

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Investments in securities

Investments in securities are recognised on a trade date basis and are initially measured at cost.

At subsequent reporting dates, debt securities that the Group has the expressed intention and ability to hold to maturity (held-to-maturity securities) are measured at amortised cost, less any impairment loss recognised to reflect irrecoverable amounts. The annual amortisation of any discount or premium on the acquisition of a held-to-maturity security is aggregated with other investment income receivable over the term of the instrument so that the revenue recognised in each period represents a constant yield on the investment.

All securities other than held-to-maturity debt securities are measured at subsequent reporting dates at fair value.

Where securities are held for trading purposes, unrealised gains and losses are included in net profit or loss for the year. For other securities, unrealised gains and losses are dealt with in equity, until the security is disposed of or is determined to be impaired, at which time the cumulative gain or loss is included in net profit or loss for the year.

Taxation

The charge for taxation is based on the results for the year as adjusted for items which are non-assessable or disallowed. Timing differences arise from the recognition for tax purposes of certain items of income and expense in a different accounting period from that in which they are recognised in the financial statements. The tax effect of timing differences, computed using the liability method, is recognised as deferred taxation in the financial statements to the extent that it is probable that a liability or an asset will crystallise in the foreseeable future.

Operating leases

Rental costs under operating leases are charged to the income statement on a straight line basis over the lease term.

Financial derivative products

Financial derivative products, which include forward contracts, interest rate swaps and similar derivative products, are recognised on a trade date basis and are initially measured at cost. Financial derivative products outstanding at the year end, except for those designated as hedges, are valued at fair value, with unrealised gains and losses included in the income statement. Gains and losses related to those derivative products that are designated as hedges are dealt with in accordance with the accounting treatment applicable to the position hedged and there is no offsetting of assets and liabilities until the position is closed. To qualify as a hedge, the derivative must effectively reduce the price or interest rate risk of the asset, liability or anticipated transaction to which it is linked and be designated as a hedge at inception of the derivative contract. Accordingly, changes in the market value of the derivative must be highly correlated with changes in the market value of the underlying hedged item at inception of the hedge and over the life of the hedge contract. The financial derivative products of the Group are mainly used for hedging purposes.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Fiduciary assets

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

Retirement benefit costs

Payments to the Mandatory Provident Fund Scheme are charged as expenses as they fall due.

For defined benefit retirement benefit schemes, the cost of providing benefits is determined using the projected unit credit method, with actuarial valuations being carried out every three years. Actuarial gains and losses which exceed 10% 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 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.

4. BUSINESS AND GEOGRAPHICAL SEGMENTS

(a) Business segments

For management purposes, the Group is currently organised into two operating divisions - corporate and retail banking and treasury and foreign exchange activities. 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, chequing facilities, mandatory provident fund services, the provision of fixed deposits and savings accounts, credit card, insurance and personal wealth management services. The Group also provides fully automated telephone and internet banking services to its customers. Other financial services offered include remittance and money exchange, safe deposit boxes, auto pay 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.

Other business activities of the Group include investment holding, securities trading, stockbroking, commodities and future broking, other investment advisory services and property investment.

4. BUSINESS AND GEOGRAPHICAL SEGMENTS - continued

(a) Business segments - continued

- (i) Segment information about these businesses for the year ended 31 December 2002 is presented below:

INCOME STATEMENT

	Corporate and retail banking HK\$'000	Treasury and foreign exchange activities HK\$'000	Other business activities HK\$'000	Eliminations HK\$'000	Consolidated HK\$'000
Interest income from external customers	813,627	435,033	–	–	1,248,660
Interest expense to external customers	(487,766)	(11,523)	–	–	(499,289)
Inter-segment income	181,254	–	–	(181,254)	–
Inter-segment expense	–	(181,254)	–	181,254	–
Net income	507,115	242,256	–	–	749,371
Other operating income	95,547	21,721	83,578	–	200,846
Operating income	602,662	263,977	83,578	–	950,217
Inter-segment pricing is charged at prevailing customer deposits interest rates.					
Charge for bad and doubtful debts	(129,027)	–	–	–	(129,027)
Net (losses) gains from disposal of property and equipment	(246)	–	15	–	(231)
Operating expenses	(247,902)	(16,764)	(28,097)	–	(292,763)
Result					
Segment profit	225,487	247,213	55,496	–	528,196
Unallocated corporate expenses					(146,498)
Profit from operations					381,698
Share of results of jointly controlled entities					(9,510)
Profit from ordinary activities before taxation					372,188
Taxation					(62,694)
Net profit for the year					309,494