold properties				
Held in Hong Kong on long-term lease (over 50 years unexpired) .....	211,918	212,036	211,918	211,885
Held in Hong Kong on medium-term lease (10-50 years unexpired) .....	63,498	65,450	59,802	61,808
Held outside Hong Kong on medium-term lease (10-50 years unexpired) .....	7,263	3,218	7,263	3,218
	<u>282,679</u>	<u>280,704</u>	<u>278,983</u>	<u>276,911</u>

## 25. PREPAID LEASE PAYMENTS FOR LAND

The Group's prepaid lease payments comprise:

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
COST				
In Hong Kong held on:				
Leases of over 50 years .....	125,212	125,548	649,908	650,932
Leases of between 10 to 50 years .....	198,932	204,592	188,136	193,442
Outside Hong Kong held on:				
Leases of between 10 to 50 years .....	3,983	4,091	3,983	4,091
	<u>328,127</u>	<u>334,231</u>	<u>842,027</u>	<u>848,465</u>
Net book value at 1st January .....	334,231	316,535	848,465	842,475
Additions .....	—	28,171	—	17,071
Amortisation of prepaid operating lease payments .....	(6,104)	(5,710)	(6,438)	(6,316)
Disposals .....	—	(4,765)	—	(4,765)
	<u>328,127</u>	<u>334,231</u>	<u>842,027</u>	<u>848,465</u>
Analysed as:				
Current portion .....	6,104	5,710	6,438	6,316
Non-current portion .....	322,023	328,521	835,589	842,149
Total .....	<u>328,127</u>	<u>334,231</u>	<u>842,027</u>	<u>848,465</u>

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

## 26. DEPOSITS FROM CUSTOMERS

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Demand deposits and current accounts .....	3,004,761	2,992,184	3,004,761	2,992,184
Savings deposits .....	13,835,350	12,584,043	13,835,350	12,584,043
Time, call and notice deposits .....	42,561,549	44,751,210	42,558,316	44,747,371
	<u>59,401,660</u>	<u>60,327,437</u>	<u>59,398,427</u>	<u>60,323,598</u>

Included in the balances is an aggregate amount of approximately HK\$147,110,000 (2007: HK\$174,430,000) representing deposits of companies and their subsidiaries having significant influence on the Group.

## 27. LOAN CAPITAL

	THE GROUP AND THE BANK	
	2008	2007
	HK\$'000	HK\$'000
US\$125 million callable floating rate subordinated notes due 2016 .....	<u>965,454</u>	<u>970,871</u>

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

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



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

## 28. SHARE CAPITAL

	<b>2008 &amp; 2007</b>
	<i>HK\$'000</i>
Authorised:	
600,000,000 shares of HK\$0.50 each .....	<u>300,000</u>
Issued and fully paid:	
435,000,000 shares of HK\$0.50 each .....	<u>217,500</u>

## 29. RESERVES

	Share premium	Investment revaluation reserve	General reserve	Translation reserve	Regulatory reserve	Retained profits	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>THE BANK</b>							
At 1 January 2008.....	1,542,817	50,512	1,378,500	335	356,000	2,557,334	5,885,498
Revaluation losses, net.....	—	(229,067)	—	—	—	—	(229,067)
Exchange differences arising from translation of foreign operations	—	—	—	7,725	—	—	7,725
Deferred taxation arising from revaluation movement ( <i>Note 30</i> )	—	5,043	—	—	—	—	5,043
Net expense recognised directly in equity .....	—	(224,024)	—	7,725	—	—	(216,299)
Profit for the year .....	—	—	—	—	—	91,005	91,005
Reversal of reserves upon impairment.....	—	256,757	—	—	—	—	256,757
Reversal of reserves upon disposal.	—	(86,444)	—	—	—	—	(86,444)
Total recognised income for the year .....	—	(53,711)	—	7,725	—	91,005	45,019
Interim dividend paid .....	—	—	—	—	—	(65,250)	(65,250)
Final dividend paid .....	—	—	—	—	—	(191,400)	(191,400)
Earmark of retained profits as regulatory reserve .....	—	—	—	—	(49,000)	49,000	—
At 31 December 2008.....	<u>1,542,817</u>	<u>(3,199)</u>	<u>1,378,500</u>	<u>8,060</u>	<u>307,000</u>	<u>2,440,689</u>	<u>5,673,867</u>
At 1 January 2007.....	1,542,817	73,491	1,378,500	98	165,000	2,590,750	5,750,656
Revaluation losses, net.....	—	(328,073)	—	—	—	—	(328,073)
Exchange differences arising from translation of foreign operations	—	—	—	237	—	—	237
Deferred taxation arising from revaluation movement ( <i>Note 30</i> )	—	8,423	—	—	—	—	8,423
Net expense recognised directly in equity .....	—	(319,650)	—	237	—	—	(319,413)
Profit for the year .....	—	—	—	—	—	440,334	440,334
Reversal of reserves upon impairment.....	—	369,627	—	—	—	—	369,627
Reversal of reserves upon disposal.	—	(72,956)	—	—	—	—	(72,956)
Total recognised income for the year .....	—	(22,979)	—	237	—	440,334	417,592
Interim dividend paid .....	—	—	—	—	—	(91,350)	(91,350)
Final dividend paid .....	—	—	—	—	—	(191,400)	(191,400)
Earmark of retained profits as regulatory reserve .....	—	—	—	—	191,000	(191,000)	—
At 31 December 2007.....	<u>1,542,817</u>	<u>50,512</u>	<u>1,378,500</u>	<u>335</u>	<u>356,000</u>	<u>2,557,334</u>	<u>5,885,498</u>

The Bank's reserves available for distribution to shareholders as at 31 December 2008 comprised retained profits of HK\$2,440,689,000 (2007: HK\$2,557,334,000) and general reserve of HK\$1,378,500,000 (2007: HK\$1,378,500,000).

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

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

### 30. DEFERRED TAXATION

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

	Accelerated tax depreciation	Collectively assessed impairment allowance	Investment properties	Revaluation of available- for-sale securities	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>THE GROUP</b>					
At 1 January 2008 .....	12,282	(19,726)	6,149	16,569	15,274
Charge to consolidated income statement for the year ( <i>Note 14</i> ) .....	3,363	1,298	6,408	—	11,069
Credit to equity for the year .....	—	—	—	(20,060)	(20,060)
At 31 December 2008 .....	<u>15,645</u>	<u>(18,428)</u>	<u>12,557</u>	<u>(3,491)</u>	<u>6,283</u>
At 1 January 2007 .....	10,403	(17,263)	7,574	27,125	27,839
Charge (credit) to consolidated income statement for the year ( <i>Note 14</i> ) .....	1,879	(2,463)	(1,425)	—	(2,009)
Credit to equity for the year .....	—	—	—	(10,556)	(10,556)
At 31 December 2007 .....	<u>12,282</u>	<u>(19,726)</u>	<u>6,149</u>	<u>16,569</u>	<u>15,274</u>
<b>THE BANK</b>					
At 1 January 2008 .....	9,283	(19,725)	4,188	4,177	(2,077)
Charge to income statement for the year ...	3,511	1,298	6,055	—	10,864
Credit to equity for the year .....	—	—	—	(5,043)	(5,043)
At 31 December 2008 .....	<u>12,794</u>	<u>(18,427)</u>	<u>10,243</u>	<u>(866)</u>	<u>3,744</u>
At 1 January 2007 .....	10,403	(17,260)	7,574	12,600	13,317
Credit to income statement for the year .....	(1,120)	(2,465)	(3,386)	—	(6,971)
Credit to equity for the year .....	—	—	—	(8,423)	(8,423)
At 31 December 2007 .....	<u>9,283</u>	<u>(19,725)</u>	<u>4,188</u>	<u>4,177</u>	<u>(2,077)</u>

### 31. SHARE OPTION SCHEME

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

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

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

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

### 32. LOANS TO OFFICERS

The aggregate relevant loans to officers, included in “advances to customers” in Note 20, and disclosed pursuant to Section 161B of the Companies Ordinance are as follows:

	THE GROUP AND THE BANK	
	2008	2007
	HK\$'000	HK\$'000
Aggregate balance of all relevant loans outstanding at the balance sheet date ....	<u>91,177</u>	<u>85,172</u>
Maximum aggregate balance of relevant loans during the year .....	<u>114,996</u>	<u>172,658</u>

The loans have no fixed repayment terms and the applicable interest rate ranges from 0% to prime rate plus 10%. Included in the loans to officers are loans of HK\$90,053,000 (2007: HK\$83,683,000) with collateral.

### 33. IMPAIRMENT LOSS ON GOODWILL

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

For the year ended 31 December 2008, management has reviewed goodwill for impairment. The review comprised a comparison of the carrying amount and value in use of an acquired subsidiary (the smallest cash-generating unit) to which the goodwill has been allocated. The acquired subsidiary is involved in insurance business.

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

Value in use is derived at by discounting the expected future cash flows at 12% discount rate. Management's financial model assumes a growth in underwriting profit of 8% per annum during the first 5 years. Cash flows beyond five years are extrapolated using a terminal growth rate of 3.5%. A goodwill impairment loss of HK\$20,000,000 (2007: HK\$30,000,000), representing the excess of the carrying amount above the value in use, has been recognised for the year ended 31 December 2008.

### 34. OFF-BALANCE SHEET EXPOSURES

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Contingent liabilities and commitments				
- contractual amounts				
Direct credit substitutes .....	647,442	643,264	647,442	643,264
Trade-related contingencies .....	366,620	595,878	366,620	595,878
Forward asset purchases .....	13,548	32,926	13,548	32,926
Other commitments:				
Which are unconditionally cancellable without prior notice .....	4,703,352	5,761,482	4,703,352	5,761,482
With an original maturity of one year and under .....	8,105,056	8,632,587	8,105,056	8,632,587
With an original maturity of over one year .....	1,721,251	2,212,847	1,721,251	2,212,847
Lease commitments .....	<u>73,506</u>	<u>65,264</u>	<u>70,398</u>	<u>62,588</u>
	<u>15,630,775</u>	<u>17,944,248</u>	<u>15,627,667</u>	<u>17,941,572</u>

Most of the contingent liabilities and commitments are denominated in Hong Kong dollars.

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

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Within one year .....	28,532	28,150	26,941	26,288
In the second to fifth years inclusive .....	36,874	36,839	35,413	36,025
Over five years .....	1,043	275	1,043	275
	<u>66,449</u>	<u>65,264</u>	<u>63,397</u>	<u>62,588</u>

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

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

	THE GROUP		THE BANK	
	2008	2007	2008	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Capital expenditure contracted for but not provided in the consolidated financial statements in respect of property and equipment .....	<u>13,548</u>	<u>32,926</u>	<u>13,548</u>	<u>32,926</u>

The credit risk-weighted amount of contingent liabilities and commitments is HK\$2,990,733,000 (2007: HK\$3,321,625,000).

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

	THE GROUP AND THE BANK	
	2008	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>
Within one year.....	1,148	2
In the second to fifth years inclusive .....	<u>38</u>	<u>—</u>
	<u>1,186</u>	<u>2</u>

### 35. RETIREMENT BENEFITS SCHEME

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

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

The most recent actuarial valuation of the ORSO (Defined benefit) Scheme was carried out as at 31 December 2008 by the qualified actuaries of Watson Wyatt Hong Kong Limited. The accrued liabilities and future costs were measured using the Projected Unit Credit method.

At the date of the latest formal independent actuarial valuation made on 31 December 2008, the market value of the ORSO (Defined benefit) Scheme was HK\$52,000.

Net benefit income:

	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Current service cost .....	(94)	(84)
Interest cost on benefit obligation .....	(838)	(1,014)
Expected return on plan assets .....	2,292	1,956
Actuarial (loss) gain recognised in the year.....	<u>(23,222)</u>	<u>9,343</u>
Net benefit (cost) income .....	<u>(21,862)</u>	<u>10,201</u>

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

	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Present value of defined benefit obligation.....	(25,450)	(25,121)
Fair value of plan assets .....	<u>25,502</u>	<u>47,035</u>
Retirement benefit asset .....	<u>52</u>	<u>21,914</u>

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

	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Opening defined benefit obligation.....	25,121	28,742
Interest cost .....	94	84
Current service cost .....	838	1,014
Actuarial gains on obligations .....	(2,456)	(2,211)
Benefits forfeited (paid) .....	<u>1,853</u>	<u>(2,508)</u>
Closing defined benefit obligation.....	<u>25,450</u>	<u>25,121</u>

Changes in fair value of plan assets are as follows:

	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Opening fair value of plan assets .....	47,035	40,455
Expected return .....	2,292	1,956
Actuarial (losses) gains on plan assets .....	(21,369)	7,132
Benefits paid .....	<u>(2,456)</u>	<u>(2,508)</u>
Closing fair value of plan assets .....	<u>25,502</u>	<u>47,035</u>

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

	<b>2008</b>	<b>2007</b>
	%	%
Cash.....	47	29
Equities.....	53	71

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

The actual return on plan assets for 2008 was HK\$19,077,000 (2007: HK\$9,088,000).

The amounts of assets of the Scheme invested in the Bank's own financial instruments as at 31 December 2008 were:

	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Deposits with the Bank .....	11,756	13,270

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

	<b>2008</b>	<b>2007</b>
	%	%
Discount rate.....	2.8	3.5
Expected rate of return on plan assets.....	5.0	5.0
Expected rate of salary increase.....	3.0	3.0

### 36. RELATED PARTY TRANSACTIONS

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

	<b>Interest, commission and rental income</b>		<b>Interest and rental expenses</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Investing enterprises having significant influence on the Bank and their subsidiaries .....	7,030	11,033	26,567	16,769
Jointly controlled entities.....	18,788	13,480	6,624	12,901
Directors and their associates.....	24,046	20,100	14,202	26,638

The above transactions were carried out at market rates.

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

	<b>Amounts due from related parties</b>		<b>Amounts due to related parties</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Investing enterprises having significant influence on the Bank and subsidiaries .....	—	—	147,110	174,430
Jointly controlled entities.....	59,743	5,267	148,992	277,015
Directors and their associates.....	1,695,469	991,440	621,189	603,806

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

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

	<b>Interest, commission and rental income</b>		<b>Interest and rental expenses</b>		<b>Computer service expense</b>		<b>Dividend income</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Subsidiaries.....	<u>7,802</u>	<u>8,852</u>	<u>18,222</u>	<u>21,314</u>	<u>26,676</u>	<u>27,700</u>	<u>48,000</u>	<u>230,000</u>

The above transactions were carried out at market rates.

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

	<b>Amounts due from</b>		<b>Amounts due to</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Subsidiaries .....	<u>3,711</u>	<u>3,407</u>	<u>704,828</u>	<u>658,146</u>

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

#### Compensation of key management personnel

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

	<b>THE GROUP AND THE BANK</b>	
	<b>2008</b>	<b>2007</b>
	<i>HK\$'000</i>	<i>HK\$'000</i>
Short-term benefits.....	<u>54,769</u>	<u>49,787</u>
Post employment benefits.....	<u>3,996</u>	<u>3,324</u>
	<u>58,765</u>	<u>53,111</u>

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

#### 37. CONTINGENT LIABILITY

From time to time as part of its product offerings to customers, the Bank sells and distributes third party investment products, including the minibond series related to Lehman Brothers (the "Minibonds"). Owing to the continuing developments relating to the Minibonds incident and some of such developments are not wholly within the control of the Bank, it is difficult to assess at this stage whether potential outcomes will have any significant adverse impact on the Bank.



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