Annual disclosure statements 2014

NCB 南洋商業銀行

Consolidated Income Statement

For the year ended 31 December	2014	2013
	HK$'000	HK$'000
Interest income	**10,037,240**	8,776,796
Interest expense	**(4,847,191)**	(4,085,630)
Net interest income	**5,190,049**	4,691,166
Fee and commission income	**1,332,965**	1,075,126
Fee and commission expense	**(78,239)**	(66,501)
Net fee and commission income	**1,254,726**	1,008,625
Net trading gain	**8,858**	97,221
Net loss on financial instruments designated at fair value through profit or loss	**(7,958)**	(16,193)
Net gain on other financial assets	**122,530**	52,496
Other operating income	**70,808**	75,470
Net operating income before impairment allowances	**6,639,013**	5,908,785
Net charge of impairment allowances	**(904,294)**	(369,967)
Net operating income	**5,734,719**	5,538,818
Operating expenses	**(2,497,589)**	(2,352,498)
Operating profit	**3,237,130**	3,186,320
Net gain from fair value adjustments on investment properties	**129,896**	169,414
Net (loss)/gain from disposal/revaluation of properties, plant and equipment	**(347)**	3,476
Profit before taxation	**3,366,679**	3,359,210
Taxation	**(615,180)**	(530,553)
Profit for the year	**2,751,499**	2,828,657
Dividends	**700,000**	539,000

Consolidated Statement of Comprehensive Income

For the year ended 31 December	2014	2013
	HK$'000	HK$'000
Profit for the year	**2,751,499**	2,828,657
Items that will not be reclassified subsequently to income statement:		
Premises:		
Revaluation of premises	**495,305**	794,564
Deferred tax	**(70,286)**	(119,553)
	425,019	675,011
Items that may be reclassified subsequently to income statement:		
Available-for-sale securities:		
Change in fair value of available-for-sale securities	**557,098**	(624,520)
Release upon disposal of available-for-sale securities reclassified to income statement	**(93,642)**	(31,292)
Amortisation with respect to available-for-sale securities transferred to held-to-maturity securities reclassified to income statement	**1,062**	-
Deferred tax	**(95,845)**	117,817
	368,673	(537,995)
Change in fair value of hedging instruments under net investment hedges	**38,400**	(41,055)
Currency translation difference	**(288,736)**	301,150
	118,337	(277,900)
Other comprehensive income for the year, net of tax	**543,356**	397,111
Total comprehensive income for the year	**3,294,855**	3,225,768

Statement of Comprehensive Income

For the year ended 31 December	2014	2013
	HK$'000	HK$'000
Profit for the year	**2,609,558**	2,410,506
Items that will not be reclassified subsequently to income statement:		
Premises:		
Revaluation of premises	**461,405**	775,889
Deferred tax	**(61,945)**	(114,777)
	399,460	661,112
Items that may be reclassified subsequently to income statement:		
Available-for-sale securities:		
Change in fair value of available-for-sale securities	**342,209**	(494,573)
Release upon disposal of available-for-sale securities reclassified to income statement	**(93,642)**	(22,303)
Amortisation with respect to available-for-sale securities transferred to held-to-maturity securities reclassified to income statement	**1,062**	-
Deferred tax	**(42,123)**	83,082
	207,506	(433,794)
Currency translation difference	**(535)**	405
	206,971	(433,389)
Other comprehensive income for the year, net of tax	**606,431**	227,723
Total comprehensive income for the year	**3,215,989**	2,638,229

Consolidated Balance Sheet

As at 31 December	2014	2013
	HK$'000	HK$'000
ASSETS		
Cash and balances with banks and other financial institutions	**58,282,800**	44,739,319
Placements with banks and other financial institutions maturing between one and twelve months	**18,180,762**	21,344,000
Financial assets at fair value through profit or loss	**6,155,213**	4,164,693
Derivative financial instruments	**439,072**	508,453
Advances and other accounts	**163,903,699**	155,316,751
Investment in securities	**47,168,324**	42,272,143
Investment properties	**1,280,271**	1,174,938
Properties, plant and equipment	**7,328,497**	6,969,237
Deferred tax assets	**152,171**	152,831
Other assets	**1,013,444**	3,741,595
Total assets	**303,904,253**	280,383,960
LIABILITIES		
Deposits and balances from banks and other financial institutions	**37,735,611**	28,846,029
Financial liabilities at fair value through profit or loss	**4,970,693**	4,433,736
Derivative financial instruments	**278,506**	343,156
Deposits from customers	**209,633,935**	198,160,417
Other accounts and provisions	**15,181,966**	15,229,501
Current tax liabilities	**222,225**	205,587
Deferred tax liabilities	**986,473**	865,545
Total liabilities	**269,009,409**	248,083,971
EQUITY		
Share capital	**3,144,517**	700,000
Reserves	**31,750,327**	31,599,989
Total equity	**34,894,844**	32,299,989
Total liabilities and equity	**303,904,253**	280,383,960

Balance Sheet

As at 31 December	2014	2013
	HK$'000	HK$'000
ASSETS		
Cash and balances with banks and other financial institutions	**30,391,541**	18,840,334
Placements with banks and other financial institutions maturing between one and twelve months	**145,422**	1,858,262
Financial assets at fair value through profit or loss	**6,155,213**	4,164,693
Derivative financial instruments	**402,764**	410,434
Advances and other accounts	**106,365,558**	98,373,617
Investment in securities	**37,162,481**	36,401,978
Investment in subsidiaries	**8,171,067**	8,171,067
Investment properties	**1,258,121**	1,126,510
Properties, plant and equipment	**6,579,145**	6,191,967
Other assets	**782,548**	3,532,439
Total assets	**197,413,860**	179,071,301
LIABILITIES		
Deposits and balances from banks and other financial institutions	**10,369,369**	7,488,291
Financial liabilities at fair value through profit or loss	**4,970,693**	4,433,736
Derivative financial instruments	**167,394**	248,314
Deposits from customers	**145,870,627**	131,724,586
Other accounts and provisions	**2,425,678**	4,222,445
Current tax liabilities	**182,031**	162,987
Deferred tax liabilities	**977,874**	856,737
Total liabilities	**164,963,666**	149,137,096
EQUITY		
Share capital	**3,144,517**	700,000
Reserves	**29,305,677**	29,234,205
Total equity	**32,450,194**	29,934,205
Total liabilities and equity	**197,413,860**	179,071,301

Consolidated Statement of Changes in Equity

	Share capital	Share premium	Capital reserve	Premises revaluation reserve	Reserve for fair value changes of available-for-sale securities	Regulatory reserve*	Translation reserve	Retained earnings	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
At 1 January 2013	700,000	2,444,517	605	4,837,228	373,164	1,547,011	707,977	19,002,719	29,613,221
Profit for the year	-	-	-	-	-	-	-	2,828,657	2,828,657
Other comprehensive income:									
Premises	-	-	-	675,011	-	-	-	-	675,011
Available-for-sale securities	-	-	-	-	(537,995)	-	-	-	(537,995)
Change in fair value of hedging instruments under net investment hedges	-	-	-	-	-	-	(41,055)	-	(41,055)
Currency translation difference	-	-	-	3,500	(57)	-	297,707	-	301,150
Total comprehensive income	-	-	-	678,511	(538,052)	-	256,652	2,828,657	3,225,768
Transfer from retained earnings	-	-	-	-	-	397,969	-	(397,969)	-
Dividends	-	-	-	-	-	-	-	(539,000)	(539,000)
At 31 December 2013	700,000	2,444,517	605	5,515,739	(164,888)	1,944,980	964,629	20,894,407	32,299,989

	Share capital	**Share premium**	**Capital reserve**	**Premises revaluation reserve**	**Reserve for fair value changes of available-for-sale securities**	**Regulatory reserve***	**Translation reserve**	**Retained earnings**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
At 1 January 2014	**700,000**	**2,444,517**	**605**	**5,515,739**	**(164,888)**	**1,944,980**	**964,629**	**20,894,407**	**32,299,989**
Profit for the year	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**2,751,499**	**2,751,499**
Other comprehensive income:									
Premises	**-**	**-**	**-**	**425,019**	**-**	**-**	**-**	**-**	**425,019**
Available-for-sale securities	**-**	**-**	**-**	**-**	**368,673**	**-**	**-**	**-**	**368,673**
Change in fair value of hedging instruments under net investment hedges	**-**	**-**	**-**	**-**	**-**	**-**	**38,400**	**-**	**38,400**
Currency translation difference	**-**	**-**	**-**	**(3,649)**	**3,123**	**-**	**(288,210)**	**-**	**(288,736)**
Total comprehensive income	**-**	**-**	**-**	**421,370**	**371,796**	**-**	**(249,810)**	**2,751,499**	**3,294,855**
Transfer to share capital	**2,444,517**	**(2,444,517)**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Transfer from retained earnings	**-**	**-**	**-**	**-**	**-**	**228,610**	**-**	**(228,610)**	**-**
Dividends	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(700,000)**	**(700,000)**
At 31 December 2014	**3,144,517**	**-**	**605**	**5,937,109**	**206,908**	**2,173,590**	**714,819**	**22,717,296**	**34,894,844**

* In accordance with the requirements of the HKMA, the amounts are set aside for general banking risks, including future losses or other unforeseeable risks, in addition to the loan impairment allowances recognised under HKAS 39.

Statement of Changes in Equity

	Share capital	Share premium	Premises revaluation reserve	Reserve for fair value changes of available-for-sale securities	Regulatory reserve*	Translation reserve	Retained earnings	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
At 1 January 2013	700,000	2,444,517	4,665,171	375,089	491,984	(5,532)	19,163,747	27,834,976
Profit for the year	-	-	-	-	-	-	2,410,506	2,410,506
Other comprehensive income:								
Premises	-	-	661,112	-	-	-	-	661,112
Available-for-sale securities	-	-	-	(433,794)	-	-	-	(433,794)
Currency translation difference	-	-	-	-	-	405	-	405
Total comprehensive income	-	-	661,112	(433,794)	-	405	2,410,506	2,638,229
Transfer from retained earnings	-	-	-	-	98,905	-	(98,905)	-
Dividends	-	-	-	-	-	-	(539,000)	(539,000)
At 31 December 2013	700,000	2,444,517	5,326,283	(58,705)	590,889	(5,127)	20,936,348	29,934,205

	Share capital	**Share premium**	**Premises revaluation reserve**	**Reserve for fair value changes of available-for-sale securities**	**Regulatory reserve***	**Translation reserve**	**Retained earnings**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
At 1 January 2014	**700,000**	**2,444,517**	**5,326,283**	**(58,705)**	**590,889**	**(5,127)**	**20,936,348**	**29,934,205**
Profit for the year	**-**	**-**	**-**	**-**	**-**	**-**	**2,609,558**	**2,609,558**
Other comprehensive income:								
Premises	**-**	**-**	**399,460**	**-**	**-**	**-**	**-**	**399,460**
Available-for-sale securities	**-**	**-**	**-**	**207,506**	**-**	**-**	**-**	**207,506**
Currency translation difference	**-**	**-**	**-**	**276**	**-**	**(811)**	**-**	**(535)**
Total comprehensive income	**-**	**-**	**399,460**	**207,782**	**-**	**(811)**	**2,609,558**	**3,215,989**
Transfer to share capital	**2,444,517**	**(2,444,517)**	**-**	**-**	**-**	**-**	**-**	**-**
Transfer from retained earnings	**-**	**-**	**-**	**-**	**172,276**	**-**	**(172,276)**	**-**
Dividends	**-**	**-**	**-**	**-**	**-**	**-**	**(700,000)**	**(700,000)**
At 31 December 2014	**3,144,517**	**-**	**5,725,743**	**149,077**	**763,165**	**(5,938)**	**22,673,630**	**32,450,194**

* In accordance with the requirements of the HKMA, the amounts are set aside for general banking risks, including future losses or other unforeseeable risks, in addition to the loan impairment allowances recognised under HKAS 39.

Consolidated Cash Flow Statement

For the year ended 31 December	2014	2013
	HK$'000	HK$'000
Cash flows from operating activities		
Operating cash inflow before taxation	**15,674,762**	5,927,086
Hong Kong profits tax paid	**(458,285)**	(354,140)
Overseas profits tax paid	**(189,366)**	(118,751)
Net cash inflow from operating activities	**15,027,111**	5,454,195
Cash flows from investing activities		
Purchase of properties, plant and equipment	**(84,996)**	(109,955)
Purchase of investment properties	**(821)**	-
Proceeds from disposal of properties, plant and equipment	**248**	720
Net cash outflow from investing activities	**(85,569)**	(109,235)
Cash flows from financing activities		
Dividends paid	**(700,000)**	(539,000)
Net cash outflow from financing activities	**(700,000)**	(539,000)
Increase in cash and cash equivalents	**14,241,542**	4,805,960
Cash and cash equivalents at 1 January	**39,008,565**	33,701,213
Effect of exchange rate changes on cash and cash equivalents	**(949,036)**	501,392
Cash and cash equivalents at 31 December	**52,301,071**	39,008,565

Notes to the Financial statements

1. Summary of significant accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below.

These policies have been consistently applied to all the years presented, unless otherwise stated.

1.1 Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with Hong Kong Financial Reporting Standards (HKFRSs is a collective term which includes all applicable individual Hong Kong Financial Reporting Standards, HKASs and Interpretations) issued by the HKICPA and the requirements of the Hong Kong Companies Ordinance which for this financial year and the comparative period continue to be those of the predecessor Hong Kong Companies Ordinance (Chapter 32), in accordance with transitional and saving arrangements for Part 9 of the newly enacted Hong Kong Companies Ordinance (Chapter 622).

The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale securities, financial assets and financial liabilities (including derivative financial instruments) at fair value through profit or loss, precious metals at fair value, investment properties which are carried at fair value and premises which are carried at fair value or revalued amount less accumulated depreciation and accumulated impairment losses.

The preparation of financial statements in conformity with HKFRSs requires the use of certain critical accounting estimates. It also requires the Management to exercise judgement in the process of applying the Group's accounting policies.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.1 Basis of preparation (continued)

(a) Amendments and interpretation that are already mandatorily effective for accounting periods beginning on 1 January 2014

Amendments/ Interpretation	Content	Applicable for financial years beginning on	Currently relevant to the Group
HKAS 32 (Amendment)	Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities	1 January 2014	Yes
HKAS 36 (Amendment)	Impairment of Assets: Recoverable Amount Disclosures for Non-Financial Assets	1 January 2014	Yes
HKAS 39 (Amendment)	Financial Instruments: Recognition and Measurement – Novation of Derivatives and Continuation of Hedge Accounting	1 January 2014	Yes
HKFRS 10, 12 and HKAS 27 (Amendments)	Investment Entities	1 January 2014	No
HK(IFRIC) – Int 21	Levies	1 January 2014	Yes

• HKAS 32 (Amendment), "Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities". The amendment addresses inconsistencies in current practice when applying the offsetting criteria and clarifies the meaning of "currently has a legally enforceable right of set-off" including the circumstances of default event or insolvency for any one of all the parties; and the application of offsetting criteria to some gross settlement systems (such as central clearing house systems) that may be considered equivalent to net settlement. The adoption of this amendment does not have a material impact on the Group's financial statements.

• HKAS 36 (Amendment), "Impairment of Assets: Recoverable Amount Disclosures for Non-Financial Assets". The amendment aligns the disclosure requirements with its original intention which does not intend to disclose at level of cash generating unit if it is not impaired. It also requires additional disclosure about the fair value measurement when the recoverable amount of impaired assets is based on fair value less costs of disposal. The adoption of this amendment does not affect the disclosure of the Group's financial statements.

• HKAS 39 (Amendment), "Financial Instruments: Recognition and Measurement – Novation of Derivatives and Continuation of Hedge Accounting". The amendment introduces a relief to allow hedge accounting to continue in a situation where a derivative, which has been designated as a hedging instrument, is novated to effect clearing with a central counterparty as a result of laws or regulation. The adoption of this amendment does not have a material impact on the Group's financial statements.

• HK(IFRIC) – Int 21, "Levies". The interpretation addresses how an entity should account for liabilities to pay levies imposed by governments, other than income taxes, in its financial statements. For a levy that is triggered upon reaching a minimum threshold, no liability should be anticipated before the specified minimum threshold is reached. The adoption of this interpretation does not have a material impact on the Group's financial statements.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.1 Basis of preparation (continued)

(b) Standards and amendments issued that are not yet mandatorily effective and have not been early adopted by the Group in 2014

The following standards and amendments have been issued and are mandatory for accounting periods beginning on or after 1 July 2014:

Standards/ Amendments	Content	Applicable for financial years beginning on/after	Currently relevant to the Group
HKAS 16 and HKAS 41 (Amendments)	Agriculture: Bearer Plants	1 January 2016	No
HKAS 16 and HKAS 38 (Amendments)	Clarification of Acceptable Methods of Depreciation and Amortisation	1 January 2016	No
HKAS 19 (2011) (Amendment)	Employee Benefits: Defined Benefit Plans	1 July 2014	No
HKAS 27 (2011) (Amendment)	Equity Method in Separate Financial statements	1 January 2016	Yes
HKAS 28 (2011) and HKFRS 10 (Amendment)	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture	1 January 2016	No
HKFRS 9 (2014)	Financial Instruments	1 January 2018	Yes
HKFRS 11 (Amendment)	Joint Arrangements: Accounting for Acquisitions of Interests in Joint Operations	1 January 2016	No
HKFRS 14	Regulatory Deferral Accounts	1 January 2016	No
HKFRS 15	Revenue from Contracts with Customers	1 January 2017	Yes

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.1 Basis of preparation (continued)

(b) Standards and amendments issued that are not yet mandatorily effective and have not been early adopted by the Group in 2014 (continued)

•HKAS 27 (2011) (Amendment), "Equity Method in Separate Financial statements". The amendment restores the option to allow an entity to apply the equity method to account for its investments in subsidiaries, joint ventures and associates in its separate financial statements. Early application is permitted. Entities electing to change to the equity method in its separate financial statements will have to apply that change retrospectively. This amendment will not have any impact on the Group's financial statements.

•HKFRS 9 (2014), "Financial Instruments". The issuance of IFRS 9 (2014) Financial Instruments completes the International Accounting Standards Board's comprehensive response to the financial crisis. HKFRS 9 (2014), the equivalent standard of IFRS 9 (2014) under HKFRS, includes a logical model for classification and measurement, a single, forward-looking "expected loss" impairment model and a tighter linkage of risk management to hedge accounting. The changes introduced in HKFRS 9 are highlighted as follows:

(i) Classification and Measurement

Financial assets

Financial assets are required to be classified into one of the following measurement categories: (1) measured subsequently at amortised cost, (2) measured subsequently at fair value through other comprehensive income (all fair value changes other than interest accrual, amortisation and impairment will be recognised in other comprehensive income) or (3) measured subsequently at fair value through profit or loss. Classification is to be made on transition, and subsequently on initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instruments.

A financial instrument is subsequently measured at amortised cost only if it is a debt instrument, and the objective of the entity's business model is to hold the asset to collect the contractual cash flows, and the asset's contractual cash flows characteristics represent only unleveraged payments of principal and interest. A debt instrument is subsequently measured at fair value through other comprehensive income if it is held in a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and the instrument fulfils the contractual cash flows characteristics. All other debt instruments are to be measured at fair value through profit or loss.

Equity instruments are generally measured subsequently at fair value with limited circumstances that cost may be an appropriate estimate of fair value. Equity instruments that are held for trading will be measured at fair value through profit or loss. For all other equity investments, an irrevocable election can be made at initial recognition to recognise unrealised and realised fair value gains and losses in other comprehensive income without subsequent reclassification of fair value gains and losses to the income statement even upon disposal. Dividend income is recognised in the income statement when the right to receive payment is established.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.1 Basis of preparation (continued)

(b) Standards and amendments issued that are not yet mandatorily effective and have not been early adopted by the Group in 2014 (continued)

(i) Classification and Measurement (continued)

Financial Liabilities

Except for the two substantial changes described below, the classification and measurement requirements of financial liabilities have been basically carried forward with minimal amendments from HKAS 39.

The fair value option for financial liabilities were changed to address own credit risk. The amount of change in fair value attributable to changes in the credit risk of the financial liabilities will be presented in other comprehensive income. The remaining amount of the total gain or loss is included in the income statement. If this creates or enlarges an accounting mismatch in profit or loss, then the whole fair value change is presented in the income statement. The determination of whether there will be a mismatch will need to be made at initial recognition of individual liabilities and will not be re-assessed. Amounts presented in other comprehensive income are not subsequently reclassified to the income statement but may be transferred within equity. This removes the volatility in profit or loss that was caused by changes in the credit risk of liabilities elected to be measured at fair value. It also means that gains caused by the deterioration of an entity's own credit risk on such liabilities will no longer be recognised in profit or loss.

The standard also eliminates the exception from fair value measurement contained in HKAS 39 for derivative financial instruments that are linked to and must be settled by delivery of an unquoted equity instrument.

(ii) Impairment

The standard introduces a new, expected-loss impairment model that will require more timely recognition of expected credit losses. Specifically, it requires entities to account for 12 months expected credit losses from inception when financial instruments are first recognised and to recognise full lifetime expected credit losses on a more timely basis when there have been significant increases in credit risk since initial recognition. The impairment for financial instruments that are subsequently measured at amortised cost, fair value through other comprehensive income (debt instruments), loan commitments and financial guarantees will be governed by this standard.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.1 Basis of preparation (continued)

(b) Standards and amendments issued that are not yet mandatorily effective and have not been early adopted by the Group in 2014 (continued)

(iii) Hedge accounting

The requirements related to hedge accounting would better align the accounting treatments with risk management activities and enable entities to better reflect these activities in their financial statements. It relaxes the requirements for assessing hedge effectiveness which more risk management strategies may be eligible for hedge accounting. It also relaxes the rules on using non-derivative financial instruments as hedging instruments and allows greater flexibility on hedged items. Users of the financial statements will be provided with more relevant information about risk management and the effect of hedge accounting on the financial statements.

Early application of HKFRS 9 in its entirety at the same time is permitted. Only the part related to own credit risk can be elected to be early applied in isolation. The Group is considering the financial impact of the standard and the timing of its application.

• HKFRS 15, "Revenue from Contracts with Customers". HKFRS 15 applies a single model and specifies the accounting treatment for all revenue arising from contracts with customers. The new standard is based on the core principle that revenue is recognised to reflect the consideration expected to be entitled when control of promised good or service transfers to customer. It is also applicable to the recognition and measurement of gains or losses on the sale of some non-financial assets such as properties or equipments that are not an output of ordinary activities. HKFRS 15 also includes a set of disclosure requirements about revenue from customer contracts. The new standard will replace the separate models for goods, services and construction contracts stipulated in different standards under the current HKFRS. Early application is permitted. The Group is considering the financial impact of the standard and the timing of its application.

(c) Improvements to HKFRSs

"Improvements to HKFRSs" contains numerous amendments to HKFRSs which the HKICPA considers not urgent but necessary. It comprises amendments that result in accounting changes for presentation, recognition or measurement purpose as well as terminology or editorial amendments related to a variety of individual HKFRSs. The amendments are either effective and adopted for annual periods beginning on or after 1 July 2014 or will be effective on or after 1 January 2016. The adoption of these improvements does not have a material impact on the Group's financial statements.

In addition, the requirements of Part 9 "Accounts and Audit" of the newly enacted Hong Kong Companies Ordinance (Chapter 622) will be applied from the Company's first financial year commencing after 3 March 2014 in accordance with section 358 of that Ordinance, which will be the year ending 31 December 2015. The Group is still assessing the expected impact of the changes in the period of initial application. So far assessed, the impact is unlikely to be significant and will primarily affect the presentation and disclosure of information in the consolidated financial statements.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.2 Consolidation

The consolidated financial statements include the financial statements of the Bank and all of its subsidiaries made up to 31 December.

Subsidiaries

Subsidiaries are entities controlled by the Group. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated; unrealised losses are also eliminated unless the transaction provides evidence of impairment of the assets transferred. Where necessary, accounting policies of subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

In the Bank's balance sheet, the investments in subsidiaries are stated at cost less allowance for impairment losses. The results of subsidiaries are accounted for by the Bank on the basis of dividends received and receivable. Dividend income from subsidiaries is recognised in the income statement when the right to receive payment is established.

1.3 Segmental reporting

The operating result of segments are reported in a manner consistent with the internal reporting provided to the Management, which is the chief operating decision maker of the Group, that allocates resources and assesses the performance of operating segments. Income and expenses directly associated with each segment are included in determining operating segment performance.

1.4 Foreign currency translation

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in Hong Kong dollars, which is the Bank's functional and presentation currency.

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or exchange rates at the end of the reporting period for items that are re-measured. Foreign exchange gains and losses resulting from the settlement of foreign currency transactions using the exchange rates prevailing at the dates of the transactions and monetary assets and liabilities denominated in foreign currencies translated at the exchange rate at the end of the reporting period are recognised directly in the income statement, except when deferred in other comprehensive income as qualifying net investment hedges.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.4 Foreign currency translation (continued)

Translation differences on monetary securities held at fair value through profit or loss are reported as part of the fair value gain or loss. Changes in the fair value of monetary securities denominated in foreign currency classified as available-for-sale are analysed between translation differences resulting from changes in the amortised cost of the securities and other changes in the carrying amount of the securities. Translation differences related to changes in the amortised cost are recognised in the income statement, and other changes in the carrying amount are recognised in other comprehensive income.

Translation differences on non-monetary items are reported as part of the fair value gain or loss. Translation differences on non-monetary financial assets such as equities classified as available-for-sale are included in other comprehensive income.

The results and financial position of all the Group entities that have a functional currency different from Hong Kong dollars are translated into Hong Kong dollars as follows:

- assets and liabilities are translated at the closing rate at the end of the reporting period;
- income and expenses are translated at average exchange rates; and
- all resulting exchange differences are recognised in the currency translation reserve in equity through other comprehensive income.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments are taken to other comprehensive income. When a foreign entity is sold, such exchange differences are recognised in the income statement, as part of the gain or loss on sale.

1.5 Derivative financial instruments

Derivatives are initially recognised at fair value on the date the derivative contract is entered into and are subsequently re-measured at fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and through the use of valuation techniques, including discounted cash flow models and option pricing models, as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

Certain derivatives embedded in other financial instruments are treated as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract and the host contract is not carried at fair value through profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognised in the income statement.

Derivatives are categorised as held for trading and changes in their fair value are recognised immediately in the income statement.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.6 Hedge Accounting

The Group documents at inception the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at the hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values of hedged items. These criteria should be met before a hedge can be qualified to be accounted for under hedge accounting.

Net investment hedge

A gain or loss on the effective portion of the hedging instrument is recognised in other comprehensive income and accumulated in equity; a gain or loss on the ineffective portion is recognised immediately in the income statement. Accumulated gains and losses previously recognised in other comprehensive income are reclassified to the income statement upon disposal of the foreign operation as part of the gain or loss on disposal.

1.7 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.

1.8 Interest income and expense and fee and commission income and expense

Interest income and expense are recognised in the income statement for all financial assets and financial liabilities using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. 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, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates future cash flows considering all contractual terms of the financial instrument (e.g. prepayment options or incentives relating to residential mortgage loans) but does not consider future credit losses. The calculation includes fees, premiums or discounts and basis points paid or received between parties to the contract, and directly attributable origination fees and costs which represent an integral part of the effective yield.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised on the written down value using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. Subsequent unwinding of the discount allowance is recognised as interest income.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.8 Interest income and expense and fee and commission income and expense (continued)

Fee and commission income and expenses that are not an integral part of the effective yield are recognised on an accrual basis ratably over the period when the related service is provided, such as administrative fee, asset management fee and custody services fee. Loan syndication fees are recognised as revenue when the related syndication arrangement has been completed and the Group has retained no part of the loan package for itself or has retained a part at the same effective interest rate as that of other participants.

1.9 Financial assets

The Group classifies its financial assets into the following four categories: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity securities and available-for-sale financial assets. The Management determines the classification of investments at initial recognition. The classification depends on the purpose for which the financial assets are held. All financial assets are recognised initially at fair value. Except for financial assets carried at fair value through profit or loss, all transaction costs of financial assets are included in their initial carrying amounts.

(1) Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception.

A financial asset which has been acquired or incurred principally for the purpose of selling in the short term or is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking is classified as held for trading. Derivatives are also classified as held for trading.

A financial asset, other than one held for trading, will be designated as a financial asset at fair value through profit or loss, if it meets one of the criteria set out below, and is so designated by the Management:

• eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as "an accounting mismatch") that would otherwise arise from measuring the financial assets or recognising the gains and losses on them on different bases; or

• applies to a group of financial assets, financial liabilities or both that is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the group is provided internally on that basis to the Management; or

• relates to financial assets containing one or more embedded derivative that significantly modifies the cash flow resulting from those financial assets.

These assets are recognised initially at fair value, with transaction costs taken directly to the income statement, and are subsequently re-measured at fair value.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.9 Financial assets (continued)

(1) Financial assets at fair value through profit or loss (continued)

Gains and losses from changes in the fair value of such assets (excluding the interest component) are reported in net trading gain/loss or net gain/loss on financial instruments designated at fair value through profit or loss. The interest component is reported as part of interest income.

(2) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, including placements with and advances to banks and other financial institutions, investment debt securities without an active market and loans and advances to customers. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method less allowances for impairment losses.

(3) Held-to-maturity

Financial assets classified as held-to-maturity are those traded in active markets, with fixed or determinable payments and fixed maturities that the Group's Management has both the positive intention and the ability to hold to maturity. Where the Group sold held-to-maturity assets (i) other than due to an isolated event beyond the Group's control, non-recurring and could not have been reasonably anticipated by the Group, such as a significant deterioration in the issuer's creditworthiness, significant change in statutory or regulatory requirement or (ii) other than an insignificant amount of held-to-maturity assets, the entire category would be tainted and reclassified as available-for-sale. They are initially recorded at fair value plus any directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest method less allowances for impairment losses.

(4) Available-for-sale

Financial assets classified as available-for-sale are those that are either designated as such or are not classified in any of the other categories. They are intended to be held for an indefinite period of time but may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

Available-for-sale financial assets are initially recorded at fair value plus any directly attributable transaction costs, and are subsequently measured at fair value. Unrealised gains and losses arising from changes in the fair value of investments are recognised directly in other comprehensive income, until the financial asset is derecognised or impaired at which time the accumulated gain or loss previously recognised in equity should be transferred to the income statement. However, interest income which includes the amortisation of premium and discount is calculated using the effective interest method and is recognised in the income statement. Dividends on equity instruments classified as available-for-sale are recognised in other operating income when the Group's right to receive payment is established.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.9 Financial assets (continued)

(4) Available-for-sale (continued)

For a financial asset reclassified from the available-for-sale category, the fair value carrying amount at the date of reclassification becomes its new amortised cost and any previous gain or loss on that asset that has been recognised in other comprehensive income is amortised to profit or loss over the remaining life of the investment using the effective interest method. Any difference between the new amortised cost and the maturity amount is also amortised over the remaining life of the financial asset using the effective interest method. If the financial asset is subsequently determined to be impaired, the amount recorded in other comprehensive income is reclassified to profit or loss immediately.

The treatment of translation differences on available-for-sale securities is dealt with in Note 1.4.

1.10 Financial liabilities

The Group classifies its financial liabilities under the following categories: trading liabilities, deposits and other liabilities. All financial liabilities are classified at inception and recognised initially at fair value.

(1) Trading liabilities

A financial liability is classified as held for trading if it is incurred principally for the purpose of repurchasing in the short term. Derivatives are also classified as held for trading. It is measured at fair value and any gains and losses from changes in fair value are recognised in the income statement.

(2) Deposits and other liabilities

Deposits and other liabilities, other than those classified as trading liabilities are carried at amortised cost. Any difference (if available) between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period using the effective interest method.

1.11 Financial guarantee contracts

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a contract between the holder and the debtor.

Financial guarantee contracts are initially recognised as financial liabilities and reported under “Other accounts and provisions” in the financial statements at fair value on the date the guarantee was given. Subsequent to initial recognition, the Group’s liabilities under such guarantees are measured 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, where appropriate, accumulated amortisation recognised over the life of the guarantee on a straight-line basis. Any changes in the liability relating to financial guarantee contracts are taken to the income statement.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.12 Recognition and derecognition of financial instruments

Purchases and sales of financial assets at fair value through profit or loss, available-for-sale and held-to-maturity securities are recognised on the trade date, the date on which the Group purchases or sells the assets. Loans and receivables (except investment securities without an active market) are recognised when cash is advanced to the borrowers. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership. When the Group neither transfers nor retains substantially all the risks and rewards of ownership of the financial asset, the Group either continues to recognise the transferred financial asset to the extent of its continuing involvement if control remains or derecognise it if there is no retained control.

Trading liabilities are recognised on the trade date. Deposits that are not trading liabilities are recognised when money is received from customers, other liabilities are recognised when such obligations arise. Financial liabilities are derecognised from the balance sheet when and only when the obligation specified in the contract is discharged, cancelled or expires.

Securities and bills sold to a counterparty with an obligation to repurchase at a pre-determined price on a specified future date under a repurchase agreement are referred to as repos. Securities and bills purchased from a counterparty with an obligation to re-sell to the counterparty at a pre-determined price on a specified future date under a resale agreement are referred to as reverse repos.

Repos or securities lending are initially recorded as due to banks, placements from banks and other financial institutions, as appropriate, at the actual amount of cash received from the counterparty. Financial assets given as collateral for repurchase agreements are not derecognised and are recorded as investment in securities or financial assets at fair value through profit or loss. Reverse repos or securities borrowing are initially recorded in the balance sheet as cash and due from banks or placements with banks and other financial institutions, as appropriate, at the actual amount of cash paid to the counterparty. Financial assets received as collateral under reverse repurchase agreements are not recognised on the balance sheet. The difference between sale and repurchase price is recognised as interest income or interest expense over the life of the agreements using the effective interest method.

1.13 Fair value measurement

The Group measures its premises and investment properties, precious metals and certain financial instruments at fair value at the end of each reporting period. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants in its principal market or the most advantageous market accessible by the Group at the measurement date.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.13 Fair value measurement (continued)

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

If the market for assets or liabilities is not active, the Group uses valuation techniques, including the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants, that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

1.14 Precious metals

Precious metals comprise gold. Precious metals are initially recognised and subsequently re-measured at fair value. Mark-to-market gains or losses on precious metals are included in net trading gain/loss.

1.15 Impairment of financial assets

The Group assesses as at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a "loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. Objective evidence that a financial asset or group of financial assets may be impaired includes observable data that comes to the attention of the Group about the following probable loss events:

(i) significant financial difficulty of the issuer or obligor;

(ii) a breach of contract, such as a default or delinquency in interest or principal payment;

(iii) the Group granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a concession that the lender would not otherwise consider;

(iv) it becoming probable that the borrower will enter into bankruptcy or other financial reorganisation;

(v) the disappearance of an active market or downgrading below investment grade level for that financial asset because of financial difficulties; or

(vi) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:

• adverse changes in the payment status of borrowers in the group; or

• national or local economic conditions that correlate with defaults on the assets in the group.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.15 Impairment of financial assets (continued)

(1) Assets carried at amortised cost

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment together with all other financial assets that are not individually significant or for which impairment has not yet been identified. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity securities has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred), discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a loan or held-to-maturity security has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Group may measure impairment on the basis of an instrument's fair value using an observable market price.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral.

For the purposes of a collective assessment of impairment, financial assets are grouped on the basis of similar and relevant credit risk characteristics. Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the group and historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

When a loan is uncollectible, it is written off against the related allowance for impairment losses. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of impairment losses in the income statement.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.15 Impairment of financial assets (continued)

(1) Assets carried at amortised cost (continued)

If, in a subsequent period, the amount of allowance for impairment losses decreases and the decrease can be related objectively to an event occurring after the impairment loss was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss to the extent of its decrease is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

Loans whose terms have been renegotiated with substantial difference in the terms are no longer considered to be past due but are treated as new loans.

(2) Assets classified as available-for-sale

If evidence of impairment exists for available-for-sale financial assets, the accumulated losses, measured as the difference between the acquisition cost or amortised cost and the current fair value, less any impairment loss on that financial asset previously recognised in the income statement, is removed from equity and recognised in the income statement. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss to the extent of its decrease is reversed through the income statement. With respect to equity instruments, further fair value changes are recognised in the reserve for fair value change of available-for-sale securities through other comprehensive income, impairment losses are not reversed through the income statement.

1.16 Impairment of investment in subsidiaries and non-financial assets

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Potential indications of impairment may include significant adverse changes in the technological, market, economic or legal environment in which the assets operate or whether there has been a significant or prolonged decline in value below their cost.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units). Assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

In the Bank's financial statements, impairment testing of the investment in a subsidiary is also required upon receiving dividend from that entity if the dividend exceeds the total comprehensive income of that entity concerned in the period the dividend is declared or if the carrying amount of that entity in the Bank's balance sheet exceeds the carrying amount of that entity's net assets including goodwill in its consolidated balance sheet.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.17 Investment properties

Properties that are held for long-term rental yields or for capital appreciation or both, and that are not occupied by the companies in the Group, are classified as investment properties. Properties leased out within Group companies are classified as investment properties in individual companies' financial statements and as premises in consolidated financial statements. Land held under operating lease is classified and accounted for as investment property when the rest of the definition of investment property is met. The operating lease is accounted for as if it is a finance lease.

Investment properties are recognised initially at cost, including related transaction costs. After initial recognition, investment properties are measured at fair value.

Subsequent expenditure is charged to the asset's carrying amount only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The item is stated at cost less impairment and is included in the carrying amount of investment properties. Once the item begins to generate economic benefits, it is then measured at fair value. All other repairs and maintenance costs are expensed in the income statement during the financial period in which they are incurred.

Any changes in fair value are recognised directly in the income statement.

If an investment property becomes owner-occupied, it is reclassified as premises, and its fair value at the date of reclassification becomes its cost for accounting purposes. If an item of premises becomes an investment property because its use has changed, any difference resulting between the carrying amount and the fair value of this item at the date of transfer is recognised in other comprehensive income as a revaluation of premises under HKAS 16 "Property, Plant and Equipment". However, if a fair value gain reverses a previous revaluation loss or impairment loss, the gain is recognised in the income statement up to the amount previously debited.

1.18 Properties, plant and equipment

Properties are mainly branches and office premises. Premises are shown at fair value based on periodic, at least annual, valuations by external independent valuers less subsequent accumulated depreciation. Any accumulated depreciation at the date of revaluation is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. In the intervening periods, the directors review the carrying amount of premises, by reference to the open market value of similar properties, and adjustments are made when there has been a material change.

All plant and equipment are stated at historical cost less accumulated depreciation. Historical cost includes expenditures that are directly attributable to the acquisition and installation of the items.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.18 Properties, plant and equipment (continued)

Subsequent costs are included in an asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The item is stated at cost until it begins to generate economic benefits, then the item is subsequently measured according to the measurement basis of its respective assets class. All other repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred.

Increases in the carrying amount arising on revaluation of premises are credited to the premises revaluation reserve through other comprehensive income. Decreases that offset previous increases of the same individual asset are charged against premises revaluation reserve through other comprehensive income; all other decreases are expensed in the income statement. Any subsequent increases are credited to the income statement up to the amount previously debited, and then to the premises revaluation reserve. Upon disposal of premises, the relevant portion of the premises revaluation reserve realised in respect of previous valuations is released and transferred from the premises revaluation reserve to retained earnings.

Depreciation is calculated on the straight-line method to write down the cost or revalued amount of such assets over their estimated useful lives as follows:

• Properties	Over the life of government land leases
• Plant and equipment	2 to 15 years

The useful lives of assets are reviewed, and adjusted if appropriate, as at the end of each reporting period.

At the end of each reporting period, both internal and external sources of information are considered to determine whether there is any indication that properties, plant and equipment, are impaired. If any such indication exists, the recoverable amount of the asset is estimated and where relevant, an impairment loss is recognised to reduce the asset to its recoverable amount. Such an impairment loss is recognised in the income statement except where the asset is carried at valuation and the impairment loss does not exceed the revaluation surplus for that same asset, in which case it is treated as a revaluation decrease. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use. Impairment loss is reversed through the premises revaluation reserve or the income statement as appropriate.

Gains and losses on disposals are determined by comparing proceeds with carrying amount, relevant taxes and expenses. These are recognised in the income statement.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.19 Leases

(1) Operating leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. The total payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place. Rental income from operating leases is recognised on a straight-line basis over the lease term.

(2) Finance leases

Leases of assets where lessee have obtained substantially all the risks and rewards of ownership are classified as finance leases. Government land leases in Hong Kong are classified as finance leases as the present value of the minimum lease payments (i.e. transaction price) of the land amounted to substantially all of the fair value of the land as if it were freehold.

Finance leases are capitalised at the lease's commencement at the lower of the fair value of the leased asset and the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included in other liabilities. Investment properties acquired under finance leases are carried at their fair value.

When assets are leased out under a finance lease, the present value of the lease payments is recognised as a receivable. Lease income is recognised over the term of the lease using net investment method, which reflects a constant periodic rate of return.

1.20 Cash and cash equivalents

For the purposes of the consolidated cash flow statement, cash and cash equivalents comprise balances with original maturity less than three months from the date of acquisition, including cash, balances with banks and other financial institutions, short-term bills and notes classified as investment securities.

1.21 Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.22 Employee benefits

(1) Retirement benefit costs

The Group contributes to defined contribution retirement schemes under either recognised ORSO schemes or MPF schemes that are available to the Group's employees. Contributions to the schemes by the Group and employees are calculated as a percentage of employees' basic salaries for the ORSO schemes and in accordance with the MPF rules for MPF schemes. The retirement benefit scheme costs are charged to the income statement as incurred and represent contributions payable by the Group to the schemes. Contributions made by the Group that are forfeited by those employees who leave the ORSO scheme prior to the full vesting of their entitlement to the contributions are used by the Group to reduce the existing level of contributions or to meet its expenses under the trust deed of the ORSO schemes.

The assets of the schemes are held in independently-administered funds separate from those of the Group.

(2) Leave entitlements

Employee entitlements to annual leave and sick leave are recognised when they accrue to employees. A provision is made for the estimated liability for unused annual leave and the amount of sick leave expected to be paid as a result of services rendered by employees up to the end of the reporting period.

Compensated absences other than sick leave and special approved annual leaves are non-accumulating; they lapse if the current period's entitlement is not used in full. Except for unexpired annual leaves, they do not entitle employees to a cash payment for unused entitlement on leaving the Group.

(3) Bonus plans

The expected cost of bonus payments are recognised as a liability when the Group has a present legal or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made. Liabilities for bonus plans that are expected to be settled longer than twelve months will be discounted if the amounts are significant.

1.23 Current and deferred income taxes

Tax expenses for the period comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised directly in other comprehensive income. In this case, the tax is also recognised in other comprehensive income.

Income tax payable on profits, based on the applicable tax law enacted or substantially enacted at the end of the reporting period in each jurisdiction where the Bank and the subsidiaries operate and generate taxable income, is recognised as a current income tax expense in the period in which profits arise.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.23 Current and deferred income taxes (continued)

Deferred income tax is provided in full, using the balance sheet liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates and laws that have been enacted or substantially enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

The principal temporary differences arise from asset impairment provisions, depreciation of premises and equipment, revaluation of certain assets including available-for-sale securities and premises, and tax losses carried forward. However, the deferred income tax is not recognised if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss.

Deferred income tax liabilities are provided in full on all taxable temporary differences and deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is charged or credited in the income statement except for deferred income tax relating to fair value re-measurement of available-for-sale securities and revaluation of premises which are charged or credited to other comprehensive income, in which case the deferred income tax is also credited or charged to other comprehensive income and is subsequently recognised in the income statement together with the realisation of the deferred gain and loss.

Deferred tax liability or deferred tax asset arising from investment property is determined based on the presumption that the revaluation amount of such investment property will be recovered through sale with the relevant tax rate applied.

1.24 Repossessed assets

Repossessed assets are initially recognised at the lower of their fair value less costs to sell and the amortised cost of the related outstanding loans on the date of repossession, and the related loans and advances together with the related impairment allowances are derecognised from the balance sheet. Subsequently, repossessed assets are measured at the lower of their cost and fair values less costs to sell and are reported as "non-current assets held for sale" included in "Other assets".

1.25 Fiduciary activities

The Group commonly acts as a trustee, or in other fiduciary capacities, that result in its holding or managing assets on behalf of individuals, trusts and other institutions. These assets and any gains or losses arising thereon are excluded from these financial statements, as they are not assets of the Group.

Notes to the Financial statements (continued)

1. Summary of significant accounting policies (continued)

1.26 Contingent liabilities and contingent assets

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that an outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised as a provision but is disclosed in the notes to the financial statements. When a change in the probability of an outflow occurs so that outflow is probable, it will then be recognised as a provision.

A contingent asset is a possible asset that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain events not wholly within the control of the Group.

Contingent assets are not recognised but are disclosed in the notes to the financial statements when an inflow of economic benefits is probable. When the inflow is virtually certain, it will be recognised as an asset.

1.27 Related parties

For the purposes of these financial statements, a party is considered to be related to the Group if (i) that party controls, jointly controls or has significant influence over the Group; (ii) is a member of the same financial reporting group, such as parents, subsidiaries and fellow subsidiaries; (iii) is an associate or a joint venture of the Group or parent reporting group; (iv) is a key management personnel of the Group or parents; (v) the party is subject to common control with the Group; and (vi) an entity in which a person identified in (iv) controls. Related parties may be individuals or entities.

Notes to the Financial statements (continued)

2. Financial risk management

The Group is exposed to financial risks as a result of engaging in a variety of business activities. The principal financial risks are credit risk, market risk (including currency risk and interest rate risk) and liquidity risk. This note summarises the Group's exposures to these risks, as well as its objectives, risk management governance structure, policies and processes for managing and the methods used to measure these risks.

Financial risk management framework

The Group's risk management governance structure is designed to cover all business processes and ensures various risks are properly managed and controlled in the course of conducting business. The Group has a robust risk management organisational structure with a comprehensive set of policies and procedures to identify, measure, monitor and control various risks that may arise. These risk management policies and procedures are regularly reviewed and updated to reflect changes in markets and business strategies. Various groups of risk takers assume their respective responsibilities for risk management.

The Board of Directors, representing the interests of shareholders, is the highest decision-making authority of the Group and has the ultimate responsibility for risk management. The Board, with the assistance of its committees, has the primary responsibility for the formulation of risk management strategies and for ensuring that the Group has an effective risk management system to implement these strategies.

The Risk Management Committee, a standing committee established by the Board of Directors, is responsible for overseeing the Group's various types of risks, approving high-level risk-related policies and monitoring their implementation, approving significant or high risk exposures or transactions. The Risk Management Committee would refer any specific transaction to the Board if it is deemed so significant that Board approval is desirable. The Audit Committee assists the Board in fulfilling its role in overseeing the internal control system.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

Financial risk management framework (continued)

Various units of the Group have their respective risk management responsibilities. Business units act as the first line of defence while risk management units, which are independent from the business units, are responsible for the day-to-day management of different kinds of risks. Risk management units have the primary responsibilities for drafting, reviewing and updating various risk management policies and procedures.

The Group has put in place appropriate internal control systems, including establishment of an organisation structure that sets clear lines of authority and responsibility for monitoring compliance with policies, procedures and limits. Proper reporting lines also provide sufficient independence of the control functions from the business areas, as well as adequate segregation of duties throughout the organisation which helps promote an appropriate internal control environment.

Pursuant to a risk-based approach, the Audit Department conducts independent reviews on areas including principal risks, regulatory compliance, adequacy and effectiveness of risk policies and internal control systems.

Product development and risk monitoring

To ensure the effectiveness of risk assessment and monitoring, the Group has a comprehensive product development and risk monitoring system where roles and responsibilities of all related units are clearly defined and proper due diligence processes on product development are in place.

In accordance with the strategic objectives set by the Board and the Management, the respective product management units are responsible for formulating business and product development plans, and proceeding to specific product development activities. The division of strategic development shall ensure the plans are aligned with the Group's overall strategies. Divisions that are responsible for risk management, legal, compliance and finance etc. are accountable for risk assessment and review.

Apart from product development, the respective product management units shall work closely with relevant risk evaluating divisions to identify and assess the risks of new products. Risk evaluating divisions shall conduct independent review on the risk assessment results and the corresponding risk management measures. Products can only be launched upon completion of the product due diligence process to the satisfaction of all risk evaluating divisions.

A prudent approach is adopted in offering treasury products to our clients. All new treasury products require approval from the Management or the special committee before launching.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk

Credit risk is the risk of loss that a customer or counterparty is unable to or unwilling to meet its contractual obligations. Credit risk exists in the trading book and banking book, as well as from on- and off-balance sheet transactions of the Group. It arises principally from lending, trade finance and treasury businesses.

Credit risk management framework

The Group has formulated a comprehensive set of credit risk management policies and procedures, and appropriate credit risk limits to manage and control credit risk that may arise. These policies, procedures and credit risk limits are regularly reviewed and updated to cope with changes in market conditions and business strategies.

The Group's organisation structure establishes a clear set of authority and responsibility for monitoring compliance with policies, procedures and limits.

The Credit and Loans Management Committee, a management committee authorised by the Chief Executive, is responsible for the implementation of the credit risk management strategies as well as the approval of credit policies. It also monitors various aspects of the Group's loan portfolio such as asset quality, risk concentration. Various units of the Group have their respective credit risk management responsibilities. Business units act as the first line of defence. They are obliged to make thorough assessment on every credit application and are fully responsible for monitoring credit performance and punctual repayments. The business activities conducted should also comply with the credit policies and procedures. The risk management units, which are independent from the business units, are responsible for the day-to-day management of credit risks and have the primary responsibilities for providing an independent due diligence through identifying, measuring, monitoring and controlling credit risk, as well as drafting, reviewing and updating credit risk management policies and procedures. They report directly to the Credit and Loans Management Committee, Chief Executive and Risk Management Committee. NCB (China) sets up independent risk monitoring teams to monitor credit risk, and submits management information and reports to the Bank on a regular basis.

The Board of Directors is the ultimate source of credit authority. The Board of Directors delegates credit approval authority to the Chief Executive. Based on management needs, the Chief Executive can further delegate to the subordinates within the limits authorised by the Board of Directors. The Group sets the limits of credit approval authority according to business nature, internal rating, level of transaction risk and extent of the credit exposure.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

Credit risk measurement and control

In view of the rapidly changing market conditions, the Group has been continuously revisiting its credit strategies and conducting rigorous reviews on the concerned portfolios.

Advances

Different credit approval and control procedures are adopted according to level of risk associated with the customer, counterparty or transaction. All credit applications are subject to thorough risk assessment and proper approval. In general, most of the credit applications will be reviewed and assessed by independent officer(s) of risk management unit(s) before approval, with exceptions given to certain designated products which satisfy certain conditions. These designated advances will be (randomly) reviewed by designated unit(s) which is(are) independent from the front line business units after funding being drawn. Obligor ratings (in terms of probability of default) and facility ratings (in terms of loss given default) are assigned to credit applications for non-retail exposures to support credit approval. Retail internal rating systems are deployed in the risk assessment of retail credit transactions, including small business retail exposures, residential mortgage loans and personal loans. Loan grades, obligor and facility ratings as well as loss estimates (if applicable) are used to support credit approval.

The Group also uses loan grades, obligor ratings and loss estimates (if applicable) to support credit monitoring, reporting and analysis of credit risk information. For non-retail exposures, more frequent rating review and closer monitoring are required for higher-risk customers. For retail exposures, monthly updated internal ratings and loss estimates are used for credit monitoring on a portfolio basis. More comprehensive review is required for obligors being identified under high-risk pools.

The Group employs an internal master rating scale that can be mapped to Standard & Poor's external credit ratings. The structure of internal master rating scale is in compliance with the requirement of the Banking (Capital) Rules under the Hong Kong Banking Ordinance.

Regular credit management information reports and ad hoc reports are provided to the Management, Risk Management Committee and Board of Directors to facilitate their continuous monitoring of credit risk.

In addition, the Group identifies credit concentration risk by industry, geography, customer and counterparty. The Group monitors changes to counterparties credit risk, quality of the credit portfolio and risk concentrations, and reports regularly to the Group's management.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

Credit risk measurement and control (continued)

Advances (continued)

In the year of 2014, the Group continues to adopt loan grading criteria which divide credit assets into 5 categories with reference to HKMA's guidelines, as below:

"Pass" represents loans where the borrower is current in meeting its repayment obligations and full repayment of interest and principal is not in doubt.

"Special Mention" represents loans where the borrower is experiencing difficulties which may threaten the Group's position. Ultimate loss is not expected at this stage but could occur if adverse conditions persist.

"Substandard" represents loans where the borrower displays a definable weakness that is likely to jeopardise repayment.

"Doubtful" represents loans where collection in full is improbable and the Group expects to sustain a loss of principal and/or interest, taking into account the net realisable value of the collateral.

"Loss" represents loans which are considered uncollectible after all collection options (such as the realisation of collateral or the institution of legal proceedings) have been exhausted.

Debt securities and derivatives

For investments in debt securities and securitisation assets, the obligor ratings or external credit ratings, assessment of the underlying assets and credit limits setting on customer/security issuer basis are used for managing credit risk associated with the investment. For derivatives, the Group sets customer limits to manage the credit risk involved and follows the same approval and control processes as applied for advances. On-going monitoring and stop-loss procedures are established.

Settlement risk arises mainly from foreign exchange transactions with counterparties and also from derivatives transactions in any situation where a payment in cash, securities or equities is made in the expectation of a corresponding receipt in cash, securities or equities. Daily settlement limits are established for each counterparty or customer to cover all settlement risks arising from the Group's market transactions on any single day.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

Collateral held as security and other credit enhancements

The valuation and management of collateral have been documented in the credit risk management policies and procedures which cover acceptance criteria, validity of collateral, loan-to-value ratio, haircut ratio, valuation and insurance, etc. The collateral is revalued on a regular basis, though the frequency and the method used varies with the type of collateral involved and the nature and the risk of the underlying credit. The Group has established a mechanism to update the value of its main type of collateral, real estate properties, with the use of public indices on a portfolio basis. Collateral is insured with the Group as the beneficiary.

For loans guaranteed by a third party, the Group assesses the guarantor's financial condition, credit history and ability to meet obligations.

As at 31 December 2014 the Group did not hold any collateral that it was permitted to sell or re-pledge in the absence of default by the borrower (2013: Nil).

(A) Credit exposures

The maximum credit exposure is the worst case scenario of exposure to the Group without taking into account any collateral held or other credit enhancements. For on-balance sheet assets, the maximum exposure to credit risk equals their carrying amount. For letters of guarantee issued, the maximum exposure to credit risk is the maximum amount that the Group could be required to pay if the guarantees are called upon. For loan commitment and other credit related liabilities, the maximum exposure to credit risk is the full amount of the committed facilities.

The nature of the collateral held and other credit enhancements and their financial effect to the different classes of the Group's financial assets are as follows.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(A) Credit exposures (continued)

Balances and placements with banks and other financial institutions

These exposures are generally considered to be low risk due to the nature of the counterparties. Collateral is generally not sought on these assets.

Financial assets at fair value through profit or loss and investment in securities

Collateral is generally not sought on debt securities.

Derivative financial instruments

The Master Agreement published by the International Swaps and Derivatives Association, Inc. ("ISDA Master Agreement") is the preferred agreement for documenting derivatives activities of the Group. It provides the contractual framework under which dealing activities across a full range of OTC transactions are conducted, and set out close-out netting provisions upon termination following the occurrence of an event of default or a termination event. In addition, if deemed necessary, Credit Support Annex ("CSA") will be included to form part of the Schedule to the ISDA Master Agreement. Under a CSA, collateral is passed from one counterparty to another, as appropriate, to mitigate the exposures.

Advances and other accounts, contingent liabilities and commitments

Advances and other accounts, contingent liabilities and commitments are collateralised to the extent considered appropriate by the Group taking account of the risk assessment of individual exposures. The components and nature of contingent liabilities and commitments are disclosed in Note 4. Regarding the commitments that are unconditionally cancellable without prior notice, the Group would assess the necessity to withdraw the credit line in case where the credit quality of a borrower deteriorates. For contingent liabilities and commitments, 12.62% (2013: 14.94%) is covered by collateral as at 31 December 2014.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts

Gross advances and other accounts before impairment allowances are summarised by product type as follows:

	The Group	
	2014	2013
	HK$'000	HK$'000
Advances to customers		
Personal		
- Mortgages	**21,137,660**	19,071,015
- Credit cards	**1,058,032**	454,882
- Others	**9,260,192**	7,201,697
Corporate		
- Commercial loans	**110,404,053**	108,469,101
- Trade finance	**7,642,319**	8,345,348
	149,502,256	143,542,043
Trade bills	**16,371,563**	13,242,636
Total	**165,873,819**	156,784,679

	The Bank	
	2014	2013
	HK$'000	HK$'000
Advances to customers		
Personal		
- Mortgages	**10,787,904**	10,468,766
- Others	**8,033,358**	6,053,509
Corporate		
- Commercial loans	**74,187,027**	66,166,653
- Trade finance	**6,744,382**	6,902,201
	99,752,671	89,591,129
Trade bills	**7,238,603**	9,458,019
Total	**106,991,274**	99,049,148

Advances with a specific repayment date are classified as overdue when the principal or interest is past due and remains unpaid. Advances repayable by regular instalments are classified as overdue when an instalment payment is past due and remains unpaid. Advances repayable on demand are classified as overdue either when a demand for repayment has been served on the borrower but repayment has not been made in accordance with the instruction or when the advances have remained continuously outside the approved limit that was advised to the borrower.

Advances are impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred and that loss event(s) has an impact on the estimated future cash flows of the advances that can be reliably estimated.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

If there is objective evidence that an impairment loss on advances has been incurred, the amount of loss is measured as the difference between the carrying amount and the present value of estimated future cash flows generated by the advances. Objective evidence that advances are impaired includes observable data that comes to the attention of the Group about the loss events.

The criteria that the Group uses to determine that there is objective evidence of an impairment loss mainly include:

- Significant financial difficulty incurred by the borrower;
- A breach of contract, such as a default or delinquency in principal or interest payment;
- For economic or legal reasons related to the borrower's financial difficulty, the Group has granted to the borrower a concession that it would not otherwise consider;
- Probable that the borrower will become bankrupt or undergo other financial reorganisation; or
- Other observable data indicating that there is a measurable decrease in the estimated future cash flows from such advances.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(a) Advances neither overdue nor impaired

Advances that were neither overdue nor impaired are analysed by internal credit grades as follows:

	The Group			
	2014			
	Pass	Special mention	Substandard or below	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Advances to customers				
Personal				
- Mortgages	**20,837,952**	**19,811**	**1,729**	**20,859,492**
- Credit cards	**988,572**	**-**	**99**	**988,671**
- Others	**9,187,486**	**3,660**	**1,363**	**9,192,509**
Corporate				
- Commercial loans	**107,368,945**	**1,492,590**	**29,394**	**108,890,929**
- Trade finance	**7,368,171**	**163,793**	**-**	**7,531,964**
	145,751,126	**1,679,854**	**32,585**	**147,463,565**
Trade bills	**16,371,563**	**-**	**-**	**16,371,563**
Total	**162,122,689**	**1,679,854**	**32,585**	**163,835,128**

	The Group			
	2013			
	Pass	Special mention	Substandard or below	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Advances to customers				
Personal				
- Mortgages	18,699,997	23,672	1,958	18,725,627
- Credit cards	445,096	-	-	445,096
- Others	7,111,627	3,798	1,697	7,117,122
Corporate				
- Commercial loans	104,860,954	2,953,206	12,863	107,827,023
- Trade finance	8,193,494	87,262	-	8,280,756
	139,311,168	3,067,938	16,518	142,395,624
Trade bills	13,242,636	-	-	13,242,636
Total	152,553,804	3,067,938	16,518	155,638,260

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(a) Advances neither overdue nor impaired (continued)

	The Bank			
	2014			
	Pass	Special mention	Substandard or below	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Advances to customers				
Personal				
- Mortgages	**10,705,641**	**5,001**	**1,438**	**10,712,080**
- Others	**7,985,480**	**2,930**	**1,363**	**7,989,773**
Corporate				
- Commercial loans	**73,439,334**	**308,640**	**29,394**	**73,777,368**
- Trade finance	**6,572,726**	**112,334**	**-**	**6,685,060**
	98,703,181	**428,905**	**32,195**	**99,164,281**
Trade bills	**7,238,603**	**-**	**-**	**7,238,603**
Total	**105,941,784**	**428,905**	**32,195**	**106,402,884**

	The Bank			
	2013			
	Pass	Special mention	Substandard or below	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Advances to customers				
Personal				
- Mortgages	10,345,633	4,093	1,285	10,351,011
- Others	5,986,849	3,155	1,697	5,991,701
Corporate				
- Commercial loans	64,167,947	1,728,339	12,863	65,909,149
- Trade finance	6,810,267	54,863	-	6,865,130
	87,310,696	1,790,450	15,845	89,116,991
Trade bills	9,458,019	-	-	9,458,019
Total	96,768,715	1,790,450	15,845	98,575,010

The occurrence of loss event(s) may not necessarily result in impairment loss where the advances are fully collateralised. While such advances are of "substandard" or lower grades, they are regarded as not being impaired and have been included in the above tables.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(b) Advances overdue but not impaired

The gross amount of advances overdue but not impaired is analysed as follows:

	The Group 2014				
	Overdue for three months or less HK$'000	**Overdue for six months or less but over three months HK$'000**	**Overdue for one year or less but over six months HK$'000**	**Overdue for over one year HK$'000**	**Total HK$'000**
Advances to customers					
Personal					
- Mortgages	**246,890**	**4,993**	**-**	**7,087**	**258,970**
- Credit cards	**31,892**	**-**	**-**	**-**	**31,892**
- Others	**47,856**	**2,441**	**-**	**6,014**	**56,311**
Corporate					
- Commercial loans	**523,957**	**18,936**	**1,160**	**1,090**	**545,143**
- Trade finance	**7,488**	**24**	**-**	**-**	**7,512**
Total	**858,083**	**26,394**	**1,160**	**14,191**	**899,828**

	The Group 2013				
	Overdue for three months or less HK$'000	Overdue for six months or less but over three months HK$'000	Overdue for one year or less but over six months HK$'000	Overdue for over one year HK$'000	Total HK$'000
Advances to customers					
Personal					
- Mortgages	312,480	92	-	5,475	318,047
- Credit cards	9,243	543	-	-	9,786
- Others	69,397	1,174	5,117	-	75,688
Corporate					
- Commercial loans	288,300	6,221	2,178	1,042	297,741
- Trade finance	9,882	-	477	-	10,359
Total	689,302	8,030	7,772	6,517	711,621

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(b) Advances overdue but not impaired (continued)

	The Bank				
	2014				
	Overdue for three months or less	**Overdue for six months or less but over three months**	**Overdue for one year or less but over six months**	**Overdue for over one year**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
Advances to customers					
Personal					
- Mortgages	**70,831**	**4,993**	**-**	**-**	**75,824**
- Others	**40,373**	**2,441**	**-**	**-**	**42,814**
Corporate					
- Commercial loans	**297,876**	**-**	**-**	**-**	**297,876**
- Trade finance	**1,666**	**-**	**-**	**-**	**1,666**
Total	**410,746**	**7,434**	**-**	**-**	**418,180**

	The Bank				
	2013				
	Overdue for three months or less	Overdue for six months or less but over three months	Overdue for one year or less but over six months	Overdue for over one year	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Advances to customers					
Personal					
- Mortgages	117,425	92	-	238	117,755
- Others	54,407	1,174	-	-	55,581
Corporate					
- Commercial loans	125,212	6,221	2,178	-	133,611
- Trade finance	9,882	-	477	-	10,359
Total	306,926	7,487	2,655	238	317,306

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(c) Impaired advances

Advances individually identified to be impaired are analysed by product type as follows:

	The Group			
	2014		2013	
	Gross advances	**Market value of collateral**	Gross advances	Market value of collateral
	HK$'000	**HK$'000**	HK$'000	HK$'000
Advances to customers				
Personal				
- Mortgages	**19,198**	**12,425**	27,341	30,941
- Credit cards	**37,469**	**-**	-	-
- Others	**11,372**	**10,027**	8,887	5,702
Corporate				
- Commercial loans	**967,981**	**883,162**	344,337	109,922
- Trade finance	**102,843**	**45,703**	54,233	57,575
Total	**1,138,863**	**951,317**	434,798	204,140
Impairment allowances made in respect of such advances	**732,356**		280,913	

	The Group	
	2014	2013
	HK$'000	HK$'000
Current market value of collateral held against the covered portion of such advances to customers	**951,317**	204,140
Covered portion of such advances to customers	**637,382**	153,690
Uncovered portion of such advances to customers	**501,481**	281,108

	The Bank			
	2014		2013	
	Gross advances	**Market value of collateral**	Gross advances	Market value of collateral
	HK$'000	**HK$'000**	HK$'000	HK$'000
Advances to customers				
Personal				
- Others	**771**	**-**	6,227	3,412
Corporate				
- Commercial loans	**111,783**	**32,054**	123,893	42,303
- Trade finance	**57,656**	**7,596**	26,712	8,177
Total	**170,210**	**39,650**	156,832	53,892
Impairment allowances made in respect of such advances	**107,058**		79,556	

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(c) Impaired advances (continued)

	The Bank	
	2014	2013
	HK$'000	HK$'000
Current market value of collateral held against the covered portion of such advances to customers	**39,650**	53,892
Covered portion of such advances to customers	**19,026**	48,739
Uncovered portion of such advances to customers	**151,184**	108,093

The impairment allowances were made after taking into account the value of collateral in respect of impaired advances.

As at 31 December 2014, there were no impaired trade bills (2013: Nil).

Classified or impaired advances to customers are analysed as follows:

	The Group	
	2014	2013
	HK$'000	HK$'000
Gross classified or impaired advances to customers	**1,254,636**	485,811
Gross classified or impaired advances to customers as a percentage of gross advances to customers	**0.84%**	0.34%
Individually assessed impairment allowances made in respect of such advances	**731,598**	280,913

	The Bank	
	2014	2013
	HK$'000	HK$'000
Gross classified or impaired advances to customers	**223,553**	192,199
Gross classified or impaired advances to customers as a percentage of gross advances to customers	**0.22%**	0.21%
Individually assessed impairment allowances made in respect of such advances	**107,058**	79,556

Classified or impaired advances to customers represent advances which are either classified as “substandard”, “doubtful” or “loss” under the Group’s classification of loan quality, or individually assessed to be impaired.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(d) Advances overdue for more than three months

The gross amount of advances overdue for more than three months is analysed as follows:

	The Group			
	2014		2013	
	Amount	% of gross advances to customers	Amount	% of gross advances to customers
	HK$'000		HK$'000	
Gross advances to customers which have been overdue for:				
- six months or less but over three months	261,805	0.17%	197,953	0.14%
- one year or less but over six months	153,074	0.10%	67,182	0.04%
- over one year	173,289	0.12%	126,102	0.09%
Advances overdue for over three months	588,168	0.39%	391,237	0.27%
Individually assessed impairment allowances made in respect of such advances	505,549		266,765	

	The Bank			
	2014		2013	
	Amount	% of gross advances to customers	Amount	% of gross advances to customers
	HK$'000		HK$'000	
Gross advances to customers which have been overdue for:				
- six months or less but over three months	27,257	0.03%	41,010	0.05%
- one year or less but over six months	14,396	0.01%	48,844	0.05%
- over one year	80,970	0.08%	49,067	0.06%
Advances overdue for over three months	122,623	0.12%	138,921	0.16%
Individually assessed impairment allowances made in respect of such advances	68,495		68,315	

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(d) Advances overdue for more than three months (continued)

	The Group	
	2014	2013
	HK$'000	HK$'000
Current market value of collateral held against the covered portion of such advances to customers	**430,468**	201,240
Covered portion of such advances to customers	**284,182**	145,200
Uncovered portion of such advances to customers	**303,986**	246,037

	The Bank	
	2014	2013
	HK$'000	HK$'000
Current market value of collateral held against the covered portion of such advances to customers	**36,124**	50,439
Covered portion of such advances to customers	**13,390**	41,597
Uncovered portion of such advances to customers	**109,233**	97,324

Collateral held against overdue or impaired loans is principally represented by charges over business assets such as commercial and residential premises for corporate loans and mortgages over residential properties for personal loans.

As at 31 December 2014, there were no trade bills overdue for more than three months for the Group and the Bank (2013: Nil).

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(e) Rescheduled advances

	The Group			
	2014		2013	
	Amount	**% of gross advances to customers**	Amount	% of gross advances to customers
	HK$'000		HK$'000	
Rescheduled advances to customers net of amounts included in "Advances overdue for more than three months"	**9,803**	**0.01%**	6,288	0.00%

	The Bank			
	2014		2013	
	Amount	**% of gross advances to customers**	Amount	% of gross advances to customers
	HK$'000		HK$'000	
Rescheduled advances to customers net of amounts included in "Advances overdue for more than three months"	**9,803**	**0.01%**	6,288	0.01%

Rescheduled advances are those advances that have been restructured or renegotiated because of deterioration in the financial position of the borrower or of the inability of the borrower to meet the original repayment schedule. Rescheduled advances, which have been overdue for more than three months under the revised repayment terms, are included in "Advances overdue for more than three months".

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers

(i) Sectoral analysis of gross advances to customers

The following analysis of the gross advances to customers by industry sector is based on the categories with reference to the Completion Instructions for the HKMA return of loans and advances.

	The Group 2014					
	Gross advances to customers HK$'000	% Covered by collateral or other security	Classified or impaired HK$'000	Overdue HK$'000	Individually assessed impairment allowances HK$'000	Collectively assessed impairment allowances HK$'000
Loans for use in Hong Kong						
Industrial, commercial and financial						
- Property development	3,109,845	30.32%	-	-	-	10,877
- Property investment	12,223,689	86.15%	9,397	35,519	1,322	119,117
- Financial concerns	2,001,248	21.71%	-	-	-	5,040
- Stockbrokers	101,383	1.35%	-	-	-	236
- Wholesale and retail trade	11,956,256	26.82%	92,507	308,788	26,800	84,717
- Manufacturing	6,307,305	23.80%	38,178	41,590	26,344	33,372
- Transport and transport equipment	4,056,145	10.50%	30,386	6,486	12,159	14,822
- Recreational activities	56,908	1.97%	-	-	-	133
- Information technology	1,728,779	1.80%	2,479	4,875	919	4,273
- Others	13,754,281	42.32%	9,630	15,346	6,830	81,038
Individuals						
- Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	455,145	99.99%	2,006	12,250	-	226
- Loans for purchase of other residential properties	10,333,678	99.51%	5,903	64,808	-	3,240
- Credit card advances	20,012	-	609	-	-	290
- Others	6,759,164	41.17%	5,411	38,361	782	5,835
Total loans for use in Hong Kong	72,863,838	50.36%	196,506	528,023	75,156	363,216
Trade finance	7,642,319	27.90%	102,867	110,355	73,200	59,473
Loans for use outside Hong Kong	68,996,099	41.47%	955,263	1,249,484	583,242	815,833
Gross advances to customers	149,502,256	45.11%	1,254,636	1,887,862	731,598	1,238,522

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

(i) Sectoral analysis of gross advances to customers (continued)

	The Group					
	2013					
	Gross advances to customers	% Covered by collateral or other security	Classified or impaired	Overdue	Individually assessed impairment allowances	Collectively assessed impairment allowances
	HK$'000		HK$'000	HK$'000	HK$'000	HK$'000
Loans for use in Hong Kong						
Industrial, commercial and financial						
- Property development	2,216,959	49.42%	-	-	-	9,953
- Property investment	12,296,487	86.23%	15,573	58,529	1,150	124,766
- Financial concerns	2,819,772	13.24%	-	-	-	8,427
- Stockbrokers	266,540	0.53%	-	-	-	643
- Wholesale and retail trade	10,133,696	32.83%	67,961	109,124	19,731	79,617
- Manufacturing	4,580,945	37.58%	39,580	43,157	24,498	43,219
- Transport and transport equipment	3,944,329	13.50%	713	2,855	167	34,125
- Recreational activities	61,579	-	-	-	-	159
- Information technology	2,051,533	1.76%	2,298	2,298	649	5,388
- Others	10,931,760	48.71%	19,871	26,902	8,016	70,296
Individuals						
- Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	565,821	100.00%	3,178	14,067	-	302
- Loans for purchase of other residential properties	9,902,944	99.91%	1,153	103,688	-	3,820
- Others	4,807,678	47.61%	3,886	45,691	771	4,769
Total loans for use in Hong Kong	64,580,043	55.38%	154,213	406,311	54,982	385,484
Trade finance	8,345,348	26.31%	54,710	64,592	34,580	60,959
Loans for use outside Hong Kong	70,616,652	41.43%	276,888	654,409	191,351	740,572
Gross advances to customers	143,542,043	46.83%	485,811	1,125,312	280,913	1,187,015

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

(i) Sectoral analysis of gross advances to customers (continued)

	The Bank					
	2014					
	Gross advances to customers	% Covered by collateral or other security	Classified or impaired	Overdue	Individually assessed impairment allowances	Collectively assessed impairment allowances
	HK$'000		HK$'000	HK$'000	HK$'000	HK$'000
Loans for use in Hong Kong						
Industrial, commercial and financial						
- Property development	3,109,845	30.32%	-	-	-	10,877
- Property investment	12,223,689	86.15%	9,397	35,519	1,322	119,117
- Financial concerns	2,001,248	21.71%	-	-	-	5,040
- Stockbrokers	101,383	1.35%	-	-	-	236
- Wholesale and retail trade	11,956,256	26.82%	92,507	308,788	26,800	84,717
- Manufacturing	6,307,305	23.80%	38,178	41,590	26,344	33,372
- Transport and transport equipment	4,026,146	9.86%	386	6,486	195	14,388
- Recreational activities	56,908	1.97%	-	-	-	133
- Information technology	1,728,779	1.80%	2,479	4,875	919	4,273
- Others	13,754,281	44.32%	9,630	15,346	6,830	81,038
Individuals						
- Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	455,145	99.99%	2,006	12,250	-	226
- Loans for purchase of other residential properties	10,332,759	99.51%	5,903	63,574	-	3,227
- Others	6,758,678	41.16%	5,411	38,361	782	5,828
Total loans for use in Hong Kong	72,812,422	50.35%	165,897	526,789	63,192	362,472
Trade finance	6,744,382	29.81%	57,656	59,322	43,866	46,480
Loans for use outside Hong Kong	20,195,867	19.31%	-	-	-	109,706
Gross advances to customers	99,752,671	42.68%	223,553	586,111	107,058	518,658

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

(i) Sectoral analysis of gross advances to customers (continued)

	The Bank					
	2013					
	Gross advances to customers	% Covered by collateral or other security	Classified or impaired	Overdue	Individually assessed impairment allowances	Collectively assessed impairment allowances
	HK$'000		HK$'000	HK$'000	HK$'000	HK$'000
Loans for use in Hong Kong						
Industrial, commercial and financial						
- Property development	2,216,959	49.42%	-	-	-	9,953
- Property investment	12,296,487	86.23%	15,573	58,529	1,150	124,766
- Financial concerns	2,819,772	13.24%	-	-	-	8,427
- Stockbrokers	266,540	0.53%	-	-	-	643
- Wholesale and retail trade	10,133,696	32.83%	67,961	109,124	19,731	79,617
- Manufacturing	4,580,945	37.58%	39,580	43,157	24,498	43,219
- Transport and transport equipment	3,910,573	13.49%	713	2,855	167	33,755
- Recreational activities	61,579	-	-	-	-	159
- Information technology	2,051,533	1.76%	2,298	2,298	649	5,388
- Others	10,931,759	48.71%	19,871	26,902	8,016	70,296
Individuals						
- Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	565,821	100.00%	3,178	14,067	-	302
- Loans for purchase of other residential properties	9,902,944	99.91%	1,153	103,688	-	3,820
- Others	4,807,678	47.61%	3,886	45,691	771	4,769
Total loans for use in Hong Kong	64,546,286	55.40%	154,213	406,311	54,982	385,114
Trade finance	6,902,201	28.82%	27,189	37,071	16,296	45,249
Loans for use outside Hong Kong	18,142,642	20.73%	10,797	11,168	8,278	165,612
Gross advances to customers	89,591,129	46.33%	192,199	454,550	79,556	595,975

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

(i) Sectoral analysis of gross advances to customers (continued)

The amount of new impairment allowances charged to the income statement, and classified or impaired loans written off during the year are shown below:

	The Group			
	2014		2013	
	New impairment allowances	**Classified or impaired loans written off**	New impairment allowances	Classified or impaired loans written off
	HK$'000	**HK$'000**	HK$'000	HK$'000
Loans for use in Hong Kong				
Industrial, commercial and financial				
- Property investment	**2,484**	**3,237**	1,954	738
- Stockbrokers	**-**	**-**	36	-
- Wholesale and retail trade	**13,970**	**5,433**	11,310	7,449
- Manufacturing	**7,173**	**3,244**	7,211	2,841
- Transport and transport equipment	**11,881**	**-**	210	-
- Information technology	**270**	**-**	70	-
- Others	**3,283**	**470**	8,679	2,152
Individuals				
- Loans for purchase of other residential properties	**2**	**-**	-	-
- Credit card advances	**32**	**-**	-	-
- Others	**18,262**	**17,193**	9,467	6,747
Total loans for use in Hong Kong	**57,357**	**29,577**	38,937	19,927
Trade finance	**55,594**	**4,339**	11,337	2,556
Loans for use outside Hong Kong	**899,775**	**344,936**	383,201	137,691
Gross advances to customers	**1,012,726**	**378,852**	433,475	160,174

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

(i) Sectoral analysis of gross advances to customers (continued)

	The Bank			
	2014		2013	
	New impairment allowances	**Classified or impaired loans written off**	New impairment allowances	Classified or impaired loans written off
	HK$'000	**HK$'000**	HK$'000	HK$'000
Loans for use in Hong Kong				
Industrial, commercial and financial				
- Property investment	**2,484**	**3,237**	1,954	738
- Stockbrokers	**-**	**-**	36	-
- Wholesale and retail trade	**13,970**	**5,433**	11,310	7,449
- Manufacturing	**7,173**	**3,244**	7,211	2,841
- Transport and transport equipment	**229**	**-**	77	-
- Information technology	**270**	**-**	70	-
- Others	**3,283**	**470**	8,679	2,152
Individuals				
- Others	**18,262**	**17,193**	9,467	6,747
Total loans for use in Hong Kong	**45,671**	**29,577**	38,804	19,927
Trade finance	**41,922**	**4,339**	5,688	2,556
Loans for use outside Hong Kong	**93**	**3,000**	10,243	-
Gross advances to customers	**87,686**	**36,916**	54,735	22,483

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

(ii) Geographical analysis of gross advances to customers

The following geographical analysis of advances to customers is based on the location of the counterparties, after taking into account the transfer of risk. For an advance to customer guaranteed by a party situated in a country different from the customer, the risk will be transferred to the country of the guarantor.

Gross advances to customers

	The Group	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**73,959,116**	71,198,417
Mainland of China	**69,650,228**	66,923,361
Others	**5,892,912**	5,420,265
	149,502,256	143,542,043

	The Bank	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**70,872,475**	66,697,103
Mainland of China	**23,987,373**	18,605,455
Others	**4,892,823**	4,288,571
	99,752,671	89,591,129

Collectively assessed impairment allowances in respect of the gross advances to customers

	The Group	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**412,140**	463,692
Mainland of China	**730,437**	633,469
Others	**95,945**	89,854
	1,238,522	1,187,015

	The Bank	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**355,366**	406,112
Mainland of China	**120,996**	155,014
Others	**42,296**	34,849
	518,658	595,975

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

(ii) Geographical analysis of gross advances to customers (continued)

Overdue advances

	The Group	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**332,232**	422,834
Mainland of China	**1,546,827**	659,877
Others	**8,803**	42,601
	1,887,862	1,125,312

	The Bank	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**327,189**	399,093
Mainland of China	**257,525**	43,917
Others	**1,397**	11,540
	586,111	454,550

Individually assessed impairment allowances in respect of the overdue advances

	The Group	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**52,960**	50,989
Mainland of China	**546,644**	217,507
Others	**1,448**	4,377
	601,052	272,873

	The Bank	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**52,960**	46,567
Mainland of China	**50,375**	21,953
Others	**1,448**	4,257
	104,783	72,777

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

(ii) Geographical analysis of gross advances to customers (continued)

Overdue advances (continued)

Collectively assessed impairment allowances in respect of the overdue advances

	The Group	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**6,660**	8,155
Mainland of China	**6,844**	3,632
Others	**20**	238
	13,524	12,025

	The Bank	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**6,646**	8,016
Mainland of China	**3,310**	35
Others	**-**	57
	9,956	8,108

Classified or impaired advances

	The Group	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**151,434**	154,186
Mainland of China	**1,101,806**	324,675
Others	**1,396**	6,950
	1,254,636	485,811

	The Bank	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**151,434**	148,681
Mainland of China	**70,723**	36,707
Others	**1,396**	6,811
	223,553	192,199

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

(ii) Geographical analysis of gross advances to customers (continued)

Classified or impaired advances (continued)

Individually assessed impairment allowances in respect of the classified or impaired advances

	The Group	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**55,235**	57,768
Mainland of China	**674,915**	218,768
Others	**1,448**	4,377
	731,598	280,913

	The Bank	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**55,235**	53,345
Mainland of China	**50,375**	21,954
Others	**1,448**	4,257
	107,058	79,556

Collectively assessed impairment allowances in respect of the classified or impaired advances

	The Group	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**3,524**	2,298
Mainland of China	**1,609**	39
	5,133	2,337

	The Bank	
	2014	2013
	HK$'000	HK$'000
Hong Kong	**3,524**	2,297
	3,524	2,297

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(C) Repossessed assets

During the year, the Group and the Bank obtained assets by taking possession of collateral held as security. The nature and carrying value of these assets held as at 31 December are summarised as follows:

	The Group		The Bank	
	2014	2013	**2014**	2013
	HK$'000	HK$'000	**HK$'000**	HK$'000
Industrial properties	**-**	2,790	**-**	2,790
Residential properties	**-**	19,494	**-**	15,300
Other	**583**	-	**583**	-
	583	22,284	**583**	18,090

The estimated market value of repossessed assets held by the Group and the Bank as at 31 December 2014 amounted to HK$4,906,000 (2013: HK$38,822,000) and HK$730,000 (2013: HK$34,250,000). They comprise properties in respect of which the Group and the Bank have acquired access or control (e.g. through court proceedings or voluntary actions by the proprietors concerned) for release in full or in part of the obligations of the borrowers.

When the repossessed assets are not readily convertible into cash, the Group may consider the following alternatives:

- adjusting the selling prices
- selling the loans together with the assets
- arranging loan restructuring

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(D) Balances and placements with banks and other financial institutions

The following tables present an analysis of balances and placements with banks and other financial institutions that are neither overdue nor impaired as at 31 December by rating agency designation.

	The Group			
	2014			
	Aaa to A3	**Lower than A3**	**Unrated**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Central banks	**18,694,761**	**-**	**-**	**18,694,761**
Banks and other financial institutions	**20,208,603**	**20,003,535**	**16,963,308**	**57,175,446**
	38,903,364	**20,003,535**	**16,963,308**	**75,870,207**

	The Group			
	2013			
	Aaa to A3	Lower than A3	Unrated	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Central banks	17,068,323	-	-	17,068,323
Banks and other financial institutions	15,178,049	20,416,998	12,536,250	48,131,297
	32,246,372	20,416,998	12,536,250	65,199,620

	The Bank			
	2014			
	Aaa to A3	**Lower than A3**	**Unrated**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Central banks	**2,364,763**	**-**	**-**	**2,364,763**
Banks and other financial institutions	**15,314,234**	**8,535,286**	**3,916,785**	**27,766,305**
	17,678,997	**8,535,286**	**3,916,785**	**30,131,068**

	The Bank			
	2013			
	Aaa to A3	Lower than A3	Unrated	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Central banks	853,838	-	-	853,838
Banks and other financial institutions	6,302,846	8,051,195	4,899,332	19,253,373
	7,156,684	8,051,195	4,899,332	20,107,211

As at 31 December 2014, there were no overdue or impaired balances and placements with banks and other financial institutions (2013: Nil).

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.1 Credit Risk (continued)

(E) Debt securities and certificates of deposit

The following tables present an analysis of the carrying value of debt securities and certificates of deposit by issue rating.

In the absence of such issue ratings, the ratings designated for the issuers are reported.

	The Group					
	2014					
	Aaa	**Aa1 to Aa3**	**A1 to A3**	**Lower than A3**	**Unrated**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
Available-for-sale securities	**5,179,077**	**20,657,187**	**11,750,008**	**448,511**	**4,364,791**	**42,399,574**
Held-to-maturity securities	**243,450**	**1,759,590**	**615,350**	**-**	**-**	**2,618,390**
Loans and receivables	**-**	**-**	**62,421**	**-**	**2,012,173**	**2,074,594**
Financial assets at fair value through profit or loss	**4,589,985**	**1,309,309**	**255,919**	**-**	**-**	**6,155,213**
Total	**10,012,512**	**23,726,086**	**12,683,698**	**448,511**	**6,376,964**	**53,247,771**

	The Group					
	2013					
	Aaa	Aa1 to Aa3	A1 to A3	Lower than A3	Unrated	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Available-for-sale securities	895,932	18,002,312	15,328,029	445,839	5,266,560	39,938,672
Held-to-maturity securities	-	585,144	-	298	-	585,442
Loans and receivables	-	-	1,008,897	-	675,167	1,684,064
Financial assets at fair value through profit or loss	624	3,665,412	498,657	-	-	4,164,693
Total	896,556	22,252,868	16,835,583	446,137	5,941,727	46,372,871

	The Bank					
	2014					
	Aaa	**Aa1 to Aa3**	**A1 to A3**	**Lower than A3**	**Unrated**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
Available-for-sale securities	**5,179,077**	**15,402,866**	**10,347,509**	**448,511**	**3,390,708**	**34,768,671**
Held-to-maturity securities	**243,450**	**-**	**-**	**-**	**-**	**243,450**
Loans and receivables	**-**	**-**	**62,421**	**-**	**2,012,173**	**2,074,594**
Financial assets at fair value through profit or loss	**4,589,985**	**1,309,309**	**255,919**	**-**	**-**	**6,155,213**
Total	**10,012,512**	**16,712,175**	**10,665,849**	**448,511**	**5,402,881**	**43,241,928**

	The Bank					
	2013					
	Aaa	Aa1 to Aa3	A1 to A3	Lower than A3	Unrated	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Available-for-sale securities	895,932	14,633,726	14,733,437	445,839	3,944,717	34,653,651
Held-to-maturity securities	-	-	-	298	-	298
Loans and receivables	-	-	1,008,897	-	675,167	1,684,064
Financial assets at fair value through profit or loss	624	3,665,412	498,657	-	-	4,164,693
Total	896,556	18,299,138	16,240,991	446,137	4,619,884	40,502,706

As at 31 December 2014, there were no impaired or overdue debt securities and certificates of deposit (2013: Nil).

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk

Market risk refers to the risk of loss arising from movements in the value of foreign exchange, interest rate, equity and commodity positions held by the Group due to the volatility of financial market price (foreign exchange rate, interest rate, equity price, commodity price). The Group adopts a moderate market risk appetite to achieve a balance between risk and return.

The Group's objective in managing market risk is to secure healthy growth of the treasury business, by effective management of potential market risk in the Group's business, according to the Group's overall risk appetite and strategy of treasury business on the basis of a well established risk management regime and related management measures.

In accordance with the Group's corporate governance principles in respect of risk management, the Board and Risk Management Committee, Senior Management and functional units perform their duties and responsibilities to manage the Group's market risk. The risk management units are responsible for assisting Senior Management to perform their day-to-day duties, independently monitoring the market risk profile and compliance of management policies and limits of the Group to ensure that the aggregate and individual market risks are within acceptable levels. Independent units are assigned to monitor the risk exposure against risk limits on a daily basis, together with profit and loss reports submitted to Senior Management on a regular basis, while limit excesses should be reported at once when they occur. NCB (China) sets up independent risk monitoring teams to monitor daily market risk and limit compliance, and submit management information and reports to the Bank on a regular basis.

The Group sets up market risk indicators and limits to identify, measure, monitor and control market risk. Major risk indicators and limits include but are not limited to VAR, Stop Loss, Open Position, Stress Testing and Sensitivity Analysis (Basis Point Value), etc. To meet management requirements, major risk indicators and limits are classified into four levels, and are approved by the Risk Management Committee, Asset and Liability Management Committee or Senior Management respectively. Treasury business units are required to conduct their business within approved market risk indicators and limits.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk (continued)

(A) VAR

The Group uses the VAR to measure and report general market risks to the Risk Management Committee and Senior Management on a periodic basis. The Group adopts a uniformed VAR calculation model, using a historical simulation approach and two years of historical market data, to calculate the VAR of the Group and the Bank over 1-day holding period with a 99% confidence level, and sets up the VAR limit of the Group and the Bank.

The following table sets out the VAR for all general market risk exposure[1] of the Group.

	Year	At 31 December	Minimum for the year	Maximum for the year	Average for the year
		HK$'000	HK$'000	HK$'000	HK$'000
VAR for all market risk	2014	635	635	1,901	1,181
	2013	1,294	1,294	2,982	2,196
VAR for foreign exchange risk	2014	544	544	1,975	1,145
	2013	1,191	1,191	3,047	2,196
VAR for interest rate risk	2014	274	225	883	644
	2013	502	117	635	268

Note:

1. Structural FX positions have been excluded.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk (continued)

(A) VAR (continued)

Although VAR is a valuable guide to risk, it should always be viewed in the context of its limitations. For example:

- the use of historical market data as a proxy for estimating future events may not encompass all potential events, particularly those which are extreme in nature;
- the use of a one-day holding period assumes that all positions can be liquidated or hedged in one day. This may not fully reflect the market risk arising at times of severe illiquidity, when a one-day holding period may be insufficient to liquidate or hedge all positions fully;
- the use of a 99% confidence level, by definition, does not take into account losses that might occur beyond this level of confidence; and
- VAR is calculated on the basis of exposures outstanding at the close of business and therefore does not necessarily reflect intra-day exposures.

The Group recognises these limitations by formulating stress test indicators and limits to assess and manage the market risk uncovered by VAR. The stress testing programme of the market risk includes sensitivity testing on changes in risk factors with various degrees of severity, as well as scenario analysis on historical events including the 1997 Asian Financial Crisis and 2008 Financial Tsunami, etc.

(B) Currency risk

The Group's assets and liabilities are denominated in major currencies, particularly the HK dollar, the US dollar and Renminbi. To ensure the currency risk exposure of the Group is kept to an acceptable level, risk limits (e.g. Position and VAR limit) are used to serve as a monitoring tool. Moreover, the Group seeks to minimise the gap between assets and liabilities in the same currency. Foreign exchange contracts (e.g. FX swaps) are usually used to manage FX risk associated with foreign currency-denominated assets and liabilities.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk (continued)

(B) Currency risk (continued)

The tables below summarise the Group's and the Bank's exposure to foreign currency exchange rate risk as at 31 December. Included in the tables are the assets and liabilities at carrying amounts in HK dollars equivalent, categorised by the original currency.

	The Group							
	2014							
	Renminbi	US Dollars	HK Dollars	Euro	Japanese Yen	Pound Sterling	Others	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets								
Cash and balances with banks and other financial institutions	42,364,659	2,960,246	11,289,701	831,519	239,946	507,181	89,548	58,282,800
Placements with banks and other financial institutions maturing between one and twelve months	16,629,417	1,551,345	-	-	-	-	-	18,180,762
Financial assets at fair value through profit or loss	-	255,919	5,899,294	-	-	-	-	6,155,213
Derivative financial instruments	29,429	23,304	386,339	-	-	-	-	439,072
Advances and other accounts	47,159,099	45,377,082	70,479,469	692,972	39,198	6,024	149,855	163,903,699
Investment in securities								
- Available-for-sale securities	18,630,828	5,063,554	11,506,285	1,288,052	-	328,143	5,658,478	42,475,340
- Held-to-maturity securities	2,374,940	-	-	-	-	-	243,450	2,618,390
- Loans and receivables	2,074,594	-	-	-	-	-	-	2,074,594
Investment properties	22,150	-	1,258,121	-	-	-	-	1,280,271
Properties, plant and equipment	749,352	2,349	6,576,796	-	-	-	-	7,328,497
Other assets (including deferred tax assets)	383,240	8,160	771,987	71	8	1	2,148	1,165,615
Total assets	130,417,708	55,241,959	108,167,992	2,812,614	279,152	841,349	6,143,479	303,904,253
Liabilities								
Deposits and balances from banks and other financial institutions	27,383,278	8,127,490	962,567	2,631	5,388	7,837	1,246,420	37,735,611
Financial liabilities at fair value through profit or loss	-	-	4,970,693	-	-	-	-	4,970,693
Derivative financial instruments	104,275	40,231	134,000	-	-	-	-	278,506
Deposits from customers	71,779,386	38,596,971	91,755,578	2,890,697	203,270	743,193	3,664,840	209,633,935
Other accounts and provisions (including current and deferred tax liabilities)	12,005,185	1,249,882	2,906,653	79,319	65,738	1,910	81,977	16,390,664
Total liabilities	111,272,124	48,014,574	100,729,491	2,972,647	274,396	752,940	4,993,237	269,009,409
Net on-balance sheet position	19,145,584	7,227,385	7,438,501	(160,033)	4,756	88,409	1,150,242	34,894,844
Off-balance sheet net notional position*	(11,131,241)	(6,861,852)	19,219,651	172,949	(2,371)	(87,995)	(1,120,512)	188,629
Contingent liabilities and commitments	63,550,780	29,571,235	19,307,558	404,777	72,017	7,968	-	112,914,335

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk (continued)

(B) Currency risk (continued)

	The Group							
	2013							
	Renminbi	US Dollars	HK Dollars	Euro	Japanese Yen	Pound Sterling	Others	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets								
Cash and balances with banks and other financial institutions	37,895,965	3,302,233	3,031,355	287,594	76,650	43,356	102,166	44,739,319
Placements with banks and other financial institutions maturing between one and twelve months	20,497,328	846,672	-	-	-	-	-	21,344,000
Financial assets at fair value through profit or loss	-	498,657	3,666,036	-	-	-	-	4,164,693
Derivative financial instruments	95,469	15,990	396,994	-	-	-	-	508,453
Advances and other accounts	46,507,717	43,888,535	64,276,248	391,263	34,633	11,410	206,945	155,316,751
Investment in securities								
- Available-for-sale securities	14,477,805	6,151,826	11,191,446	780,426	-	-	7,401,134	40,002,637
- Held-to-maturity securities	585,144	-	298	-	-	-	-	585,442
- Loans and receivables	833,378	850,686	-	-	-	-	-	1,684,064
Investment properties	48,428	-	1,126,510	-	-	-	-	1,174,938
Properties, plant and equipment	777,270	3,467	6,188,500	-	-	-	-	6,969,237
Other assets (including deferred tax assets)	309,581	49,808	3,532,919	399	7	6	1,706	3,894,426
Total assets	122,028,085	55,607,874	93,410,306	1,459,682	111,290	54,772	7,711,951	280,383,960
Liabilities								
Deposits and balances from banks and other financial institutions	17,115,023	9,846,139	1,340,154	72,617	4,195	3,290	464,611	28,846,029
Financial liabilities at fair value through profit or loss	-	-	4,433,736	-	-	-	-	4,433,736
Derivative financial instruments	92,363	59,342	191,451	-	-	-	-	343,156
Deposits from customers	82,735,748	30,587,345	75,681,802	2,254,533	211,583	922,912	5,766,494	198,160,417
Other accounts and provisions (including current and deferred tax liabilities)	10,488,966	1,026,354	4,607,189	57,944	32,756	1,391	86,033	16,300,633
Total liabilities	110,432,100	41,519,180	86,254,332	2,385,094	248,534	927,593	6,317,138	248,083,971
Net on-balance sheet position	11,595,985	14,088,694	7,155,974	(925,412)	(137,244)	(872,821)	1,394,813	32,299,989
Off-balance sheet net notional position*	(4,137,873)	(12,082,047)	15,842,217	929,725	138,070	873,190	(1,347,921)	215,361
Contingent liabilities and commitments	58,871,709	30,613,919	20,015,614	566,451	54,213	8,978	15,232	110,146,116

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk (continued)

(B) Currency risk (continued)

	The Bank							
	2014							
	Renminbi	US Dollars	HK Dollars	Euro	Japanese Yen	Pound Sterling	Others	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets								
Cash and balances with banks and other financial institutions	16,143,673	1,970,310	10,838,411	710,845	215,837	459,018	53,447	30,391,541
Placements with banks and other financial institutions maturing between one and twelve months	-	145,422	-	-	-	-	-	145,422
Financial assets at fair value through profit or loss	-	255,919	5,899,294	-	-	-	-	6,155,213
Derivative financial instruments	-	16,425	386,339	-	-	-	-	402,764
Advances and other accounts	1,958,855	36,046,955	67,475,695	688,976	39,198	6,024	149,855	106,365,558
Investment in securities								
- Available-for-sale securities	10,999,925	5,063,554	11,506,285	1,288,052	-	328,143	5,658,478	34,844,437
- Held-to-maturity securities	-	-	-	-	-	-	243,450	243,450
- Loans and receivables	2,074,594	-	-	-	-	-	-	2,074,594
Investment in subsidiaries	3,030,038	-	5,141,029	-	-	-	-	8,171,067
Investment properties	-	-	1,258,121	-	-	-	-	1,258,121
Properties, plant and equipment	-	2,349	6,576,796	-	-	-	-	6,579,145
Other assets	5,301	4,143	770,949	2	5	1	2,147	782,548
Total assets	34,212,386	43,505,077	109,852,919	2,687,875	255,040	793,186	6,107,377	197,413,860
Liabilities								
Deposits and balances from banks and other financial institutions	3,919,899	4,063,439	1,029,794	18,166	38,733	25,795	1,273,543	10,369,369
Financial liabilities at fair value through profit or loss	-	-	4,970,693	-	-	-	-	4,970,693
Derivative financial instruments	-	33,394	134,000	-	-	-	-	167,394
Deposits from customers	20,825,936	30,211,854	87,735,231	2,684,191	180,081	677,746	3,555,588	145,870,627
Other accounts and provisions (including current and deferred tax liabilities)	110,675	478,337	2,874,792	6,251	37,161	1,842	76,525	3,585,583
Total liabilities	24,856,510	34,787,024	96,744,510	2,708,608	255,975	705,383	4,905,656	164,963,666
Net on-balance sheet position	9,355,876	8,718,053	13,108,409	(20,733)	(935)	87,803	1,201,721	32,450,194
Off-balance sheet net notional position*	(6,147,233)	(8,463,514)	16,020,834	33,550	3,328	(87,995)	(1,171,170)	187,800
Contingent liabilities and commitments	8,882	15,104,193	18,567,782	267,386	19,062	-	-	33,967,305

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk (continued)

(B) Currency risk (continued)

	The Bank							
	2013							
	Renminbi	US Dollars	HK Dollars	Euro	Japanese Yen	Pound Sterling	Others	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets								
Cash and balances with banks and other financial institutions	13,761,499	2,100,851	2,594,300	235,431	47,250	17,418	83,585	18,840,334
Placements with banks and other financial institutions maturing between one and twelve months	-	1,858,262	-	-	-	-	-	1,858,262
Financial assets at fair value through profit or loss	-	498,657	3,666,036	-	-	-	-	4,164,693
Derivative financial instruments	-	13,440	396,994	-	-	-	-	410,434
Advances and other accounts	2,395,627	33,962,136	61,418,574	344,292	34,633	11,410	206,945	98,373,617
Investment in securities								
- Available-for-sale securities	9,192,784	6,151,826	11,191,446	780,426	-	-	7,401,134	34,717,616
- Held-to-maturity securities	-	-	298	-	-	-	-	298
- Loans and receivables	833,378	850,686	-	-	-	-	-	1,684,064
Investment in subsidiaries	3,030,038	-	5,141,029	-	-	-	-	8,171,067
Investment properties	-	-	1,126,510	-	-	-	-	1,126,510
Properties, plant and equipment	-	3,467	6,188,500	-	-	-	-	6,191,967
Other assets	550	2,859	3,526,912	399	7	6	1,706	3,532,439
Total assets	29,213,876	45,442,184	95,250,599	1,360,548	81,890	28,834	7,693,370	179,071,301
Liabilities								
Deposits and balances from banks and other financial institutions	2,140,690	3,358,178	1,399,295	100,521	7,539	7,822	474,246	7,488,291
Financial liabilities at fair value through profit or loss	-	-	4,433,736	-	-	-	-	4,433,736
Derivative financial instruments	-	56,863	191,451	-	-	-	-	248,314
Deposits from customers	25,779,819	24,834,671	72,183,662	2,101,770	181,948	893,395	5,749,321	131,724,586
Other accounts and provisions (including current and deferred tax liabilities)	108,830	457,151	4,555,742	8,242	29,666	1,301	81,237	5,242,169
Total liabilities	28,029,339	28,706,863	82,763,886	2,210,533	219,153	902,518	6,304,804	149,137,096
Net on-balance sheet position	1,184,537	16,735,321	12,486,713	(849,985)	(137,263)	(873,684)	1,388,566	29,934,205
Off-balance sheet net notional position*	1,655,076	(14,852,193)	12,889,029	854,243	138,070	873,190	(1,342,053)	215,362
Contingent liabilities and commitments	259,936	10,495,869	19,684,741	183,512	24,371	1,015	699	30,650,143

* Off-balance sheet net notional position represents the net notional amounts of foreign currency derivative financial instruments, which are principally used to reduce the Group's and the Bank's exposure to currency movements.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk (continued)

(C) Interest rate risk

Interest rate risk means the risks to a bank's earnings and economic value arising from adverse movements in interest rate and term structures of the bank's asset and liability positions. The Group's interest rate risk exposures are mainly structural. The major types of interest rate risk from structural positions are:

- Repricing risk: mismatches in the maturity or repricing periods of assets and liabilities that may affect net interest income;

- Basis risk: different pricing basis for different transactions resulting that the yield on assets and cost of liabilities may change by different amounts within the same repricing period;

- Yield curve risk: non-parallel shifts in the yield curve that may have an adverse impact on net interest income or economic value;

- Option risk: exercise of the options embedded in assets, liabilities or off-balance sheet items that can cause a change in the cash flows of assets and liabilities.

The Group's risk management framework also applies to interest rate risk management. The Asset and Liability Management Committee exercises its oversight of interest rate risk in accordance with Banking Book Interest Rate Risk Management Policy" approved by Risk Management Committee. Financial Management Division is responsible for interest rate risk management. With the cooperation of the Treasury Division, Financial Management Division assists the Asset and Liability Management Committee to perform day-to-day interest rate risk management. Its roles include, but are not limited to, the formulation of management policies, selection of methodologies, setting of risk indicators and limits, assessment of target balance sheet, monitoring of the compliance with policies and limits, and submission of interest rate risk management reports to the Management and Risk Management Committee, etc.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk (continued)

(C) Interest rate risk (continued)

The Group sets out interest rate risk indicators and limits to identify, measure, monitor and control interest rate risk. The indicators and limits include, but are not limited to, repricing gap limits, basis risk, duration, price value of a basis point ("PVBP"), net interest income sensitivity ratio ("NII"), economic value sensitivity ratio ("EV"), etc. The indicators and limits are classified into three levels, which are approved by the Risk Management Committee, Asset and Liability Management Committee and Deputy General Manager of Middle-office respectively. Risk-taking business units are required to conduct their business within the boundary of the interest rate risk limits. Before launching a new product or business in the banking book, the relevant departments are required to go through a risk assessment process, which includes the assessment of underlying interest rate risk and consideration of the adequacy of current risk monitoring mechanism. Any material impact on interest rate risk noted during the risk assessment process will be submitted to Risk Management Committee for approval.

NII and EV assess the impact of interest rate movement on the Group's net interest income and capital base. They are the Group's key interest rate risk indicators. The former assesses the impact of interest rate movement on net interest income as a percentage to the projected net interest income for the year. The latter assesses the impact of interest rate movement on economic value (i.e. the net present value of cash flows of assets, liabilities and off-balance sheet items discounted using market interest rate) as a percentage to the latest capital base. Limits are set by the Risk Management Committee on these two indicators to monitor and control the Group's banking book interest rate risk.

The Group uses scenario analysis and stress tests to assess the banking book interest rate risk that the Group would face under adverse circumstances. Scenario analyses and stress tests are also devised to assess the impact on net interest income and economic value arising from the optionality of demand and savings deposits and the prepayment of mortgage loans.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk (continued)

(C) Interest rate risk (continued)

The Group is principally exposed to HKD, USD and RMB in terms of interest rate risk. As at 31 December 2014, if HKD, USD and RMB market interest rates had been 100 basis point higher with other variables held constant, the sensitivities on net interest income over the next twelve months and on reserves for the Group and the Bank would have been as follows:

	Impact on net interest income over the next twelve months at 31 December				Impact on reserves at 31 December			
	The Group		The Bank		The Group		The Bank	
	2014	2013	**2014**	2013	**2014**	2013	**2014**	2013
	HK$'000	HK$'000	**HK$'000**	HK$'000	**HK$'000**	HK$'000	**HK$'000**	HK$'000
HK Dollar	**256,299**	232,271	**216,891**	198,455	**(46,786)**	(53,388)	**(46,786)**	(53,388)
US Dollar	**(32,688)**	(30,024)	**(49,851)**	(35,681)	**(60,416)**	(100,832)	**(60,416)**	(100,832)
Renminbi	**(13,535)**	(12,059)	**(92,021)**	(74,957)	**(324,817)**	(263,101)	**(163,634)**	(154,352)

The overall positive impact on Group's net interest income of the above currencies has increased when compared with 2013 and is mainly because of the widened short term positive gaps in HKD. Reserves would have been reduced because of the expected reduction in valuation of available-for-sale portfolio due to a parallel shift up of 100 basis point in the yield curve (simulated scenario). The reduction of reserves is increased compared with 2013 because the size of Renminbi available-for-sale portfolio is increased.

The sensitivities above are for illustration only and are based on several assumptions, including (but not limited to) the change in the correlation between interest rates of relevant currencies, parallel movement of interest rates, the absence of actions that would be taken to mitigate the impact of interest rate risk, the effectiveness of hedging accounting, all positions being assumed to run to maturity, behavioural assumptions of products in which actual repricing date differs from contractual repricing date or products without contractual maturity. The above exposures form only a part of the Group's overall interest rate risk exposures.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk (continued)

(C) Interest rate risk (continued)

The tables below summarise the Group's and the Bank's on-balance sheet exposure to interest rate risk as at 31 December. Included in the tables are the assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

	The Group						
	2014						
	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Non-interest bearing	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets							
Cash and balances with banks and other financial institutions	54,183,243	-	-	-	-	4,099,557	58,282,800
Placements with banks and other financial institutions maturing between one and twelve months	-	9,477,006	8,703,756	-	-	-	18,180,762
Financial assets at fair value through profit or loss	470,000	2,671,893	2,757,401	255,919	-	-	6,155,213
Derivative financial instruments	-	-	-	-	-	439,072	439,072
Advances and other accounts	108,282,638	31,356,774	20,553,491	3,451,440	259,356	-	163,903,699
Investment in securities							
- Available-for-sale securities	2,375,913	10,487,111	12,504,107	16,466,480	565,963	75,766	42,475,340
- Held-to-maturity securities	-	-	-	1,998,756	619,634	-	2,618,390
- Loans and receivables	-	620,262	1,454,332	-	-	-	2,074,594
Investment properties	-	-	-	-	-	1,280,271	1,280,271
Properties, plant and equipment	-	-	-	-	-	7,328,497	7,328,497
Other assets (including deferred tax assets)	2,208	-	-	-	-	1,163,407	1,165,615
Total assets	165,314,002	54,613,046	45,973,087	22,172,595	1,444,953	14,386,570	303,904,253
Liabilities							
Deposits and balances from banks and other financial institutions	18,391,118	9,332,830	8,050,874	-	-	1,960,789	37,735,611
Financial liabilities at fair value through profit or loss	1,978,491	873,945	2,118,257	-	-	-	4,970,693
Derivative financial instruments	-	-	-	-	-	278,506	278,506
Deposits from customers	122,791,320	36,089,981	32,061,913	9,455,287	-	9,235,434	209,633,935
Other accounts and provisions (including current and deferred tax liabilities)	5,111,293	2,685,535	4,055,058	194,043	736	4,343,999	16,390,664
Total liabilities	148,272,222	48,982,291	46,286,102	9,649,330	736	15,818,728	269,009,409
Interest sensitivity gap	17,041,780	5,630,755	(313,015)	12,523,265	1,444,217	(1,432,158)	34,894,844

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk (continued)

(C) Interest rate risk (continued)

	The Group 2013						
	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Non-interest bearing	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets							
Cash and balances with banks and other financial institutions	43,239,550	-	-	-	-	1,499,769	44,739,319
Placements with banks and other financial institutions maturing between one and twelve months	-	10,324,490	11,019,510	-	-	-	21,344,000
Financial assets at fair value through profit or loss	296,487	704,859	2,901,993	261,354	-	-	4,164,693
Derivative financial instruments	-	-	-	-	-	508,453	508,453
Advances and other accounts	95,905,202	24,502,236	29,683,287	5,037,156	183,445	5,425	155,316,751
Investment in securities							
- Available-for-sale securities	4,121,084	7,615,224	10,198,263	16,543,097	1,461,004	63,965	40,002,637
- Held-to-maturity securities	298	-	585,144	-	-	-	585,442
- Loans and receivables	105,185	661,988	916,891	-	-	-	1,684,064
Investment properties	-	-	-	-	-	1,174,938	1,174,938
Properties, plant and equipment	-	-	-	-	-	6,969,237	6,969,237
Other assets (including deferred tax assets)	770	-	-	-	-	3,893,656	3,894,426
Total assets	143,668,576	43,808,797	55,305,088	21,841,607	1,644,449	14,115,443	280,383,960
Liabilities							
Deposits and balances from banks and other financial institutions	15,176,539	3,306,414	8,778,777	-	-	1,584,299	28,846,029
Financial liabilities at fair value through profit or loss	701,490	1,727,292	2,004,954	-	-	-	4,433,736
Derivative financial instruments	-	-	-	-	-	343,156	343,156
Deposits from customers	111,858,553	29,530,001	38,410,496	9,873,053	39,057	8,449,257	198,160,417
Other accounts and provisions (including current and deferred tax liabilities)	2,966,037	2,588,722	4,105,753	397,216	-	6,242,905	16,300,633
Total liabilities	130,702,619	37,152,429	53,299,980	10,270,269	39,057	16,619,617	248,083,971
Interest sensitivity gap	12,965,957	6,656,368	2,005,108	11,571,338	1,605,392	(2,504,174)	32,299,989

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk (continued)

(C) Interest rate risk (continued)

	The Bank						
	2014						
	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Non-interest bearing	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets							
Cash and balances with banks and other financial institutions	26,479,443	-	-	-	-	3,912,098	30,391,541
Placements with banks and other financial institutions maturing between one and twelve months	-	145,422	-	-	-	-	145,422
Financial assets at fair value through profit or loss	470,000	2,671,893	2,757,401	255,919	-	-	6,155,213
Derivative financial instruments	-	-	-	-	-	402,764	402,764
Advances and other accounts	81,223,872	17,897,620	4,938,514	2,292,605	12,947	-	106,365,558
Investment in securities							
- Available-for-sale securities	2,375,913	10,345,533	10,974,586	11,072,639	-	75,766	34,844,437
- Held-to-maturity securities	-	-	-	243,450	-	-	243,450
- Loans and receivables	-	620,262	1,454,332	-	-	-	2,074,594
Investment in subsidiaries	-	-	-	-	-	8,171,067	8,171,067
Investment properties	-	-	-	-	-	1,258,121	1,258,121
Properties, plant and equipment	-	-	-	-	-	6,579,145	6,579,145
Other assets	-	-	-	-	-	782,548	782,548
Total assets	110,549,228	31,680,730	20,124,833	13,864,613	12,947	21,181,509	197,413,860
Liabilities							
Deposits and balances of banks and other financial institutions	6,243,974	1,044,267	1,026,373	-	-	2,054,755	10,369,369
Financial liabilities at fair value through profit or loss	1,978,491	873,945	2,118,257	-	-	-	4,970,693
Derivative financial instruments	-	-	-	-	-	167,394	167,394
Deposits from customers	96,034,199	27,388,448	12,186,968	1,019,829	-	9,241,183	145,870,627
Other accounts and provisions (including current and deferred tax liabilities)	450,549	-	-	-	-	3,135,034	3,585,583
Total liabilities	104,707,213	29,306,660	15,331,598	1,019,829	-	14,598,366	164,963,666
Interest sensitivity gap	5,842,015	2,374,070	4,793,235	12,844,784	12,947	6,583,143	32,450,194

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.2 Market Risk (continued)

(C) Interest rate risk (continued)

	The Bank						
	2013						
	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Non-interest bearing	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets							
Cash and balances with banks and other financial institutions	17,632,879	-	-	-	-	1,207,455	18,840,334
Placements with banks and other financial institutions maturing between one and twelve months	-	1,527,931	330,331	-	-	-	1,858,262
Financial assets at fair value through profit or loss	296,487	704,859	2,901,993	261,354	-	-	4,164,693
Derivative financial instruments	-	-	-	-	-	410,434	410,434
Advances and other accounts	75,387,024	13,990,291	7,150,346	1,834,237	6,284	5,435	98,373,617
Investment in securities							
- Available-for-sale securities	4,121,084	7,562,793	9,824,754	11,684,016	1,461,004	63,965	34,717,616
- Held-to-maturity securities	298	-	-	-	-	-	298
- Loans and receivables	105,185	661,988	916,891	-	-	-	1,684,064
Investment in subsidiaries	-	-	-	-	-	8,171,067	8,171,067
Investment properties	-	-	-	-	-	1,126,510	1,126,510
Properties, plant and equipment	-	-	-	-	-	6,191,967	6,191,967
Other assets	-	-	-	-	-	3,532,439	3,532,439
Total assets	97,542,957	24,447,862	21,124,315	13,779,607	1,467,288	20,709,272	179,071,301
Liabilities							
Deposits and balances of banks and other financial institutions	4,198,955	561,061	1,096,468	-	-	1,631,807	7,488,291
Financial liabilities at fair value through profit or loss	701,490	1,727,292	2,004,954	-	-	-	4,433,736
Derivative financial instruments	-	-	-	-	-	248,314	248,314
Deposits from customers	86,849,459	18,627,211	16,800,148	993,900	-	8,453,868	131,724,586
Other accounts and provisions (including current and deferred tax liabilities)	438,109	-	-	-	-	4,804,060	5,242,169
Total liabilities	92,188,013	20,915,564	19,901,570	993,900	-	15,138,049	149,137,096
Interest sensitivity gap	5,354,944	3,532,298	1,222,745	12,785,707	1,467,288	5,571,223	29,934,205

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk

Liquidity risk is the risk that banks fail to provide sufficient funds to grow assets or pay due obligations, and need to bear an unacceptable loss. The Group follows sound liquidity risk appetite, to provide stable, reliable and adequate sources of cash to meet liquidity needs under normal circumstances or stressed scenarios; and to survive with net positive cumulative cash flow in extreme scenarios, without requesting HKMA to act as the lender of last resort.

The Group's liquidity risk management objective is to effectively manage the liquidity of on- and off-balance sheet items with reasonable cost based on the liquidity risk appetite to achieve sound operation and sustainable profitability. Customer deposits are the Group’s primary source of funds. To ensure stable and sufficient source of funds are in place, the Group actively attracts new deposits, keeps the core deposit and obtains supplementary funding from the interbank market. According to different term maturities and the results of funding needs estimated from stressed scenarios, the Group adjusts its asset structure (including loans, bonds investment, interbank placement, etc.) to maintain sufficient liquid assets which provides adequate funds in support of normal business needs and ensure its ability to raise funds at a reasonable cost to serve external claims in case of emergency. The Group is committed to diversify the source of funds and the use of funds to avoid excessive concentration of assets and liabilities and prevent triggering liquidity risk due to the break of funding strand when problem occurred in one concentrated funding source. The Group has established intragroup liquidity risk management guideline to manage the liquidity funding among different entities within the Group, and to restrict their reliance of funding on each other. The Group also pays attention to manage liquidity risk created by off-balance sheet activities, such as loan commitments and derivatives. The Group has overall liquidity risk management strategy to cover the liquidity management of foreign currency assets and liabilities, collaterals, intra-day liquidity, intra-group liquidity, the liquidity risk arising from other risks, etc., and has formulated corresponding contingency plan.

Risk Management Committee is the decision-making authority of liquidity risk management, and assumes the ultimate responsibility of liquidity risk management. As authorised by Risk Management Committee, Asset and Liability Management Committee exercises its oversight of liquidity risk and ensures the daily operations of the Group are in accordance with risk appetite and policies as set by Risk Management Committee. Financial Management Division is responsible for overseeing the Group’s liquidity risk. It cooperates with the Treasury Division to assist the Asset and Liability Management Committee to perform liquidity management functions according to their specific responsibilities.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

The Group established liquidity risk management indicators and limits to identify, measure, monitor and control liquidity risk on daily basis. Such indicators and limits include, but are not limited to liquidity ratio, loan-to-deposit ratio, Maximum Cumulative Cash Outflow ("MCO") and liquidity buffer asset portfolio. The Group applies cash flow analysis to assess the Group's liquidity condition under normal conditions and also performs liquidity stress test (including institution specific crisis, general market crisis and combined crisis) at least on monthly basis to assess the Group's capability to withstand various severe liquidity crises. Also, Assets and Liabilities Management System is developed to provide data and generate regular management reports facilitating the liquidity risk management duties.

In accordance with the requirements of Supervisory Policy Manual LM-2 "Sound Systems and Controls for Liquidity Risk Management" issued by the HKMA in 2011, the Group has implemented in 2013 the refinements on the behaviour model and assumptions of cash flow analysis and stress test to enhance the Group's cash flow analysis under both normal and stressed conditions. In cash flow analysis under normal circumstances, refinements have been made to assumptions relating to on-balance sheet items (such as customer deposits) and off-balance sheet items (such as loan commitments). According to various characteristics of the assets, liabilities and off-balance sheet items, the Group forecasts the future cash flow based on contractual maturity date and the assumptions of customer behaviour and balance sheet changes. The Group establishes MCO indicator which predicts the future 30 days maximum cumulative net cash outflow in normal situations based on the above assumptions, to assess if the Group has sufficient financing capacity to meet the cash flow gap in order to achieve the objective of continuing operation. As at 31 December 2014, before taking the cash inflow through the sale of outstanding marketable securities into consideration, the Bank's 30 day cumulative cash flow was a net cash inflow, amounting to HK$4,424,474,000 (2013: HK$4,658,471,000), and was in compliant with the internal limit requirements.

In liquidity stress test, a new combined scenario which is a combination of institution specific and general market crisis has been set up in 2013 to assess the Group's capability to withstand a more severe liquidity crisis, with a more stringent set of assumptions being adopted. Stress test assumptions include the run-off rate of retail, wholesale and interbank deposits; drawdown rate of loan commitments and trade-related contingent liabilities; delinquency ratio and rollover rate of customer loan; and haircut of interbank placement and marketable securities. As at 31 December 2014, the Group was able to maintain a positive cash flow under the three stressed scenarios, indicating the Group has the ability to meet financing needs under stressed conditions. In addition, the Group has a policy in place to maintain an asset buffer portfolio which includes high quality or comparable quality marketable securities issued or guaranteed by sovereigns, central banks, public sector entities or multilateral development banks with 0% or 20% risk weight or non-financial corporate issued or guaranteed marketable securities with a corresponding external credit rating of A- or above (adopt corresponding internal rating if external credit rating is unavailable) to ensure funding needs even under stressed scenarios, as at 31 December 2014, the liquidity cushion (before haircut) was HK$20,399,765,000. A contingency funding plan is established which details the conditions to trigger the plan based on stress test results and early warning indicators, the action plans and relevant procedures and responsibility of various departments.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

In certain derivative contracts, counterparties have the right to request the Group for additional collateral if they have credit concerns on the Group's creditworthiness.

The Group's liquidity risk management also covers new product or business development. Before launching a new product or business, the relevant departments are required to go through a risk assessment process, which includes the assessment of underlying liquidity risk and consideration of the adequacy of the current risk management mechanism. Any material impact on liquidity risk noted during the risk assessment process will be reported to Risk Management Committee for approval.

The Group has established a set of uniform liquidity risk management policies. The principal banking subsidiary develops its own liquidity management policies according to its own characteristics, assumes its own liquidity risk management responsibility, executes its daily risk management processes independently, and reports to the Group's Management on a regular basis.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

(A) Liquidity ratio

	2014	2013
Average liquidity ratio	**51.99%**	47.80%

The average liquidity ratio is calculated as the simple average of each calendar month's average liquidity ratio of Bank for the year.

The liquidity ratio is computed on the solo basis (the Hong Kong offices only) and is in accordance with the Fourth Schedule to the Banking Ordinance.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

(B) Maturity analysis

The tables below analyse the Group's and the Bank's assets and liabilities as at 31 December into relevant maturity groupings based on the remaining period at balance sheet date to the contractual maturity date.

	The Group							
	2014							
	On demand	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Indefinite	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets								
Cash and balances with banks and other financial institutions	25,068,696	21,881,782	-	-	-	-	11,332,322	58,282,800
Placements with banks and other financial institutions maturing between one and twelve months	-	-	9,477,006	8,703,756	-	-	-	18,180,762
Financial assets at fair value through profit or loss								
– held for trading								
- debt securities	-	470,000	2,671,893	2,757,401	-	-	-	5,899,294
– designated at fair value through profit or loss								
- debt securities	-	-	-	2,170	253,749	-	-	255,919
Derivative financial instruments	352,831	18,163	18,247	46,452	3,379	-	-	439,072
Advances and other accounts								
– advances to customers	5,600,078	9,742,952	16,597,492	36,208,391	52,393,120	26,179,173	810,930	147,532,136
– trade bills	32,219	4,961,240	7,500,572	3,877,532	-	-	-	16,371,563
Investment in securities								
– available-for-sale								
- certificates of deposit	-	71,704	1,121,059	5,071,150	1,633,772	-	-	7,897,685
- debt securities	-	1,282,624	6,181,988	8,984,351	17,486,963	565,963	-	34,501,889
– held-to-maturity								
- debt securities	-	-	1,415	644	1,996,697	619,634	-	2,618,390
– loans and receivables								
- debt securities	-	-	620,262	1,454,332	-	-	-	2,074,594
– equity securities	-	-	-	-	-	-	75,766	75,766
Investment properties	-	-	-	-	-	-	1,280,271	1,280,271
Properties, plant and equipment	-	-	-	-	-	-	7,328,497	7,328,497
Other assets (including deferred tax assets)	185,402	779,942	3,202	47,394	139,094	46	10,535	1,165,615
Total assets	31,239,226	39,208,407	44,193,136	67,153,573	73,906,774	27,364,816	20,838,321	303,904,253

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

(B) Maturity analysis (continued)

	The Group							
	2014							
	On demand	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Indefinite	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Liabilities								
Deposits and balances from banks and other financial institutions	2,649,041	17,702,866	9,332,830	8,050,874	-	-	-	37,735,611
Financial liabilities at fair value through profit or loss	-	1,978,491	873,945	2,118,257	-	-	-	4,970,693
Derivative financial instruments	98,057	86,204	30,223	32,269	31,753	-	-	278,506
Deposits from customers	75,443,820	54,407,895	35,397,115	34,231,783	10,153,322	-	-	209,633,935
Other accounts and provisions (including current and deferred tax liabilities)	4,834,848	3,156,033	2,893,494	4,333,573	1,171,922	794	-	16,390,664
Total liabilities	83,025,766	77,331,489	48,527,607	48,766,756	11,356,997	794	-	269,009,409
Net liquidity gap	(51,786,540)	(38,123,082)	(4,334,471)	18,386,817	62,549,777	27,364,022	20,838,321	34,894,844

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

(B) Maturity analysis (continued)

	The Group							
	2013							
	On demand	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Indefinite	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets								
Cash and balances with banks and other financial institutions	19,625,303	12,929,170	-	-	-	-	12,184,846	44,739,319
Placements with banks and other financial institutions maturing between one and twelve months	-	-	10,324,490	11,019,510	-	-	-	21,344,000
Financial assets at fair value through profit or loss								
– held for trading								
- debt securities	-	296,487	704,859	2,664,066	624	-	-	3,666,036
– designated at fair value through profit or loss								
- debt securities	-	-	-	240,097	258,560	-	-	498,657
Derivative financial instruments	345,025	55,479	16,455	90,390	1,104	-	-	508,453
Advances and other accounts								
– advances to customers	5,317,238	8,893,638	12,414,991	39,468,912	46,982,868	28,731,200	265,268	142,074,115
– trade bills	1,078	2,482,327	4,693,586	6,065,645	-	-	-	13,242,636
Investment in securities								
– available-for-sale								
- certificates of deposit	-	6,064	899,663	6,044,492	726,666	-	-	7,676,885
- debt securities	-	2,482,919	2,569,203	5,167,277	20,598,317	1,444,071	-	32,261,787
– held-to-maturity								
- debt securities	-	-	-	585,144	298	-	-	585,442
– loans and receivables								
- debt securities	-	105,185	661,988	916,891	-	-	-	1,684,064
– equity securities	-	-	-	-	-	-	63,965	63,965
Investment properties	-	-	-	-	-	-	1,174,938	1,174,938
Properties, plant and equipment	-	-	-	-	-	-	6,969,237	6,969,237
Other assets (including deferred tax assets)	152,748	3,519,657	13,437	90,958	76,003	380	41,243	3,894,426
Total assets	25,441,392	30,770,926	32,298,672	72,353,382	68,644,440	30,175,651	20,699,497	280,383,960

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

(B) Maturity analysis (continued)

	The Group							
	2013							
	On demand	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Indefinite	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Liabilities								
Deposits and balances from banks and other financial institutions	2,303,726	14,457,112	3,306,414	8,778,777	-	-	-	28,846,029
Financial liabilities at fair value through profit or loss	-	701,490	1,727,292	2,004,954	-	-	-	4,433,736
Derivative financial instruments	94,553	85,890	34,974	70,803	56,936	-	-	343,156
Deposits from customers	72,261,365	45,965,432	29,462,615	38,560,815	11,871,133	39,057	-	198,160,417
Other accounts and provisions (including current and deferred tax liabilities)	2,755,008	4,962,292	2,901,823	4,361,272	1,309,372	10,866	-	16,300,633
Total liabilities	77,414,652	66,172,216	37,433,118	53,776,621	13,237,441	49,923	-	248,083,971
Net liquidity gap	(51,973,260)	(35,401,290)	(5,134,446)	18,576,761	55,406,999	30,125,728	20,699,497	32,299,989

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

(B) Maturity analysis (continued)

	The Bank							
	2014							
	On demand	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Indefinite	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets								
Cash and balances with banks and other financial institutions	20,075,025	10,316,516	-	-	-	-	-	30,391,541
Placements with banks and other financial institutions maturing between one and twelve months	-	-	145,422	-	-	-	-	145,422
Financial assets at fair value through profit or loss								
– held for trading								
- debt securities	-	470,000	2,671,893	2,757,401	-	-	-	5,899,294
– designated at fair value through profit or loss								
- debt securities	-	-	-	2,170	253,749	-	-	255,919
Derivative financial instruments	351,637	13,166	12,983	24,710	268	-	-	402,764
Advances and other accounts								
– advances to customers	5,551,541	5,813,882	10,058,854	18,632,217	42,676,748	15,792,018	601,695	99,126,955
– trade bills	249	1,456,575	2,913,644	2,868,135	-	-	-	7,238,603
Investment in securities								
– available-for-sale								
- certificates of deposit	-	71,704	1,121,059	5,071,150	1,633,772	-	-	7,897,685
- debt securities	-	1,282,624	6,040,410	7,454,830	12,093,122	-	-	26,870,986
– held-to-maturity								
- debt securities	-	-	1,415	644	241,391	-	-	243,450
– loans and receivables								
- debt securities	-	-	620,262	1,454,332	-	-	-	2,074,594
– equity securities	-	-	-	-	-	-	75,766	75,766
Investment in subsidiaries	-	-	-	-	-	-	8,171,067	8,171,067
Investment properties	-	-	-	-	-	-	1,258,121	1,258,121
Properties, plant and equipment	-	-	-	-	-	-	6,579,145	6,579,145
Other assets	19,092	758,476	105	1,598	333	-	2,944	782,548
Total assets	25,997,544	20,182,943	23,586,047	38,267,187	56,899,383	15,792,018	16,688,738	197,413,860

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

(B) Maturity analysis (continued)

	The Bank							
	2014							
	On demand	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Indefinite	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Liabilities								
Deposits and balances from banks and other financial institutions	**2,852,772**	**5,445,958**	**1,044,267**	**1,026,372**	**-**	**-**	**-**	**10,369,369**
Financial liabilities at fair value through profit or loss	**-**	**1,978,491**	**873,945**	**2,118,257**	**-**	**-**	**-**	**4,970,693**
Derivative financial instruments	**97,061**	**18,375**	**8,571**	**14,267**	**29,120**	**-**	**-**	**167,394**
Deposits from customers	**57,795,082**	**46,836,801**	**27,078,634**	**13,140,275**	**1,019,835**	**-**	**-**	**145,870,627**
Other accounts and provisions (including current and deferred tax liabilities)	**1,601,932**	**742,322**	**95,001**	**177,917**	**968,411**	**-**	**-**	**3,585,583**
Total liabilities	**62,346,847**	**55,021,947**	**29,100,418**	**16,477,088**	**2,017,366**	**-**	**-**	**164,963,666**
Net liquidity gap	**(36,349,303)**	**(34,839,004)**	**(5,514,371)**	**21,790,099**	**54,882,017**	**15,792,018**	**16,688,738**	**32,450,194**

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

(B) Maturity analysis (continued)

	The Bank							
	2013							
	On demand	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Indefinite	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets								
Cash and balances with banks and other financial institutions	15,427,036	3,413,298	-	-	-	-	-	18,840,334
Placements with banks and other financial institutions maturing between one and twelve months	-	-	1,527,931	330,331	-	-	-	1,858,262
Financial assets at fair value through profit or loss								
– held for trading								
- debt securities	-	296,487	704,859	2,664,066	624	-	-	3,666,036
– designated at fair value through profit or loss								
- debt securities	-	-	-	240,097	258,560	-	-	498,657
Derivative financial instruments	345,025	41,713	2,712	20,638	346	-	-	410,434
Advances and other accounts								
– advances to customers	4,796,737	7,448,303	7,460,242	15,953,432	37,099,624	16,047,873	109,387	88,915,598
– trade bills	1,078	1,544,684	3,152,502	4,759,755	-	-	-	9,458,019
Investment in securities								
– available-for-sale								
- certificates of deposit	-	6,064	899,663	6,044,492	726,666	-	-	7,676,885
- debt securities	-	2,482,919	2,516,773	4,793,767	15,739,236	1,444,071	-	26,976,766
– held-to-maturity								
- debt securities	-	-	-	-	298	-	-	298
– loans and receivables								
- debt securities	-	105,185	661,988	916,891	-	-	-	1,684,064
– equity securities	-	-	-	-	-	-	63,965	63,965
Investment in subsidiaries	-	-	-	-	-	-	8,171,067	8,171,067
Investment properties	-	-	-	-	-	-	1,126,510	1,126,510
Properties, plant and equipment	-	-	-	-	-	-	6,191,967	6,191,967
Other assets	17,129	3,482,064	845	2,305	360	-	29,736	3,532,439
Total assets	20,587,005	18,820,717	16,927,515	35,725,774	53,825,714	17,491,944	15,692,632	179,071,301

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

(B) Maturity analysis (continued)

	The Bank							
	2013							
	On demand	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Indefinite	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Liabilities								
Deposits and balances from banks and other financial institutions	2,421,609	3,409,153	561,061	1,096,468	-	-	-	7,488,291
Financial liabilities at fair value through profit or loss	-	701,490	1,727,292	2,004,954	-	-	-	4,433,736
Derivative financial instruments	94,553	68,659	11,159	17,512	56,431	-	-	248,314
Deposits from customers	57,481,019	37,739,386	18,559,824	16,950,467	993,890	-	-	131,724,586
Other accounts and provisions (including current and deferred tax liabilities)	1,146,948	2,996,225	89,274	120,325	889,397	-	-	5,242,169
Total liabilities	61,144,129	44,914,913	20,948,610	20,189,726	1,939,718	-	-	149,137,096
Net liquidity gap	(40,557,124)	(26,094,196)	(4,021,095)	15,536,048	51,885,996	17,491,944	15,692,632	29,934,205

The above maturity classifications have been prepared in accordance with relevant provisions under the Banking (Disclosure) Rules. The Group has reported assets such as advances and debt securities which have been overdue for not more than one month as "On demand". In the case of an asset that is repayable by different payments or instalments, only that portion of the asset that is actually overdue is reported as overdue. Any part of the asset that is not due is reported according to the residual maturity unless the repayment of the asset is in doubt in which case the amount is reported as "Indefinite". The above assets are stated after deduction of provisions, if any.

The analysis of debt securities by remaining period to maturity is disclosed in order to comply with relevant provisions under the Banking (Disclosure) Rules. The disclosure does not imply that the securities will be held to maturity.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities

(a) Non-derivative cash flows

The tables below summarise the cash flows of the Group and the Bank as at 31 December for non-derivative financial liabilities by remaining contractual maturities.

	The Group					
	2014					
	Up to 1 month	**1 to 3 months**	**3 to 12 months**	**1 to 5 years**	**Over 5 years**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
Financial liabilities						
Deposits and balances from banks and other financial institutions	**20,388,137**	**9,396,895**	**8,182,134**	**-**	**-**	**37,967,166**
Financial liabilities at fair value through profit or loss	**1,978,500**	**874,000**	**2,119,000**	**-**	**-**	**4,971,500**
Deposits from customers	**129,885,722**	**35,519,941**	**34,833,788**	**11,008,039**	**-**	**211,247,490**
Other financial liabilities	**7,636,441**	**2,688,501**	**4,078,030**	**194,912**	**794**	**14,598,678**
Total financial liabilities	**159,888,800**	**48,479,337**	**49,212,952**	**11,202,951**	**794**	**268,784,834**

	The Group					
	2013					
	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Financial liabilities						
Deposits and balances from banks and other financial institutions	16,778,992	3,341,129	8,942,010	-	-	29,062,131
Financial liabilities at fair value through profit or loss	701,500	1,727,500	2,006,500	-	-	4,435,500
Deposits from customers	118,257,428	29,568,037	39,248,181	13,029,817	51,735	200,155,198
Other financial liabilities	7,599,320	2,657,072	4,241,374	411,167	10,867	14,919,800
Total financial liabilities	143,337,240	37,293,738	54,438,065	13,440,984	62,602	248,572,629

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities (continued)

(a) Non-derivative cash flows (continued)

	The Bank					
	2014					
	Up to 1 month	**1 to 3 months**	**3 to 12 months**	**1 to 5 years**	**Over 5 years**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
Financial liabilities						
Deposits and balances from banks and other financial institutions	**8,300,889**	**1,049,403**	**1,037,616**	**-**	**-**	**10,387,908**
Financial liabilities at fair value through profit or loss	**1,978,500**	**874,000**	**2,119,000**	**-**	**-**	**4,971,500**
Deposits from customers	**104,651,546**	**27,152,527**	**13,265,976**	**1,036,651**	**-**	**146,106,700**
Other financial liabilities	**2,341,047**	**199**	**-**	**-**	**-**	**2,341,246**
Total financial liabilities	**117,271,982**	**29,076,129**	**16,422,592**	**1,036,651**	**-**	**163,807,354**

	The Bank					
	2013					
	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Financial liabilities						
Deposits and balances from banks and other financial institutions	5,831,713	563,102	1,097,739	-	-	7,492,554
Financial liabilities at fair value through profit or loss	701,500	1,727,500	2,006,500	-	-	4,435,500
Deposits from customers	95,238,323	18,603,469	17,118,139	1,044,047	-	132,003,978
Other financial liabilities	4,141,243	2,006	427	-	-	4,143,676
Total financial liabilities	105,912,779	20,896,077	20,222,805	1,044,047	-	148,075,708

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities (continued)

(b) Derivative cash flows

The tables below summarise the cash flows of the Group and the Bank by remaining contractual maturities as at 31 December for derivative financial liabilities that will be settled on a net basis, together with all derivative financial instruments that will be settled on a gross basis regardless of whether the contract is in an asset or liability position. The amounts disclosed in the tables are the contractual undiscounted cash flows, except for certain derivatives which are disclosed at fair value.

The Group's derivative financial instruments that will be settled on a net basis mainly include interest rate swaps whereas derivative financial instruments that will be settled on a gross basis mainly include currency forwards and currency swaps.

	The Group					
	2014					
	Up to 1 month	**1 to 3 months**	**3 to 12 months**	**1 to 5 years**	**Over 5 years**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
Derivative financial liabilities settled on a net basis	**(100,241)**	**(9,011)**	**(25,332)**	**(15,614)**	**-**	**(150,198)**
Derivative financial instruments settled on a gross basis						
Total inflow	**20,417,338**	**6,924,041**	**11,252,454**	**834,845**	**-**	**39,428,678**
Total outflow	**(20,719,023)**	**(6,952,942)**	**(11,370,225)**	**(834,202)**	**-**	**(39,876,392)**

	The Group					
	2013					
	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Derivative financial liabilities settled on a net basis	(98,868)	(15,176)	(67,761)	(30,561)	-	(212,366)
Derivative financial instruments settled on a gross basis						
Total inflow	23,866,437	4,369,915	9,679,171	180,102	-	38,095,625
Total outflow	(23,897,683)	(4,397,226)	(9,657,460)	(179,071)	-	(38,131,440)

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.3 Liquidity Risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities (continued)

(b) Derivative cash flows (continued)

	The Bank					
	2014					
	Up to 1 month	**1 to 3 months**	**3 to 12 months**	**1 to 5 years**	**Over 5 years**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
Derivative financial liabilities settled on a net basis	**(97,317)**	**(5,379)**	**(13,815)**	**(15,312)**	**-**	**(131,823)**
Derivative financial instruments settled on a gross basis						
Total inflow	**12,429,030**	**4,586,773**	**7,147,431**	**77,472**	**-**	**24,240,706**
Total outflow	**(12,435,472)**	**(4,584,822)**	**(7,194,230)**	**(77,357)**	**-**	**(24,291,881)**

	The Bank					
	2013					
	Up to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Derivative financial liabilities settled on a net basis	(94,591)	(5,900)	(26,400)	(30,037)	-	(156,928)
Derivative financial instruments settled on a gross basis						
Total inflow	20,430,976	616,475	2,265,259	43,549	-	23,356,259
Total outflow	(20,456,849)	(625,212)	(2,253,894)	(42,785)	-	(23,378,740)

(c) Off-balance sheet items

Loan commitments

The contractual amounts of the Group's and the Bank's off-balance sheet financial instruments as at 31 December 2014 that the Group and the Bank commit to extend credit to customers and other facilities amounted to HK$74,498,453,000 (2013: HK$76,884,033,000) and HK$30,529,429,000 (2013: HK$26,338,710,000) respectively. Those loan commitments can be drawn within one year.

Financial guarantees and other financial facilities

Financial guarantees and other financial facilities of the Group and the Bank as at 31 December 2014 amounting to HK$38,415,882,000 (2013: HK$33,262,083,000) and HK$3,437,876,000 (2013: HK$4,311,433,000) respectively are maturing no later than one year.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.4 Capital Management

The major objective of the Group's capital management is to maximise total shareholders' return while maintaining a capital adequacy position in relation to the Group's overall risk profile. The Assets and Liability Management Committee periodically reviews the Group's capital structure and adjusts the capital mix where appropriate to maintain an optimal balance among risk, return and capital adequacy.

The Group has developed and maintained a sound framework of policies and controls on capital management to support the development of the Group's business and to meet the statutory capital adequacy ratio. The Assets and Liability Management Committee monitors the Group's capital adequacy. The Group has complied with all the statutory capital requirements of the HKMA for the reported periods in respect of banking operation as further ellaborated below.

The Group has adopted the foundation internal ratings-based ("FIRB") approach to calculate the credit risk capital charge for the majority of its non-securitisation exposures. A small residual credit exposures are remained under the standardised (credit risk) ("STC") approach. The Group has adopted standardised credit valuation adjustment ("CVA") method to calculate the capital charge for the CVA risk of the counterparty.

The Group continues to adopt the internal models ("IMM") approach to calculate the general market risk capital charge for foreign exchange and interest rate exposures and, with the approvals of HKMA, exclude its structural FX positions arising from overseas branches and NCB (China) in the calculation of the market risk capital charge. The Group continues to adopt the standardised (market risk) ("STM") approach to calculate the market risk capital charge for remaining exposures.

The Group continues to adopt standardised (operational risk) ("STO") approach to calculate the capital charge for operational risk.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.4 Capital Management (continued)

The Group has continued to adopt an internal capital adequacy assessment process ("ICAAP") to comply with the HKMA's requirements in the Supervisory Policy Manual "Supervisory Review Process" in 2014. Based on the HKMA's guidelines on Pillar II, ICAAP has been initiated to assess the extra capital needed to cover the material risks not captured or not adequately captured under Pillar I, and therefore minimum Common Equity Tier 1 capital ratio, minimum Tier 1 capital ratio and the minimum Total capital ratio are determined. Meanwhile, operating ranges for the aforementioned capital ratios have also been established which enable the flexibility for future business growth and efficiency of capital utilisation. The Group considers this ICAAP process as an on-going process for capital management and periodically reviews and adjusts its capital structure where appropriate in relation to the overall risk profile.

In addition, the capital plan of the Group is drawn up annually and then submitted to the Board for approval after endorsement of the Assets and Liability Management Committee. The plan is built up by assessing the implications of various factors upon capital adequacy such as the business strategies, return on equity, risk appetite, credit rating, as well as regulatory requirements. Hence, the future capital requirement is determined and capital sources are identified also. The plan is to ensure the Group maintains adequate capital and appropriate capital structure which align with our business development needs thereby achieving an optimal balance among risk, return and capital adequacy.

(A) Basis of regulatory consolidation

The consolidation basis for regulatory purposes comprises the positions of the Bank and certain subsidiaries specified by the HKMA in accordance with the Banking (Capital) Rules. For accounting purposes, subsidiaries are consolidated in accordance with HKFRSs.

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.4 Capital Management (continued)

(A) Basis of regulatory consolidation (continued)

Subsidiaries of Bank are included within the accounting scope of consolidation but not included within the regulatory scope of consolidation are as follows:

	2014		2013	
Name	**Total assets**	**Total equity**	Total assets	Total equity
	HK$'000	**HK$'000**	HK$'000	HK$'000
Nanyang Commercial Bank Trustee Limited	**16,295**	**16,186**	16,869	16,510
Kwong Li Nam Investment Agency Limited	**4,481**	**4,027**	4,168	4,029
Nanyang Commercial Bank (Nominees) Limited	**1,477**	**1,477**	1,483	1,483

There are no subsidiaries which are included within the regulatory scope of consolidation but not included within the accounting scope of consolidation as at 31 December 2014 (2013: Nil).

There are also no subsidiaries which are included within both the accounting scope of consolidation and the regulatory scope of consolidation but the methods of consolidation differ as at 31 December 2014 (2013: Nil).

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.4 Capital Management (continued)

(B) Capital ratio

	2014	2013
CET1 capital ratio	**14.19%**	13.53%
Tier 1 capital ratio	**14.19%**	13.53%
Total capital ratio	**16.55%**	15.80%

(C) Components of capital base after deductions

The consolidated capital base after deductions used in the calculation of the above capital ratios as at 31 December and reported to the HKMA is analysed as follows:

	2014	2013
	HK$'000	HK$'000
CET1 capital: instruments and reserves		
Directly issued qualifying CET1 capital instruments	**3,144,517**	3,144,517
Retained earnings	**22,764,425**	20,879,091
Disclosed reserves	**8,978,910**	8,260,460
CET1 capital before regulatory deductions	**34,887,852**	32,284,068
CET1 capital: regulatory deductions		
Valuation adjustments	**(3,465)**	-
Deferred tax assets net of deferred tax liabilities	**(152,171)**	(152,418)
Gains and losses due to changes in own credit risk on fair valued liabilities	**(877)**	(677)
Cumulative fair value gains arising from the revaluation of land and buildings (own-use and investment properties)	**(6,919,824)**	(6,422,662)
Regulatory reserve for general banking risks	**(2,173,590)**	(1,944,980)
Total regulatory deductions to CET1 capital	**(9,249,927)**	(8,520,737)
CET1 capital	**25,637,925**	23,763,331
Tier 1 capital	**25,637,925**	23,763,331

Notes to the Financial statements (continued)

2. Financial risk management (continued)

2.4 Capital Management (continued)

(C) Components of capital base after deductions (continued)

	2014	2013
	HK$'000	HK$'000
Tier 2 capital: instruments and provisions		
Collective impairment allowances and regulatory reserve for general banking risks eligible for inclusion in Tier 2 capital	**1,155,025**	1,099,587
Tier 2 capital before regulatory deductions	**1,155,025**	1,099,587
Tier 2 capital: regulatory deductions		
Add back of cumulative fair value gains arising from the revaluation of land and buildings (own-use and investment properties) eligible for inclusion in Tier 2 capital	**3,113,921**	2,890,198
Total regulatory deductions to Tier 2 capital	**3,113,921**	2,890,198
Tier 2 capital	**4,268,946**	3,989,785
Total capital	**29,906,871**	27,753,116

To comply with the Banking (Disclosure) Rules, a section "Regulatory Disclosures" is available on the Bank's website at www.ncb.com.hk and includes the following consolidated information of the Bank.

- A detailed breakdown of the capital base and regulatory deductions, using the standard template as specified by the HKMA.
- A reconciliation of capital components to the balance sheet, using the standard template as specified by the HKMA.
- A description of the main features and the full terms and conditions of the issued capital instruments.

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy as defined in HKFRS 13, “Fair value measurement”. The categorisation are determined with reference to the observability and significance of the inputs used in the valuation methods and based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1: based on quoted prices (unadjusted) in active markets for identical assets or liabilities. This category includes certain exchange-traded derivative contracts.
- Level 2: based on valuation techniques for which the lowest level input that is significant to the fair value measurement is observable, either directly or indirectly. This category includes majority of the over-the-counter (“OTC”) derivative contracts, debt securities and certificates of deposit with quote from pricing services vendors. It also includes precious metals and properties with insignificant adjustments made to observable market inputs.
- Level 3: based on valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable. This category includes equity investment and certificates of deposit with significant unobservable components. It also includes properties with significant adjustments made to observable market inputs.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by reassessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

3.1 Financial instruments measured at fair value

The Group has an established governance structure and controls framework to ensure that fair values are either determined or validated by control units independent of the front offices. Control units have overall responsibility for independent verification of valuation results from front line businesses and all other significant fair value measurements. Specific controls include verification of observable pricing inputs. Significant valuation issues are reported to the Management.

The Group uses valuation techniques or broker/dealer quotations to determine the fair value of financial instruments when unable to obtain the open market quotation in active markets.

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities (continued)

3.1 Financial instruments measured at fair value (continued)

The main parameters used in valuation techniques for financial instruments held by the Group include bond prices, interest rates, foreign exchange rates, equity and stock prices, volatilities, counterparty credit spreads and others, which are mostly observable and obtainable from open market.

The technique used to calculate the fair value of the following financial instruments is as below:

Debt securities and certificates of deposit

The fair value of these instruments is determined by obtaining quoted market prices from exchange, dealer or independent pricing service vendors or using discounted cash flow technique. Discounted cash flow model is a valuation technique that measures present value using estimated expected future cash flows from the instruments and then discounts these flows using a discount rate or discount margin that reflects the credit spreads required by the market for instruments with similar risk. These inputs are observable or can be corroborated by observable or unobservable market data.

Asset backed securities

For this class of instruments, external prices are obtained from independent third parties.

Derivatives

OTC derivative contracts include forward, swap and option contracts on foreign exchange, interest rate, equity or commodity. The fair values of these contracts are mainly measured using valuation techniques such as discounted cash flow models and option pricing models. The inputs can be observable or unobservable market data. Observable inputs include interest rate, foreign exchange rates, equity and stock prices, commodity prices and volatilities.

Credit valuation adjustments (“CVA”) and debit valuation adjustments (“DVA”) are applied to the Group’s OTC derivatives. These adjustments reflect interest rates, expectations of counterparty creditworthiness and the Group’s own credit spread respectively. They are determined for each counterparty and are dependent on expected future values of exposures, default probabilities and recovery rates.

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities (continued)

3.1 Financial instruments measured at fair value (continued)

(A) Fair value hierarchy

	The Group			
	2014			
	Level 1	**Level 2**	**Level 3**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Financial assets				
Financial assets at fair value through profit or loss				
- Trading securities				
- Debt securities	**-**	**5,899,294**	**-**	**5,899,294**
- Financial assets designated at fair value through profit or loss				
- Debt securities	**-**	**255,919**	**-**	**255,919**
Derivative financial instruments	**352,831**	**86,237**	**4**	**439,072**
Available-for-sale securities				
- Debt securities	**-**	**34,501,889**	**-**	**34,501,889**
- Certificates of deposit	**-**	**7,897,685**	**-**	**7,897,685**
- Equity securities	**-**	**-**	**75,766**	**75,766**
Financial liabilities				
Financial liabilities at fair value through profit or loss				
- Trading liabilities	**-**	**4,970,693**	**-**	**4,970,693**
Derivative financial instruments	**98,057**	**180,421**	**28**	**278,506**

	The Group			
	2013			
	Level 1	Level 2	Level 3	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Financial assets				
Financial assets at fair value through profit or loss				
- Trading securities				
- Debt securities	-	3,666,036	-	3,666,036
- Financial assets designated at fair value through profit or loss				
- Debt securities	-	498,657	-	498,657
Derivative financial instruments	345,027	163,426	-	508,453
Available-for-sale securities				
- Debt securities	-	32,261,787	-	32,261,787
- Certificates of deposit	-	5,540,037	2,136,848	7,676,885
- Equity securities	-	-	63,965	63,965
Financial liabilities				
Financial liabilities at fair value through profit or loss				
- Trading liabilities	-	4,433,736	-	4,433,736
Derivative financial instruments	94,553	248,603	-	343,156

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities (continued)

3.1 Financial instruments measured at fair value (continued)

(A) Fair value hierarchy (continued)

	The Bank			
	2014			
	Level 1	**Level 2**	**Level 3**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Financial assets				
Financial assets at fair value through profit or loss				
- Trading securities				
- Debt securities	**-**	**5,899,294**	**-**	**5,899,294**
- Financial assets designated at fair value through profit or loss				
- Debt securities	**-**	**255,919**	**-**	**255,919**
Derivative financial instruments	**351,637**	**51,127**	**-**	**402,764**
Available-for-sale securities				
- Debt securities	**-**	**26,870,986**	**-**	**26,870,986**
- Certificates of deposit	**-**	**7,897,685**	**-**	**7,897,685**
- Equity securities	**-**	**-**	**75,766**	**75,766**
Financial liabilities				
Financial liabilities at fair value through profit or loss				
- Trading liabilities	**-**	**4,970,693**	**-**	**4,970,693**
Derivative financial instruments	**97,061**	**70,333**	**-**	**167,394**

	The Bank			
	2013			
	Level 1	Level 2	Level 3	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Financial assets				
Financial assets at fair value through profit or loss				
- Trading securities				
- Debt securities	-	3,666,036	-	3,666,036
- Financial assets designated at fair value through profit or loss				
- Debt securities	-	498,657	-	498,657
Derivative financial instruments	345,027	65,407	-	410,434
Available-for-sale securities				
- Debt securities	-	26,976,766	-	26,976,766
- Certificates of deposit	-	5,540,037	2,136,848	7,676,885
- Equity securities	-	-	63,965	63,965
Financial liabilities				
Financial liabilities at fair value through profit or loss				
- Trading liabilities	-	4,433,736	-	4,433,736
Derivative financial instruments	94,553	153,761	-	248,314

There were no financial asset and liability transfers between level 1 and level 2 for the Group during the year (2013: Nil).

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities (continued)

3.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items

	The Group		
	2014		
	Derivative financial instruments (net)	Financial assets – Available-for-sale securities – Certificates of deposit	Financial assets – Available-for-sale securities – Equity securities
	HK$'000	HK$'000	HK$'000
At 1 January 2014	-	2,136,848	63,965
Gains			
- Income statement	4	-	-
- Other comprehensive income	-	660	11,801
Sales	-	(2,057,390)	-
Transfers out of level 3	-	(80,118)	-
At 31 December 2014	4	-	75,766
Total unrealised gain for the year included in income statement for financial assets held as at 31 December 2014	4	-	-

	The Bank		
	2014		
	Derivative financial instruments (net)	Financial assets – Available-for-sale securities – Certificates of deposit	Financial assets – Available-for-sale securities – Equity securities
	HK$'000	HK$'000	HK$'000
At 1 January 2014	-	2,136,848	63,965
Gains			
- Other comprehensive income	-	660	11,801
Sales	-	(2,057,390)	-
Transfers out of level 3	-	(80,118)	-
At 31 December 2014	-	-	75,766
Total unrealised gain for the year included in income statement for financial assets held as at 31 December 2014	-	-	-

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities (continued)

3.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items (continued)

	The Group and the Bank		
	2013		
	Derivative financial instruments (net)	Financial assets Available-for-sale securities Certificates of deposit	Equity securities
	HK$'000	HK$'000	HK$'000
At 1 January 2013	-	-	56,146
Gains			
- Other comprehensive income	-	-	7,819
Purchases	-	1,976,386	-
Transfers into level 3	-	160,462	-
At 31 December 2013	-	2,136,848	63,965
Total unrealised gain for the year included in income statement for financial assets held as at 31 December 2013	-	-	-

As at 31 December 2014 and 2013, financial instruments categorised as level 3 are mainly comprised of certificates of deposit and unlisted equity shares.

Certificates of deposit were transferred into and out of level 3 in the year of 2014 and 2013 due to change of valuation observability. For certain illiquid certificates of deposit, the Group obtains valuation quotations from counterparties which may be based on unobservable inputs with significant impact on the valuation. Therefore, these instruments have been classified by the Group as level 3. The Group has established internal control procedures to control the Group's exposure to such financial instruments.

The fair values of unlisted available-for-sale equity shares are determined with reference to multiples of comparable listed companies, such as average of the price/earning ratios of comparables or net asset value, if appropriate comparables are not available. The fair value is positively correlated to the price/earning ratios of appropriate comparables or net asset values. Had the net asset value of the underlying equity investments increased/decreased by 5%, the Group's other comprehensive income would have increased/decreased by HK$3,788,000 (2013: HK$3,198,000).

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities (continued)

3.2 Financial instruments not measured at fair value

Fair value estimates are made at a specific point in time based on relevant market information and information about various financial instruments. The following methods and assumptions have been used to estimate the fair value of each class of financial instrument as far as practicable.

Balances with/from banks and other financial institutions and trade bills

Substantially all the financial assets and liabilities mature within one year from the balance sheet date and their carrying value approximates fair value.

Advances to customers

Substantially all the advances to customers are on floating rate terms, bear interest at prevailing market interest rates and their carrying value approximates fair value.

Held-to-maturity securities

The fair value of held-to-maturity securities is determined by using the same approach as those debt securities and certificates of deposit and asset backed securities measured at fair value as described in Note 3.1.

Loans and receivables

The fair value of loans and receivable is determined by using the same approach as those debt securities as described in Note 3.1.

Deposits from customers

Substantially all the deposits from customers mature within one year from the balance sheet date and their carrying value approximates fair value.

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities (continued)

3.2 Financial instruments not measured at fair value (continued)

The following tables set out the carrying values and fair values of the financial instruments not measured at fair value, except for the above with their carrying values being approximation of fair values.

	The Group			
	2014		2013	
	Carrying value	**Fair value**	Carrying value	Fair value
	HK$'000	**HK$'000**	HK$'000	HK$'000
Financial assets				
Held-to-maturity securities				
- Debt securities	**2,618,390**	**2,668,585**	585,442	583,975
Loans and receivables	**2,074,594**	**2,072,809**	1,684,064	1,679,326

	The Bank			
	2014		2013	
	Carrying value	**Fair value**	Carrying value	Fair value
	HK$'000	**HK$'000**	HK$'000	HK$'000
Financial assets				
Held-to-maturity securities				
- Debt securities	**243,450**	**246,232**	298	295
Loans and receivables	**2,074,594**	**2,072,809**	1,684,064	1,679,326

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities (continued)

3.2 Financial instruments not measured at fair value (continued)

The following tables show the fair value hierarchy for financial instruments with fair values disclosed.

	The Group			
	2014			
	Level 1	**Level 2**	**Level 3**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Financial assets				
Held-to-maturity securities				
- Debt securities	**-**	**2,668,585**	**-**	**2,668,585**
Loans and receivables	**-**	**2,072,809**	**-**	**2,072,809**

	The Group			
	2013			
	Level 1	Level 2	Level 3	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Financial assets				
Held-to-maturity securities				
- Debt securities	-	583,680	295	583,975
Loans and receivables	-	1,679,326	-	1,679,326

	The Bank			
	2014			
	Level 1	**Level 2**	**Level 3**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Financial assets				
Held-to-maturity securities				
- Debt securities	**-**	**246,232**	**-**	**246,232**
Loans and receivables	**-**	**2,072,809**	**-**	**2,072,809**

	The Bank			
	2013			
	Level 1	Level 2	Level 3	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Financial assets				
Held-to-maturity securities				
- Debt securities	-	-	295	295
Loans and receivables	-	1,679,326	-	1,679,326

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities (continued)

3.3 Non-financial instruments measured at fair value

The Group uses valuation techniques or quoted market prices in active market to determine the fair value of non-financial instruments.

Investment properties and premises

The Group's properties can be divided into investment properties and premises. All of the Group's investment properties and premises were revalued as at year end. The valuations were carried out by an independent firm of chartered surveyors, Savills Valuation and Professional Services Limited, who have among their staff Fellow and Members of The Hong Kong Institute of Surveyors with recent experience in the locations and categories of properties being valued. The Group's Management had discussions with the surveyors on the valuation methods, valuation assumptions and valuation results when the valuation is performed at each interim and annual reporting date. There has been no change in valuation methods during the year.

Valuation methods and inputs used in Level 2 fair value measurements

The fair value of properties classified as Level 2 is determined using either the market comparison approach by reference to recent sales price of comparable properties or the income capitalisation approach by reference to market rent and capitalisation rate, with appropriate adjustments to reflect the differences between the comparable properties and the subject properties. These adjustments are considered as insignificant to the entire measurement.

The Group's properties are located in Hong Kong and major cities in the PRC where the property markets are considered active and transparent. Sales price, market rent and capitalisation rate of comparable properties are generally observable either directly or indirectly in these markets.

Information about Level 3 fair value measurements

The fair value of all of the Group's properties classified as Level 3 is determined using either the market comparison approach or the income capitalisation approach, adjusted for a premium or a discount specific to the features of the Group's properties compared to the comparable properties.

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities (continued)

3.3 Non-financial instruments measured at fair value (continued)

Investment properties and premises (continued)

The valuation methods and significant unobservable inputs used in the fair value measurement of the Group's properties classified as Level 3 are as follows:

	Valuation method	Significant unobservable inputs	Weighted average	Relationship of unobservable inputs to fair value
Other properties	Market comparison approach or income capitalisation approach	Premium/(discount) on features of the property compared to comparable properties	-12% (2013: -8.4%)	The higher the premium, the higher the fair value. The higher the discount, the lower the fair value.

Premium/(discount) on features of the property are determined after taken into account various factors, such as time for market movement, location, accessibility, building age/condition, floor level, size, layout, etc., with reference to their differences in features with comparable properties.

Precious metals

The fair values of precious metals are determined by obtaining quoted market prices in active market or market quote with certain adjustments.

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities (continued)

3.3 Non-financial instruments measured at fair value (continued)

(A) Fair value hierarchy

	The Group			
	2014			
	Level 1	Level 2	Level 3	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Non-financial assets				
Investment properties	**-**	**-**	**1,280,271**	**1,280,271**
Properties, plant and equipment				
- Premises	**-**	**213,970**	**6,821,340**	**7,035,310**
Other assets				
- Precious metals	**-**	**11,691**	**-**	**11,691**

	The Group			
	2013			
	Level 1	Level 2	Level 3	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Non-financial assets				
Investment properties	-	27,000	1,147,938	1,174,938
Properties, plant and equipment				
- Premises	-	1,931,868	4,677,510	6,609,378

	The Bank			
	2014			
	Level 1	Level 2	Level 3	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Non-financial assets				
Investment properties	**-**	**-**	**1,258,121**	**1,258,121**
Properties, plant and equipment				
- Premises	**-**	**180,461**	**6,338,666**	**6,519,127**

	The Bank			
	2013			
	Level 1	Level 2	Level 3	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Non-financial assets				
Investment properties	-	27,000	1,099,510	1,126,510
Properties, plant and equipment				
- Premises	-	1,889,585	4,231,196	6,120,781

There were no non-financial asset transfers between level 1 and level 2 for the Group during the year (2013: Nil).

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities (continued)

3.3 Non-financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items

	The Group 2014 Non-financial assets	
	Investment properties	Properties, plant and equipment Premises
	HK$'000	HK$'000
At 1 January 2014	**1,147,938**	**4,677,510**
Gains		
- Income statement		
- Net gain from fair value adjustments on investment properties	**126,896**	**-**
- Net gain from revaluation of properties, plant and equipment	**-**	**2,033**
- Other comprehensive income		
- Revaluation of premises	**-**	**336,325**
Depreciation	-	**(65,649)**
Additions	**821**	**28,906**
Reclassification	**(24,085)**	**24,085**
Exchange difference	**(1,299)**	**(11,969)**
Transfer into level 3	**30,000**	**1,830,099**
At 31 December 2014	**1,280,271**	**6,821,340**
Total unrealised gain for the year included in income statement for non-financial assets held as at 31 December 2014		
- Net gain from fair value adjustments on investment properties	**126,896**	**-**
- Net gain from revaluation of premises	**-**	**2,033**
	126,896	**2,033**

	The Group 2013 Non-financial assets	
	Investment properties	Properties, plant and equipment Premises
	HK$'000	HK$'000
At 1 January 2013	1,001,279	4,094,219
Gains		
- Income statement		
- Net gain from fair value adjustments on investment properties	166,363	-
- Net gain from revaluation of properties, plant and equipment	-	8,085
- Other comprehensive income		
- Revaluation of premises	-	582,352
Depreciation	-	(57,416)
Additions	-	16,560
Reclassification	(21,050)	21,050
Exchange difference	1,346	12,660
At 31 December 2013	1,147,938	4,677,510
Total unrealised gain for the year included in income statement for non-financial assets held as at 31 December 2013		
- Net gain from fair value adjustments on investment properties	166,363	-
- Net gain from revaluation of premises	-	8,085
	166,363	8,085

Notes to the Financial statements (continued)

3. Fair values of assets and liabilities (continued)

3.3 Non-financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items (continued)

	The Bank	
	2014	
	Non-financial assets	
		Properties, plant and equipment
	Investment properties	Premises
	HK$'000	HK$'000
At 1 January 2014	1,099,510	4,231,196
Gains		
- Income statement		
- Net gain from fair value adjustments on investment properties	125,630	-
- Other comprehensive income		
- Revaluation of premises	-	308,619
Depreciation	-	(44,817)
Additions	641	28,708
Reclassification	2,340	(2,340)
Transfer into level 3	30,000	1,817,300
At 31 December 2014	1,258,121	6,338,666
Total unrealised gain for the year included in income statement for non-financial assets held as at 31 December 2014		
- Net gain from fair value adjustments on investment properties	125,630	-

	The Bank	
	2013	
	Non-financial assets	
		Properties, plant and equipment
	Investment properties	Premises
	HK$'000	HK$'000
At 1 January 2013	955,670	3,665,303
Gains		
- Income statement		
- Net gain from fair value adjustments on investment properties	164,890	-
- Other comprehensive income		
- Revaluation of premises	-	568,212
Depreciation	-	(39,691)
Additions	-	16,322
Reclassification	(21,050)	21,050
At 31 December 2013	1,099,510	4,231,196
Total unrealised gain for the year included in income statement for non-financial assets held as at 31 December 2013		
- Net gain from fair value adjustments on investment properties	164,890	-

The transfer of properties into and out of level 3 is due to change in the premium/(discount) on features applied between the subject and comparable properties during the year. Premium/(discount) on features is determined with reference to differences in features between the subject properties and the comparable properties recently transacted in the market. As comparable properties that come from recent market transactions may be different in each year, the premium/(discount) on features applied between the subject and comparable properties would change from year to year accordingly. As a result, the significance of adjustments made to observable market inputs may vary and lead to the transfer of properties into and out of level 3.

Notes to the Financial statements (continued)

4. Hedge accounting

Hedges of net investments in foreign operations

As at 31 December 2014, a proportion of the Group's RMB-denominated deposits from customers of HK$1,393,565,000 (2013: HK$1,431,965,000) were designated as a hedging instrument to hedge against the net investments in foreign operations.

There were no gains or losses on ineffective portion recognised in the income statement during the year (2013: Nil).

5. Assets pledged as security

As at 31 December 2014, liabilities of the Group and the Bank both amounting to HK$6,532,608,000 (2013: HK$4,148,807,000) were secured by assets deposited with central depositories to facilitate settlement operations. In addition, the liabilities of the Group amounting to HK$2,090,606,000 (2013: HK$1,268,641,000) were secured by debt securities and bills related to sale and repurchase arrangements. The amount of assets pledged by the Group and the Bank to secure these liabilities was HK$8,677,155,000 (2013: HK$5,454,505,000) and HK$6,541,300,000 (2013: HK$4,155,616,000) mainly included in "Trading securities", "Available-for-sale securities", "Held-to-maturity securities" and "Trade bills".

6. Contingent liabilities and commitments

The following is a summary of the contractual amounts of each significant class of contingent liability and commitment and the aggregate credit risk-weighted amount and is prepared with reference to the Completion Instructions for the HKMA return of capital adequacy ratio.

	The Group		The Bank	
	2014	2013	**2014**	2013
	HK$'000	HK$'000	**HK$'000**	HK$'000
Direct credit substitutes	**23,145,228**	15,907,292	**121,498**	269,382
Transaction-related contingencies	**2,571,980**	5,484,250	**718,699**	565,013
Trade-related and other contingencies	**12,698,674**	11,870,541	**2,597,679**	3,477,038
Commitments that are unconditionally cancellable without prior notice	**68,666,899**	71,071,494	**25,258,247**	20,945,416
Other commitments with an original maturity of				
- up to one year	**1,158,435**	567,314	**1,158,435**	567,314
- over one year	**4,673,119**	5,245,225	**4,112,747**	4,825,980
	112,914,335	110,146,116	**33,967,305**	30,650,143
Credit risk-weighted amount	**16,759,631**	14,703,603	**2,757,654**	3,207,548

The credit risk-weighted amount is calculated in accordance with the Banking (Capital) Rules. The amount is dependent upon the status of the counterparty and the maturity characteristics of each type of contract.

Notes to the Financial statements (continued)

7. Segmental reporting

(a) By operating segment

The Group divides its business into four major segments, Personal Banking, Corporate Banking, Treasury and Investment.

Both Personal Banking and Corporate Banking provide general banking services. Personal Banking serves individual customers while Corporate Banking deals with non-individual customers. The Treasury segment is responsible for managing the capital, liquidity, and the interest rate and foreign exchange positions of the Group in addition to proprietary trades. It provides funds to other business segments and receives funds from deposit taking activities of Personal Banking and Corporate Banking. These inter-segment funding is charged according to the internal funds transfer pricing mechanism of the Group. The assets and liabilities of Treasury have not been adjusted to reflect the effect of inter-segment borrowing and lending (i.e. the profit and loss information in relation to Treasury is not comparable to the assets and liabilities information about Treasury).

Investment includes bank premises and equipment used by supporting units. Charges are paid to this segment from other business segments based on market rates per square foot for their occupation of the Group's premises. The exchange difference arising from capital of our subsidiary, NCB (China), which is recognised in its income statement, is also included in this class.

"Others" refers to other group operations and mainly comprises of items related to the Group as a whole and totally independent of the other four business segments.

Revenues and expenses of any business segment mainly include items directly attributable to the segment. For management overheads, allocations are made on reasonable bases.

In 2014, liquidity term premium was introduced into inter-segment funding. No revision has been made to the comparative figures. However, if the same mechanism was applied last year, it is estimated that the change in net interest income of Personal Banking, Corporate Banking and Treasury would not be considered as material.

Notes to the Financial statements (continued)

7. Segmental reporting (continued)

(a) By operating segment (continued)

	The Group							
	2014							
	Personal Banking	Corporate Banking	Treasury	Investment	Others	Subtotal	Eliminations	Consolidated
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Net interest income/(expense)								
- external	(418,490)	2,750,511	2,858,028	-	-	5,190,049	-	5,190,049
- inter-segment	1,307,961	(114,871)	(1,193,090)	-	-	-	-	-
	889,471	2,635,640	1,664,938	-	-	5,190,049	-	5,190,049
Net fee and commission income/(expense)	538,300	623,126	94,697	95	(1,492)	1,254,726	-	1,254,726
Net trading gain/(loss)	50,406	105,572	(125,113)	(22,424)	417	8,858	-	8,858
Net loss on financial instruments designated at fair value through profit or loss	-	-	(7,958)	-	-	(7,958)	-	(7,958)
Net gain on other financial assets	-	28,888	93,642	-	-	122,530	-	122,530
Other operating income	140	174	-	174,357	13,780	188,451	(117,643)	70,808
Net operating income before impairment allowances	1,478,317	3,393,400	1,720,206	152,028	12,705	6,756,656	(117,643)	6,639,013
Net charge of impairment allowances	(45,453)	(858,841)	-	-	-	(904,294)	-	(904,294)
Net operating income	1,432,864	2,534,559	1,720,206	152,028	12,705	5,852,362	(117,643)	5,734,719
Operating expenses	(763,907)	(1,257,493)	(301,253)	(204,538)	(88,041)	(2,615,232)	117,643	(2,497,589)
Operating profit/(loss)	668,957	1,277,066	1,418,953	(52,510)	(75,336)	3,237,130	-	3,237,130
Net gain from fair value adjustments on investment properties	-	-	-	129,896	-	129,896	-	129,896
Net loss from disposal/ revaluation of properties, plant and equipment	-	-	-	(347)	-	(347)	-	(347)
Profit/(loss) before taxation	668,957	1,277,066	1,418,953	77,039	(75,336)	3,366,679	-	3,366,679
Assets								
Segment assets	33,101,750	132,582,987	129,285,776	8,717,158	216,582	303,904,253	-	303,904,253
Liabilities								
Segment liabilities	103,437,642	120,438,397	43,259,903	7,582	1,865,885	269,009,409	-	269,009,409
Other information								
Capital expenditure	-	-	-	85,817	-	85,817	-	85,817
Depreciation	10,350	5,705	982	204,528	3,203	224,768	-	224,768
Amortisation of securities	-	-	90,773	-	-	90,773	-	90,773

Notes to the Financial statements (continued)

7. Segmental reporting (continued)

(a) By operating segment (continued)

	The Group							
	2013							
	Personal Banking	Corporate Banking	Treasury	Investment	Others	Subtotal	Eliminations	Consolidated
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Net interest income/(expense)								
- external	(597,519)	2,944,696	2,343,989	-	-	4,691,166	-	4,691,166
- inter-segment	1,435,071	(374,646)	(1,060,425)	-	-	-	-	-
	837,552	2,570,050	1,283,564	-	-	4,691,166	-	4,691,166
Net fee and commission income/(expense)	418,917	565,333	25,641	173	(1,439)	1,008,625	-	1,008,625
Net trading gain/(loss)	37,976	116,764	94,749	(152,278)	10	97,221	-	97,221
Net loss on financial instruments designated at fair value through profit or loss	-	-	(16,193)	-	-	(16,193)	-	(16,193)
Net gain on other financial assets	-	21,204	31,292	-	-	52,496	-	52,496
Other operating income	123	59	-	148,438	24,674	173,294	(97,824)	75,470
Net operating income/(expense) before impairment allowances	1,294,568	3,273,410	1,419,053	(3,667)	23,245	6,006,609	(97,824)	5,908,785
Net charge of impairment allowances	(40,580)	(329,387)	-	-	-	(369,967)	-	(369,967)
Net operating income/(expense)	1,253,988	2,944,023	1,419,053	(3,667)	23,245	5,636,642	(97,824)	5,538,818
Operating expenses	(751,369)	(1,144,769)	(387,541)	(97,468)	(69,175)	(2,450,322)	97,824	(2,352,498)
Operating profit/(loss)	502,619	1,799,254	1,031,512	(101,135)	(45,930)	3,186,320	-	3,186,320
Net gain from fair value adjustments on investment properties	-	-	-	169,414	-	169,414	-	169,414
Net gain from disposal/ revaluation of properties, plant and equipment	-	-	-	3,476	-	3,476	-	3,476
Profit/(loss) before taxation	502,619	1,799,254	1,031,512	71,755	(45,930)	3,359,210	-	3,359,210
Assets								
Segment assets	28,853,019	128,704,708	114,367,231	8,238,515	220,487	280,383,960	-	280,383,960
Liabilities								
Segment liabilities	101,329,458	108,918,619	36,005,845	7,225	1,822,824	248,083,971	-	248,083,971
Other information								
Capital expenditure	-	-	-	109,955	-	109,955	-	109,955
Depreciation	26,990	56,140	23,021	97,703	3,102	206,956	-	206,956
Amortisation of securities	-	-	(30,765)	-	-	(30,765)	-	(30,765)

Notes to the Financial statements (continued)

7. Segmental reporting (continued)

(a) By operating segment (continued)

	The Bank							
	2014							
	Personal Banking	Corporate Banking	Treasury	Investment	Others	Subtotal	Eliminations	Consolidated
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Net interest income/(expense)								
- external	(273,991)	1,627,764	1,749,897	-	-	3,103,670	-	3,103,670
- inter-segment	871,057	(96,022)	(775,035)	-	-	-	-	-
	597,066	1,531,742	974,862	-	-	3,103,670	-	3,103,670
Net fee and commission income/(expense)	474,165	380,004	(7,979)	-	(1,492)	844,698	-	844,698
Net trading gain/(loss)	46,746	45,101	(64,037)	-	417	28,227	-	28,227
Net loss on financial instruments designated at fair value through profit or loss	-	-	(7,958)	-	-	(7,958)	-	(7,958)
Net (loss)/gain on other financial assets	-	(15,405)	93,642	-	-	78,237	-	78,237
Other operating income	140	174	-	173,116	222	173,652	(117,643)	56,009
Net operating income/(expense) before impairment allowances	1,118,117	1,941,616	988,530	173,116	(853)	4,220,526	(117,643)	4,102,883
Net (charge)/credit of impairment allowances	(15,993)	34,574	-	-	-	18,581	-	18,581
Net operating income/(expense)	1,102,124	1,976,190	988,530	173,116	(853)	4,239,107	(117,643)	4,121,464
Operating expenses	(560,990)	(402,244)	(67,051)	(89,427)	(88,041)	(1,207,753)	117,643	(1,090,110)
Operating profit/(loss)	541,134	1,573,946	921,479	83,689	(88,894)	3,031,354	-	3,031,354
Net gain from fair value adjustments on investment properties	-	-	-	128,630	-	128,630	-	128,630
Net loss from disposal/ revaluation of properties, plant and equipment	-	-	-	(1,122)	-	(1,122)	-	(1,122)
Profit/(loss) before taxation	541,134	1,573,946	921,479	211,197	(88,894)	3,158,862	-	3,158,862
Assets								
Segment assets	20,312,401	87,557,320	73,442,969	16,084,689	16,481	197,413,860	-	197,413,860
Liabilities								
Segment liabilities	80,438,461	67,718,962	15,411,315	7,582	1,387,346	164,963,666	-	164,963,666
Other information								
Capital expenditure	-	-	-	39,808	-	39,808	-	39,808
Depreciation	10,350	5,705	982	89,427	3,203	109,667	-	109,667
Amortisation of securities	-	-	(17,310)	-	-	(17,310)	-	(17,310)

Notes to the Financial statements (continued)

7. Segmental reporting (continued)

(a) By operating segment (continued)

	The Bank							
	2013							
	Personal Banking	Corporate Banking	Treasury	Investment	Others	Subtotal	Eliminations	Consolidated
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Net interest income/(expense)								
- external	(249,151)	1,696,893	1,428,370	-	-	2,876,112	-	2,876,112
- inter-segment	813,473	(80,090)	(733,383)	-	-	-	-	-
	564,322	1,616,803	694,987	-	-	2,876,112	-	2,876,112
Net fee and commission income/(expense)	411,886	351,673	(6,829)	-	(1,439)	755,291	-	755,291
Net trading gain/(loss)	25,851	62,141	19,278	(742)	10	106,538	-	106,538
Net loss on financial instruments designated at fair value through profit or loss	-	-	(16,193)	-	-	(16,193)	-	(16,193)
Net gain on other financial assets	-	-	22,303	-	-	22,303	-	22,303
Other operating income	121	27	-	146,700	559	147,407	(97,824)	49,583
Net operating income/(expense) before impairment allowances	1,002,180	2,030,644	713,546	145,958	(870)	3,891,458	(97,824)	3,793,634
Net charge of impairment allowances	(12,151)	(28,577)	-	-	-	(40,728)	-	(40,728)
Net operating income/(expense)	990,029	2,002,067	713,546	145,958	(870)	3,850,730	(97,824)	3,752,906
Operating expenses	(510,799)	(391,915)	(54,139)	(79,083)	(69,175)	(1,105,111)	97,824	(1,007,287)
Operating profit/(loss)	479,230	1,610,152	659,407	66,875	(70,045)	2,745,619	-	2,745,619
Net gain from fair value adjustments on investment properties	-	-	-	167,890	-	167,890	-	167,890
Net loss from disposal/ revaluation of properties, plant and equipment	-	-	-	(1,265)	-	(1,265)	-	(1,265)
Profit/(loss) before taxation	479,230	1,610,152	659,407	233,500	(70,045)	2,912,244	-	2,912,244
Assets								
Segment assets	18,393,275	81,867,045	63,240,738	15,553,575	16,668	179,071,301	-	179,071,301
Liabilities								
Segment liabilities	77,300,761	56,094,120	14,488,430	6,726	1,247,059	149,137,096	-	149,137,096
Other information								
Capital expenditure	-	-	-	36,843	-	36,843	-	36,843
Depreciation	11,598	6,976	924	79,083	3,102	101,683	-	101,683
Amortisation of securities	-	-	3,702	-	-	3,702	-	3,702

Notes to the Financial statements (continued)

7. Segmental reporting (continued)

(b) By geographical area

The following information is presented based on the principal places of operations of the subsidiaries, or in the case of the Bank, on the locations of the branches responsible for reporting the results or booking the assets:

	The Group			
	2014		2013	
	Net operating income before impairment allowance	**Profit before taxation**	Net operating income before impairment allowance	Profit before taxation
	HK$'000	**HK$'000**	HK$'000	HK$'000
Hong Kong	**4,059,329**	**3,149,295**	3,754,292	2,899,990
Mainland of China	**2,535,739**	**207,655**	2,111,161	443,766
Others	**43,945**	**9,729**	43,332	15,454
Total	**6,639,013**	**3,366,679**	5,908,785	3,359,210

	The Group			
	2014			
	Total assets	**Total liabilities**	**Non-current assets**	**Contingent liabilities and commitments**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Hong Kong	**184,505,742**	**162,047,271**	**7,835,833**	**33,849,154**
Mainland of China	**116,624,065**	**104,331,044**	**775,587**	**78,941,179**
Others	**2,774,446**	**2,631,094**	**2,349**	**124,002**
Total	**303,904,253**	**269,009,409**	**8,613,769**	**112,914,335**

	The Group			
	2013			
	Total assets	Total liabilities	Non-current assets	Contingent liabilities and commitments
	HK$'000	HK$'000	HK$'000	HK$'000
Hong Kong	164,667,896	146,467,458	7,343,360	30,381,110
Mainland of China	112,857,400	99,487,847	830,096	79,638,140
Others	2,858,664	2,128,666	3,467	126,866
Total	280,383,960	248,083,971	8,176,923	110,146,116

Notes to the Financial statements (continued)

7. Segmental reporting (continued)

(b) By geographical area (continued)

	The Bank			
	2014		2013	
	Net operating income before impairment allowance	**Profit before taxation**	Net operating income before impairment allowance	Profit before taxation
	HK$'000	**HK$'000**	HK$'000	HK$'000
Hong Kong	**4,059,238**	**3,149,213**	3,747,959	2,893,422
Mainland of China	**(300)**	**(80)**	2,343	3,368
Others	**43,945**	**9,729**	43,332	15,454
Total	**4,102,883**	**3,158,862**	3,793,634	2,912,244

	The Bank			
	2014			
	Total assets	**Total liabilities**	**Non-current assets**	**Contingent liabilities and commitments**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Hong Kong	**194,639,414**	**162,328,311**	**7,835,833**	**33,843,303**
Others	**2,774,446**	**2,635,355**	**2,349**	**124,002**
Total	**197,413,860**	**164,963,666**	**7,838,182**	**33,967,305**

	The Bank			
	2013			
	Total assets	Total liabilities	Non-current assets	Contingent liabilities and commitments
	HK$'000	HK$'000	HK$'000	HK$'000
Hong Kong	175,682,048	146,647,568	7,343,360	30,448,151
Mainland of China	530,589	360,862	-	75,126
Others	2,858,664	2,128,666	3,467	126,866
Total	179,071,301	149,137,096	7,346,827	30,650,143

Notes to the Financial statements (continued)

8. Significant related party transactions

The Group is subject to the control of the State Council of the PRC Government through China Investment Corporation ("CIC"), its wholly-owned subsidiary Central Huijin Investment Ltd. ("Central Huijin"), BOC and BOCHK in which Central Huijin has controlling equity interests.

The significant related party transactions are defined according to HKAS 24.

Notes to the Financial statements (continued)

8. Significant related party transactions (continued)

(a) Transactions with the parent companies and the other companies controlled by the parent companies

General information of the parent companies:

The Group's immediate holding company is BOCHK, which is in turn controlled by BOC. Central Huijin is the controlling entity of BOC, and it is a wholly-owned subsidiary of CIC which is a wholly state-owned company engaging in foreign currency investment management.

Central Huijin has controlling equity interests in certain other entities in the PRC.

The Group enters into banking and other transactions with these entities in the normal course of business which include loans, investment securities and money market.

The majority of transactions with BOC arise from money market activities. As at 31 December 2014, the related aggregate amounts due from and to BOC of the Group were HK$4,756,693,000 (2013: HK$6,796,023,000) and HK$13,986,923,000 (2013: HK$2,702,999,000) respectively. The aggregate amounts of income and expenses of the Group arising from these transactions with BOC for the year ended 31 December 2014 were HK$295,494,000 (2013: HK$240,822,000) and HK$191,080,000 (2013: HK$39,549,000) respectively.

The majority of transactions with BOCHK arise from money market activities. As at 31 December 2014, the related aggregate amounts due from and to BOCHK of the Group were HK$1,840,662,000 (2013: HK$2,139,709,000) and HK$17,173,914,000 (2013: HK$21,270,585,000) respectively. The aggregate amounts of income and expenses of the Group arising from these transactions with BOCHK for the year ended 31 December 2014 were HK$2,560,000 (2013: HK$10,252,000) and HK$729,578,000 (2013: HK$708,001,000) respectively.

The majority of transactions with other companies controlled by the parent companies arise from deposits from customers. As at 31 December 2014, the related aggregate amount of the Group was HK$12,914,910,000 (2013: HK$7,093,494,000). The aggregate amount of expenses of the Group arising from these transactions with other companies controlled by the parent companies for the year ended 31 December 2014 was HK$83,057,000 (2013: HK$95,069,000).

Save as disclosed above, transactions with other parent companies and the other companies controlled by the parent companies are not considered material.

Notes to the Financial statements (continued)

8. Significant related party transactions (continued)

(b) Transactions with government authorities, agencies, affiliates and other state controlled entities

The Group is subject to the control of the State Council of the PRC Government through CIC and Central Huijin, which also directly and indirectly controls a significant number of entities through its government authorities, agencies, affiliates and other state controlled entities. The Group enters into banking transactions with government authorities, agencies, affiliates and other state controlled entities in the normal course of business at commercial terms.

These transactions include, but are not limited to, the following:

- lending, provision of credits and guarantees, and deposit taking;
- inter-bank balance taking and placing;
- sales, purchase, underwriting and redemption of bonds issued by other state controlled entities;
- rendering of foreign exchange, remittance and investment related services;
- provision of fiduciary activities; and
- purchase of utilities, transport, telecommunication and postage services.

(c) Key management personnel

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, including directors and Senior Management. The Group accepts deposits from and grants loans and credit facilities to key management personnel in the ordinary course of business. During both the current and prior years, no material transaction was conducted with key management personnel of the Bank and its holding companies, as well as parties related to them.

The compensation of key management personnel for the year ended 31 December is detailed as follows:

	2014	2013
	HK$'000	HK$'000
Salaries and other short-term employee benefits	**26,740**	28,882
Post-employment benefits	**1,694**	1,635
	28,434	30,517

Notes to the Financial statements (continued)

9. Currency concentrations

The following is a summary of the Group's major foreign currency exposures arising from trading, non-trading and structural positions and is prepared with reference to the Completion Instructions for the prudential return "Foreign Currency Position of an Authorised Institution" issued by the HKMA.

2014

Equivalent in thousand of HK$

	US Dollars	**Renminbi**	**Other foreign currencies**	**Total foreign currencies**
Spot assets	**50,714,856**	**129,625,777**	**10,170,515**	**190,511,148**
Spot liabilities	**(49,057,989)**	**(113,019,787)**	**(9,087,139)**	**(171,164,915)**
Forward purchases	**23,258,343**	**8,581,087**	**2,839,602**	**34,679,032**
Forward sales	**(24,806,626)**	**(25,023,970)**	**(3,877,531)**	**(53,708,127)**
Net long position	**108,584**	**163,107**	**45,447**	**317,138**
Net structural position	**277,715**	**8,414,836**	**-**	**8,692,551**

2013

Equivalent in thousand of HK$

	US Dollars	Renminbi	Other foreign currencies	Total foreign currencies
Spot assets	51,589,784	121,853,558	9,384,830	182,828,172
Spot liabilities	(44,518,523)	(111,464,523)	(9,925,494)	(165,908,540)
Forward purchases	24,399,649	10,648,881	4,468,976	39,517,506
Forward sales	(29,771,697)	(21,621,410)	(3,875,909)	(55,269,016)
Net long/(short) position	1,699,213	(583,494)	52,403	1,168,122
Net structural position	333,141	8,263,668	-	8,596,809

Notes to the Financial statements (continued)

10. Cross-border claims

The below analysis is prepared with reference to the Completion Instructions for the HKMA return of cross-border claims. Cross-border claims are exposures to foreign counterparties on which the ultimate risk lies, and are derived according to the location of the counterparties after taking into account the transfer of risk. For a claim guaranteed by a party situated in a country different from the counterparty, the risk will be transferred to the country of the guarantor. For a claim on an overseas branch of a bank whose head office is located in another country, the risk will be transferred to the country where its head office is located. Claims on individual countries or areas, after risk transfer, amounting to 10% or more of the aggregate cross-border claims are shown as follows:

	2014			
	Banks	**Public sector entities***	**Others**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Asia, other than Hong Kong				
- Mainland of China	**29,028,933**	**812,933**	**40,413,113**	**70,254,979**
- Others	**9,304,654**	**-**	**1,804,681**	**11,109,335**
Total	**38,333,587**	**812,933**	**42,217,794**	**81,364,314**

	2013			
	Banks	Public sector entities*	Others	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Asia, other than Hong Kong				
- Mainland of China	35,085,897	647,145	34,557,836	70,290,878
- Others	6,522,598	851	1,259,319	7,782,768
Total	41,608,495	647,996	35,817,155	78,073,646

* There are no exposures eligible to be classified as public sector entities under the Banking (Capital) Rules in the tables above.

Notes to the Financial statements (continued)

11. Non-bank Mainland exposures

The analysis of non-bank Mainland exposures is based on the categories of non-bank counterparties and the type of direct exposures with reference to the Completion Instructions for the HKMA return of non-bank Mainland exposures, which includes the Mainland exposures extended by the Bank and its banking subsidiary.

	Items in HKMA return	2014 On-balance sheet exposure HK$'000	2014 Off-balance sheet exposure HK$'000	2014 Total exposure HK$'000
Central government, central government-owned entities and their subsidiaries and joint ventures	1	**29,451,874**	**1,151,441**	**30,603,315**
Local governments, local government-owned entities and their subsidiaries and joint ventures	2	**11,599,566**	**1,810,301**	**13,409,867**
PRC nationals residing in Mainland or other entities incorporated in Mainland and their subsidiaries and joint ventures	3	**50,180,366**	**29,896,773**	**80,077,139**
Other entities of central government not reported in item 1 above	4	**318,005**	**-**	**318,005**
Other entities of local governments not reported in item 2 above	5	**-**	**-**	**-**
PRC nationals residing outside Mainland or entities incorporated outside Mainland where the credit is granted for use in Mainland	6	**6,980,121**	**1,183,797**	**8,163,918**
Other counterparties where the exposures are considered to be non-bank Mainland exposures	7	**5,177,267**	**-**	**5,177,267**
Total	8	**103,707,199**	**34,042,312**	**137,749,511**
Total assets after provision	9	**310,553,707**		
On-balance sheet exposures as percentage of total assets	10	**33.39%**		

	Items in HKMA return	(Restated) 2013 On-balance sheet exposure HK$'000	(Restated) 2013 Off-balance sheet exposure HK$'000	(Restated) 2013 Total exposure HK$'000
Central government, central government-owned entities and their subsidiaries and joint ventures	1	24,381,250	835,223	25,216,473
Local governments, local government-owned entities and their subsidiaries and joint ventures	2	10,589,130	1,800,550	12,389,680
PRC nationals residing in Mainland or other entities incorporated in Mainland and their subsidiaries and joint ventures	3	52,761,011	28,348,407	81,109,418
Other entities of central government not reported in item 1 above	4	-	-	-
Other entities of local governments not reported in item 2 above	5	-	-	-
PRC nationals residing outside Mainland or entities incorporated outside Mainland where the credit is granted for use in Mainland	6	5,630,650	1,876,581	7,507,231
Other counterparties where the exposures are considered to be non-bank Mainland exposures	7	4,593,476	42,298	4,635,774
Total	8	97,955,517	32,903,059	130,858,576
Total assets after provision	9	288,685,809		
On-balance sheet exposures as percentage of total assets	10	33.93%		

The comparative amounts have been restated to conform with the current year's presentation.

Notes to the Financial statements (continued)

12. Regulatory capital for credit, market and operational risks

The bases of regulatory capital calculation for credit risk, market risk and operational risk are described in Note 2.4 to the Financial statements.

The table below summarises the regulatory capital computed on the same consolidation basis for credit, market, and operational risks.

	2014	2013
	HK$'000	HK$'000
Credit risk	**13,828,215**	13,485,328
Market risk	**45,648**	77,209
Operational risk	**900,408**	775,167
	14,774,271	14,337,704

For details of capital management and capital ratios of the Group, please refer to Note 2.4 to the Financial statements.

Notes to the Financial statements (continued)

13. Capital requirements for credit risk

The tables below show the capital requirements for each class and subclass of credit risk exposures as specified in the Banking (Capital) Rules.

	2014	2013
	HK$'000	HK$'000
Capital required for exposures under the IRB approach		
Corporate		
Specialised lending under supervisory slotting criteria approach		
- Project finance	119,626	76,474
Small-and-medium sized corporates	1,328,166	1,201,437
Other corporates	6,031,115	6,853,958
Bank		
Banks	3,763,767	3,294,819
Securities firms	920	674
Retail		
Residential mortgages		
- Individuals	80,229	56,135
- Property-holding shell companies	5,836	5,347
Qualifying revolving retail	-	-
Other retail to individuals	271,595	166,376
Small business retail	17,195	22,470
Others		
Cash items	-	-
Other items	745,981	706,400
Credit valuation adjustment	6,549	8,245
Total capital requirements for exposures under the IRB approach	12,370,979	12,392,335
Capital required for exposures under the standardised (credit risk) approach		
On-balance sheet exposures		
Sovereigns	10,915	8,208
Public sector entities	2,238	4,500
Banks	103,306	2,398
Corporates	674,242	539,825
Regulatory retail	140,094	105,337
Residential mortgage loans	447,824	341,461
Other exposures which are not past due	44,895	55,176
Past due exposures	7,548	2,816
Off-balance sheet exposures		
Off-balance sheet exposures other than securities financing transactions and derivative contracts	25,557	31,404
Securities financing transactions and derivative contracts	617	1,868
Total capital requirements for exposures under the standardised (credit risk) approach	1,457,236	1,092,993
Total capital requirements for credit risk exposures	13,828,215	13,485,328

Notes to the Financial statements (continued)

14. Credit risk under the internal ratings-based approach

14.1 The internal rating systems and risk components

The Group adopts the FIRB approach to calculate the regulatory capital requirements for most of the corporate and bank exposures, and adopts the supervisory slotting criteria approach to project finance exposures under "specialised lending". The Group adopts retail IRB approach for retail exposures to individuals and small business. The following is the table showing the Group's different capital calculation approaches to each asset class and sub-classes of exposures (other than securitisation exposures).

Asset class	Exposure sub-class	Capital calculation approach
Corporate exposures	Specialised lending under supervisory slotting criteria approach (project finance)	Supervisory Slotting Criteria Approach
	Small-and-medium sized corporates	FIRB Approach
	Other corporates	
Sovereign exposures	Sovereigns	Standardised (credit risk) Approach
	Sovereign foreign public sector entities	
	Multilateral development banks	
Bank exposures	Banks	FIRB Approach
	Securities firms	
	Public sector entities (excluding sovereign foreign public sector entities)	Standardised (credit risk) Approach
Retail exposures	Residential mortgages to individuals	Retail IRB Approach
	Residential mortgages to property-holding shell companies	
	Qualifying revolving retail	
	Other retail to individuals	
	Small business retail	
Equity exposures	-	Standardised (credit risk) Approach
Other exposures	Cash items	Specific Risk-weight Approach
	Other items	

(A) The structure of internal rating systems and the relationship between internal ratings and external ratings

The Group's internal rating system is a two dimensional rating system that provides separate assessment of borrower and transaction characteristics. For corporate and bank portfolios, the obligor rating dimension reflects exclusively the risk of borrower default and the facility rating dimension reflects transaction specific factors that affect the loss severity in the case of borrower default.

The Group uses statistical models to provide own estimated probability of default ("PD") for its corporate, bank and retail borrowers, and loss given default ("LGD") and exposure at default ("EAD") for retail exposures under retail IRB approach.

Notes to the Financial statements (continued)

14. Credit risk under the internal ratings-based approach (continued)

14.1 The internal rating systems and risk components (continued)

(A) The structure of internal rating systems and the relationship between internal ratings and external ratings (continued)

The Group uses internal rating system to assess the borrower's likelihood of default for all IRB portfolios. PD estimates the risk of borrower default over a one-year period. A borrower credit grade means a grouping of similar credit-worthiness to which borrowers are assigned on the basis of specified and distinct set of rating criteria, from which the average PD are derived for RWA calculation.

In the process of obligor rating assignment, variables of latest financial performance, management quality, industry risks, group connection and negative warning signals of each obligor are assessed as critical factors to predict borrower's ability and willingness to meet with the contractual obligations under different economic conditions.

The obligors for corporate and bank, and retail PD pools are assigned into eight broad obligor ratings including seven grades for non-defaulted obligors with sub-divisions into 26 minor credit grades and one for defaulted obligors. In the supervisory slotting criteria approach for the project finance exposures, there are four grades for non-defaulted borrowers and one for defaulted borrowers in accordance with the HKMA guidance. The estimates for retail IRB portfolios are pooled by nature of obligors, facility types, collateral types and delinquency status into different PD, EAD and LGD pools. This pooling process provides the basis of accurate and consistent estimation for PD, LGD and EAD at the pool level for exposures arising from residential mortgages to both individuals and property-holding shell companies, qualifying revolving retail exposures and other retail exposures to individuals and small business retail exposures. All credit transactions for corporates and banks are assigned facility ratings (in terms of LGD) in accordance with the HKMA guidance. LGD estimates multiplied by the PD estimates produce the expected loss ("EL") estimates, which are used to assess credit risk quantitatively.

Notes to the Financial statements (continued)

14. Credit risk under the internal ratings-based approach (continued)

14.1 The internal rating systems and risk components (continued)

(A) The structure of internal rating systems and the relationship between internal ratings and external ratings (continued)

For each internal rating, the equivalent external rating in terms of default risk is as below:

Internal Credit Grades	Definition of Internal Ratings	Standard & Poor's Equivalent
1	The obligors in grades "1" and "2" have extremely low default risk. The obligor's capacity to meet its financial commitment on the obligation is extremely strong.	AAA
2		AA+
		AA
		AA-
3	The obligors in grade "3" have low default risk but are somewhat susceptible to the adverse effects of changes in circumstances and economic conditions. However, the obligor's capacity to meet its financial commitment on the obligation is very strong.	A+
		A
		A-
4	The obligors in grade "4" have relatively low default risk and are currently under adequate protection. However, adverse economic conditions or changing circumstances are likely to lead to a weakened capacity of the obligor to meet its financial commitment on the obligation.	BBB+
		BBB
		BBB-
5	The obligors in grade "5" have medium default risk which are less vulnerable to nonpayment than other speculative obligors. However, they face major ongoing uncertainties or exposure to adverse business, financial, or economic conditions which could lead to the obligor's inadequate capacity to meet its financial commitment on the obligation.	BB+
		BB
		BB-
6	The obligors in grade "6" have significant to very high default risk and are vulnerable to nonpayment. The obligors currently and in the near term have the capacity to meet its financial commitment on the obligation but adverse business, financial, or economic conditions will very likely impair the obligor's capacity or willingness to meet its financial commitment on the obligation.	B+
		B
		B-
7	The obligors in grade "7" have very high default risk and are currently quite vulnerable to nonpayment. The obligors' ability to meet their financial commitment and obligation are dependent upon favorable business, financial, and economic conditions. In the event of adverse business, financial, or economic conditions, these obligors are not likely to have the capacity to meet its financial commitment on the obligation.	CCC
		CC
		C
8	Obligors rated "8" are in payment default.	D

(B) Use of internal estimates

Besides using PD estimates for regulatory capital calculation in corporate and bank exposures, the Group uses the PD together with the LGD and EAD estimates in the credit approval, credit monitoring, reporting and analysis of credit risk information, etc., for the purpose of strengthening the daily management on all credit related matters.

Notes to the Financial statements (continued)

14. Credit risk under the internal ratings-based approach (continued)

14.1 The internal rating systems and risk components (continued)

(C) Process of managing and recognising credit risk mitigation

For those collaterals recognised under capital management, the Group has well-defined policies and procedures for collateral valuation and management which are compliant with the operational requirements for recognised collateral of credit risk mitigation as stated in the Banking (Capital) Rules.

For the credit exposures adopting FIRB approach for capital calculation purpose, the recognised eligible guarantees include the guarantees provided by banks, corporates and securities firms with a lower risk weights than the counterparty. The Group takes into account the credit risk mitigation effect of recognised collaterals through its determination of the net credit exposures and the effective LGD.

For retail IRB approach, the effect of the credit risk mitigation is incorporated into the internal risk parameters of PD or LGD depending on the nature of the guarantees and collaterals for calculating the risk exposures.

The credit and market risk concentrations within the credit risk mitigation (recognised collateral and guarantees for capital calculation) used by the Group are under a low level.

Up to the date of report, for capital calculation, except derivatives subject to valid bilateral netting agreements, the Group has not used any other on-balance sheet or off-balance sheet recognised netting for credit risk mitigation. The Group also has not used any recognised credit derivative contracts for credit risk mitigation.

(D) The control mechanisms used for internal rating systems

The Group has established a comprehensive control mechanism to ensure the integrity, accuracy and consistency of the rating systems including the processes for using the risk components in the day-to-day business to assess credit risk.

All of IRB risk models are approved by the Credit and Loans Management Committee and Risk Management Committee of the Board.

Notes to the Financial statements (continued)

14. Credit risk under the internal ratings-based approach (continued)

14.1 The internal rating systems and risk components (continued)

(D) The control mechanisms used for internal rating systems (continued)

In order to achieve reasonably accurate risk ratings assignment, the Group has established a rating approval process which is independent of the sales and marketing units. Since internal rating is one of the key inputs to credit decision making, a control mechanism is put in place to ensure the integrity, accuracy and consistency of the rating assignment. For the wholesale (corporate and bank) credit portfolio, internal ratings are normally approved by credit officers who are functionally separated from the sales and marketing units. In some cases where the transactions are in small amount and of very low credit risk, the credit ratings can be assigned and approved by staff within the sales and marketing units, subject to the periodic post-approval review of ratings by risk management units.

The rating assignment and risk quantification process of retail portfolio are highly automated. As an integral part of the daily credit assessment process, the accuracy and completeness of data input for automatic rating assignment are verified by units independent from business development function.

The obligor rating is reviewed at least annually as required by the Group's credit risk policy. When credit events occur to the obligor, rating review is triggered promptly in accordance with the Group's credit risk policy.

Rating override is designed to allow the credit analyst to include any other relevant credit information that has not yet been captured in the rating models. For reasons of conservatism and prudential considerations, overrides are unlimited in terms of downgrades but more restricted for upgrades. All upgrades will be limited to a maximum of two sub-grades supported by a very narrowly pre-defined list of appropriate reasons. All overrides need to be signed off by a higher level of credit approval authority. The internal rating policy sets a trigger point of 10% overrides on rating cases. The use of overrides and override reasons are analysed by BOCHK as part of performance review on IRB rating models.

The performance of internal rating system is put under ongoing periodic monitoring. The Management periodically reviews the performance and predictive ability of the internal rating system. The effectiveness of the internal rating system and processes are reviewed by independent control functions. The model maintenance unit conducts assessment on the discriminatory power, accuracy and stability of the rating systems while the validation unit performs comprehensive review of the internal rating system. Internal audit reviews the internal rating system and the operations of the related credit risk control units. The results of the review are reported to the Board and the Management regularly.

A model validation team of BOCHK which is independent from the model development unit and rating assignment units, conducts periodic model validations using both qualitative and quantitative analysis. Model acceptance standards are established by BOCHK to ensure the discriminatory power, accuracy and stability of the rating systems meet regulatory and management requirements. Review of a rating model will be triggered if the performance of the model deteriorates materially against pre-determined tolerance limits.

Notes to the Financial statements (continued)

14. Credit risk under the internal ratings-based approach (continued)

14.1 The internal rating systems and risk components (continued)

(E) Approach for determining provisions

The approach in determining provisions is in line with the Group's accounting policies. For details, please refer to Note 1.15 "Impairment of financial assets" to the Financial statements.

14.2 Exposures by IRB calculation approach

The tables below show the Group's exposures other than securitisation exposures (including the EAD of on-balance sheet exposures and off-balance sheet exposures) by each IRB calculation approach.

	2014				
	Foundation IRB Approach HK$'000	**Supervisory Slotting Criteria Approach HK$'000**	**Retail IRB Approach HK$'000**	**Specific Risk-weight Approach HK$'000**	**Total exposures HK$'000**
Corporate	**137,531,530**	**1,543,915**	**-**	**-**	**139,075,445**
Bank	**103,072,641**	**-**	**-**	**-**	**103,072,641**
Retail					
Residential mortgages to individuals and property-holding shell companies	**-**	**-**	**11,742,017**	**-**	**11,742,017**
Qualifying revolving retail	**-**	**-**	**-**	**-**	**-**
Other retail to individuals	**-**	**-**	**8,032,884**	**-**	**8,032,884**
Small business retail	**-**	**-**	**2,160,707**	**-**	**2,160,707**
Others	**-**	**-**	**-**	**10,188,547**	**10,188,547**
Total	**240,604,171**	**1,543,915**	**21,935,608**	**10,188,547**	**274,272,241**

	2013				
	Foundation IRB Approach HK$'000	Supervisory Slotting Criteria Approach HK$'000	Retail IRB Approach HK$'000	Specific Risk-weight Approach HK$'000	Total exposures HK$'000
Corporate	137,287,288	851,200	-	-	138,138,488
Bank	86,657,273	-	-	-	86,657,273
Retail					
Residential mortgages to individuals and property-holding shell companies	-	-	11,570,062	-	11,570,062
Qualifying revolving retail	-	-	-	-	-
Other retail to individuals	-	-	6,152,620	-	6,152,620
Small business retail	-	-	2,630,307	-	2,630,307
Others	-	-	-	12,746,845	12,746,845
Total	223,944,561	851,200	20,352,989	12,746,845	257,895,595

Notes to the Financial statements (continued)

14. Credit risk under the internal ratings-based approach (continued)

14.3 Exposures subject to supervisory estimates under the IRB approach

The table below shows the total EAD of the Group's exposures subject to supervisory estimates under the use of IRB approach (including the specialised lending subject to the supervisory slotting criteria approach).

	2014	2013
	HK$'000	HK$'000
Corporate	**139,075,445**	138,138,488
Bank	**103,072,641**	86,657,273
Others	**10,188,547**	12,746,845
	252,336,633	237,542,606

14.4 Exposures covered by credit risk mitigation used

(A) Exposures covered by recognised collateral

The table below shows the Group's exposures under the use of FIRB approach (after the effect of any on-balance sheet or off-balance sheet recognised netting) which are covered by recognised collateral after the application of haircuts required under the Banking (Capital) Rules. These exposures exclude securities financing transactions and derivative contracts.

	2014	2013
	HK$'000	HK$'000
Corporate	**29,599,424**	28,007,658
Bank	**3,254**	452
	29,602,678	28,008,110

(B) Exposures covered by recognised guarantees

The table below shows the Group's exposures (after the effect of any on-balance sheet or off-balance sheet recognised netting) which are covered by recognised guarantees after the application of haircuts required under the Banking (Capital) Rules. These exposures exclude securities financing transactions and derivative contracts.

	2014	2013
	HK$'000	HK$'000
Corporate	**29,330,207**	27,280,949
Bank	**7,893,668**	5,173,810
	37,223,875	32,454,759

Notes to the Financial statements (continued)

14. Credit risk under the internal ratings-based approach (continued)

14.5 Risk assessment for corporate and bank exposures under IRB approach

The tables below detail the Group's total EAD of corporate and bank exposures by exposure-weighted average risk-weight and exposure-weighted average PD for each obligor grade as at 31 December.

The EAD and PD disclosed below in respect of corporate and bank exposures have taken into account the effect of recognised collateral, recognised netting and recognised guarantees. The Group did not have any recognised credit derivative contracts.

(A) Corporate exposures (other than specialised lending under supervisory slotting criteria approach)

	2014		
Internal Credit Grades	**Exposure at default**	**Exposure-weighted average risk-weight**	**Exposure-weighted average PD**
	HK$'000	**%**	**%**
Grade 1	**-**	**0.00**	**0.00**
Grade 2	**308,114**	**23.37**	**0.04**
Grade 3	**18,733,272**	**23.45**	**0.07**
Grade 4	**34,181,018**	**40.24**	**0.24**
Grade 5	**67,372,190**	**72.01**	**1.13**
Grade 6	**15,926,506**	**121.46**	**5.18**
Grade 7	**67,764**	**171.14**	**20.40**
Grade 8 / Default	**942,666**	**62.15**	**100.00**
	137,531,530		

	2013		
Internal Credit Grades	Exposure at default	Exposure-weighted average risk-weight	Exposure-weighted average PD
	HK$'000	%	%
Grade 1	-	0.00	0.00
Grade 2	1,069,155	18.47	0.03
Grade 3	18,189,567	24.17	0.07
Grade 4	27,793,369	44.33	0.24
Grade 5	61,570,944	72.90	1.09
Grade 6	28,140,949	115.44	4.50
Grade 7	108,677	215.78	31.20
Grade 8 / Default	414,627	113.42	100.00
	137,287,288		

Notes to the Financial statements (continued)

14. Credit risk under the internal ratings-based approach (continued)

14.5 Risk assessment for corporate and bank exposures under IRB approach (continued)

(B) Corporate exposures (specialised lending under supervisory slotting criteria approach)

	2014		2013	
Supervisory Rating Grades	**Exposure at default**	**Exposure-weighted average risk-weight**	Exposure at default	Exposure-weighted average risk-weight
	HK$'000	**%**	HK$'000	%
Strong	**505,694**	**60.17**	171,262	70.00
Good	**312,252**	**86.96**	-	0.00
Satisfactory	**725,969**	**115.00**	679,938	115.00
Weak	**-**	**0.00**	-	0.00
Default	**-**	**0.00**	-	0.00
	1,543,915		851,200	

The supervisory rating grades and risk-weights of specialised lending are determined in accordance with section 158 of the Banking (Capital) Rules.

(C) Bank exposures

	2014		
Internal Credit Grades	**Exposure at default**	**Exposure-weighted average risk-weight**	**Exposure-weighted average PD**
	HK$'000	**%**	**%**
Grade 1	**-**	**0.00**	**0.00**
Grade 2	**9,809,605**	**22.95**	**0.04**
Grade 3	**49,085,042**	**31.00**	**0.07**
Grade 4	**38,122,386**	**58.62**	**0.24**
Grade 5	**6,055,608**	**75.57**	**0.75**
Grade 6	**-**	**0.00**	**0.00**
Grade 7	**-**	**0.00**	**0.00**
Grade 8 / Default	**-**	**0.00**	**0.00**
	103,072,641		

	2013		
Internal Credit Grades	Exposure at default	Exposure-weighted average risk-weight	Exposure-weighted average PD
	HK$'000	%	%
Grade 1	-	0.00	0.00
Grade 2	6,419,624	23.37	0.04
Grade 3	39,500,694	31.72	0.07
Grade 4	36,515,469	58.83	0.24
Grade 5	4,221,486	79.36	0.68
Grade 6	-	0.00	0.00
Grade 7	-	0.00	0.00
Grade 8 / Default	-	0.00	0.00
	86,657,273		

Notes to the Financial statements (continued)

14. Credit risk under the internal ratings-based approach (continued)

14.6 Risk assessment for retail exposures under IRB approach

The tables below show breakdown of retail exposures on a pool basis by expected loss percentage (EL%) range as at 31 December.

Residential mortgages

	2014	2013
	HK$'000	HK$'000
Up to 1%	**11,697,637**	11,506,539
>1%	**36,464**	59,100
Default	**7,916**	4,423
	11,742,017	11,570,062

Qualifying revolving retail

	2014	2013
	HK$'000	HK$'000
Up to 10%	**-**	-
>10%	**-**	-
Default	**-**	-
	-	-

Other retail to individuals

	2014	2013
	HK$'000	HK$'000
Up to 2%	**7,919,599**	6,038,363
>2%	**110,794**	111,983
Default	**2,491**	2,274
	8,032,884	6,152,620

Small business retail

	2014	2013
	HK$'000	HK$'000
Up to 1%	**2,078,789**	2,547,797
>1%	**46,372**	52,392
Default	**35,546**	30,118
	2,160,707	2,630,307

Notes to the Financial statements (continued)

14. Credit risk under the internal ratings-based approach (continued)

14.7 Analysis of actual loss and estimates

The table below shows the actual losses broken down by class of risk exposure, which represent the net charges (including write-offs and individually assessed impairment allowances) made by each class of exposures under the internal ratings-based approach for the year.

	2014	2013
	HK$'000	HK$'000
Corporate	**811,457**	195,492
Bank	**-**	-
Residential mortgages to individuals and property-holding shell companies	**3,653**	1,166
Qualifying revolving retail	**-**	-
Other retail to individuals	**5,750**	698
Small business retail	**4,056**	13,260
	824,916	210,616

Increase in the loan impairment charge of corporate exposures was mainly due to the increase in the amount of new classified or impaired loans in 2014.

The table below shows the expected loss broken down by class of risk exposure, which is the estimated loss likely to be incurred arising from the potential default of the obligors in respect of the exposure over a one-year period.

	Expected loss at 31 December 2013	Expected loss at 31 December 2012 (Restated)
	HK$'000	HK$'000
Corporate	**1,046,174**	1,061,792
Bank	**64,038**	40,003
Residential mortgages to individuals and property-holding shell companies	**6,249**	5,162
Qualifying revolving retail	**-**	-
Other retail to individuals	**25,832**	11,775
Small business retail	**19,598**	10,535
	1,161,891	1,129,267

The tables below set out the actual default rate compared against the estimated PD of the respective portfolio.

	Actual default rate during 2014	**Estimated PD at 31 December 2013**
	%	**%**
Corporate	**1.12**	**2.01**
Bank	**0.00**	**0.26**
Residential mortgages to individuals and property-holding shell companies	**0.04**	**0.57**
Qualifying revolving retail	**0.00**	**0.00**
Other retail to individuals	**0.10**	**0.79**
Small business retail	**0.96**	**1.42**

Notes to the Financial statements (continued)

14. Credit risk under the internal ratings-based approach (continued)

14.7 Analysis of actual loss and estimates (continued)

	Actual default rate during 2013	Estimated PD at 31 December 2012
	%	%
Corporate	0.62	2.03
Bank	0.00	0.19
Residential mortgages to individuals and property-holding shell companies	0.02	0.53
Other retail to individuals	0.07	0.73
Small business retail	1.44	1.51

It should be noted that expected loss and actual loss are measured and calculated using different methodologies compliant with relevant regulatory and accounting standards, which therefore may not be directly comparable. The limitation arises mainly from the fundamental differences in the definition of “loss”. The expected loss under Basel Accord which estimates the economic loss arising from the potential default of the obligor by taking into account the time value of money and including the direct and indirect costs associated with the recoveries on the credit exposures during the workout process, while actual loss is the net charge of individually assessed impairment allowances and write-offs made during the year in accordance with the accounting standards.

The actual default rate is measured by using the number of obligors (for wholesale exposures) or number of accounts (for retail exposures) defaulted whereas the estimated probability of default is an estimate of the long run average default rate over an economic cycle and is the estimated one-year forward-looking PD from the date of rating assignment.

Hence, actual default rate in a particular year (“point-in-time”) will typically differ from the estimated probability of default which is the “through-the-cycle” estimates as economies move above or below the cyclical norms.

The estimated probability of default is more conservative than the actual default rate for all asset classes.

Notes to the Financial statements (continued)

15. Credit risk under the standardised (credit risk) approach

15.1 Use of ratings from External Credit Assessment Institutions ("ECAI")

The Group continues to adopt STC approach based on external credit rating to determine the risk weight of the small residual credit exposures that was approved by HKMA to be exempted from FIRB approach and the following asset classes of exposures:

- Sovereign
- Public sector entity
- Multilateral development bank

The Group performs the ECAI issuer ratings mapping to its exposures in banking book in accordance with Part 4 of the Banking (Capital) Rules. The ECAIs recognised by the Group include Standard & Poor's, Moody's and Fitch.

15.2 Credit risk mitigation

For credit exposures adopting STC approach, the main types of recognised collaterals include cash deposits, debt securities and equities for non-past due exposures. In addition, real estate collateral is also recognised for past due exposures. The treatment of recognised collateral is compliant with the comprehensive approach for credit risk mitigation as mentioned in the Banking (Capital) Rules. For credit exposures under STC approach, the recognised guarantees for capital calculation include the guarantees given by sovereigns, public sector entities, multilateral development banks, or banks and those corporates with ECAI issuer ratings both exempted from FIRB approach for credit exposures, that have lower risk weights than the counterparty.

Besides, the recognised netting for credit risk mitigation includes derivatives subject to valid bilateral netting agreements.

Notes to the Financial statements (continued)

15. Credit risk under the standardised (credit risk) approach (continued)

15.3 Credit risk exposures other than securitisation exposures under the standardised (credit risk) approach

	2014						
	Total	Exposures after CRM*		Risk-weighted amount		Total exposures covered by recognised collateral	Total exposures covered by recognised guarantees
	Exposures	Rated	Unrated	Rated	Unrated		
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
On-balance sheet exposures							
Sovereigns	32,454,627	32,481,294	-	136,437	-	-	-
Public sector entities	419,432	395,107	-	27,978	-	-	26,667
Multilateral development banks	330,293	330,293	-	-	-	-	-
Banks	6,267,904	161,088	6,106,816	33,183	1,258,144	-	-
Securities firms	-	-	-	-	-	-	-
Corporates	8,490,939	-	8,428,030	-	8,428,030	62,909	-
Cash items	264	-	264	-	-	-	-
Regulatory retail	2,381,688	-	2,334,894	-	1,751,171	46,794	-
Residential mortgage loans	11,197,935	-	11,195,593	-	5,597,797	-	2,342
Other exposures which are not past due	602,837	-	444,236	-	561,191	158,601	-
Past due exposures	67,216	-	67,216	-	94,353	12,943	-
Total for on-balance sheet exposures	62,213,135	33,367,782	28,577,049	197,598	17,690,686	281,247	29,009
Off-balance sheet exposures							
Off-balance sheet exposures other than securities financing transactions and derivative contracts	366,704	25,570	341,134	5,114	314,349	-	4,759
Securities financing transactions and derivative contracts	9,781	-	9,781	-	7,714	-	-
Total for off-balance sheet exposures	376,485	25,570	350,915	5,114	322,063	-	4,759
Total for non-securitisation exposures	62,589,620	33,393,352	28,927,964	202,712	18,012,749	281,247	33,768
Exposures that are risk-weighted at 1,250%	-						

Notes to the Financial statements (continued)

15. Credit risk under the standardised (credit risk) approach (continued)

15.3 Credit risk exposures other than securitisation exposures under the standardised (credit risk) approach (continued)

	2013						
	Total Exposures	Exposures after CRM*		Risk-weighted amount		Total exposures covered by recognised collateral	Total exposures covered by recognised guarantees
		Rated	Unrated	Rated	Unrated		
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
On-balance sheet exposures							
Sovereigns	27,595,960	27,622,626	-	102,605	-	-	-
Public sector entities	664,230	638,986	-	56,253	-	-	26,667
Multilateral development banks	324,836	324,836	-	-	-	-	-
Banks	143,969	143,969	-	29,976	-	-	-
Corporates	6,757,537	116,331	6,631,485	116,331	6,631,485	9,721	-
Cash items	599	-	599	-	-	-	-
Regulatory retail	1,819,295	-	1,755,612	-	1,316,709	63,683	-
Residential mortgage loans	8,537,942	-	8,536,519	-	4,268,259	-	1,423
Other exposures which are not past due	695,770	-	589,761	-	689,706	106,010	-
Past due exposures	33,467	-	33,467	-	35,200	30,000	-
Total for on-balance sheet exposures	46,573,605	28,846,748	17,547,443	305,165	12,941,359	209,414	28,090
Off-balance sheet exposures							
Off-balance sheet exposures other than securities financing transactions and derivative contracts	625,438	429,175	196,264	224,736	167,817	-	5,171
Securities financing transactions and derivative contracts	29,638	-	29,639	-	23,350	-	-
Total for off-balance sheet exposures	655,076	429,175	225,903	224,736	191,167	-	5,171
Total for non-securitisation exposures	47,228,681	29,275,923	17,773,346	529,901	13,132,526	209,414	33,261
Exposures that are risk-weighted at 1,250%	-						

* Recognised credit risk mitigation satisfying the requirements and conditions set out in the Banking (Capital) Rules.

Notes to the Financial statements (continued)

16. Counterparty credit risk-related exposures

The Group's counterparty credit risk arising from derivative contracts and securities financing transactions both in trading and banking book is subject to the same risk management framework as mentioned in Note 2 to the Financial statements. The Group establishes credit limit through formal credit approval procedures to control the pre-settlement credit risk arising from derivative transactions and settlement limit to control the settlement risk arising from foreign exchange-related transactions for counterparties in both the trading book and banking book. The Group monitors the risk exposure due to fluctuations in the market by using the current exposure and the potential exposure value of the transactions. Exceptions or excesses are timely and closely identified and monitored by risk management unit.

Credit equivalent amount and capital charge for the relevant counterparty credit exposures are determined following the regulatory capital requirements. Currently, the Group has adopted the Current Exposure Method to measure the relevant credit equivalent amount, which comprises current exposures and potential future exposures. The relevant counterparty default risk capital charge is calculated under the FIRB/STC approach. In addition, the Group has adopted standardised credit valuation adjustment ("CVA") method to calculate the relevant counterparty CVA capital charge.

The Group establishes prudent eligibility criteria and haircut policy of debt securities being pledged as collateral for securities financing transactions.

The Group formulates policy for classification of credit assets according to the PD of counterparties and the period of overdue. If there is objective evidence that an impairment loss has been incurred, impairment allowance will be provided according to HKFRS and regulatory requirements.

In controlling and monitoring of wrong-way risk (risk of existence of positive correlation between the PD of a counterparty and credit exposures driven by mark-to-market value of the underlying transactions), specific wrong-way risk transactions are generally not allowed and monitoring measures have been formulated for those counterparties identified by stress testing that would be exposed to potential general wrong-way risk.

Notes to the Financial statements (continued)

16. Counterparty credit risk-related exposures (continued)

16.1 Counterparty credit risk exposures under the internal ratings-based approach

The following table summarises the Group's exposures to counterparty credit risk arising from securities financing transactions and derivative contracts calculated using the Current Exposure Method. There is no effect of valid cross-product netting agreements on these exposures.

	2014		2013	
	Securities financing transactions	**Derivative contracts**	Securities financing transactions	Derivative contracts
	HK$'000	**HK$'000**	HK$'000	HK$'000
Gross total positive fair value		**86,822**		107,654
Default risk exposures after the effect of valid bilateral netting agreements	**2,763,929**	**418,634**	1,282,671	476,445
Less: Value of recognised collateral				
- debt securities	**-**	**-**	-	-
- others	**(2,061,803)**	**-**	(1,262,875)	-
Default risk exposures after the effect of valid bilateral netting agreements net of recognised collateral	**702,126**	**418,634**	19,796	476,445
Default risk exposures by counterparty type				
Corporate	**-**	**102,812**	-	138,480
Bank	**2,763,929**	**315,822**	1,282,671	337,965
	2,763,929	**418,634**	1,282,671	476,445
Risk-weighted amounts by counterparty type				
Corporate	**-**	**111,619**	-	184,443
Bank	**291,016**	**101,312**	5,304	113,139
	291,016	**212,931**	5,304	297,582

Notes to the Financial statements (continued)

16. Counterparty credit risk-related exposures (continued)

16.2 Counterparty credit risk exposures under the standardised (credit risk) approach

The following table summarises the Group's exposures to counterparty credit risk arising from derivative contracts calculated using the Current Exposure Method. There is no effect of valid cross-product netting agreements on these exposures.

	2014		2013	
	Securities financing transactions	Derivative contracts	Securities financing transactions	Derivative contracts
	HK$'000	HK$'000	HK$'000	HK$'000
Gross total positive fair value		352,250		25,593
Default risk exposures after the effect of valid bilateral netting agreements	-	9,781	-	29,639
Less: Value of recognised collateral				
- debt securities	-	-	-	-
- others	-	-	-	-
Default risk exposures after the effect of valid bilateral netting agreements net of recognised collateral	-	9,781	-	29,639
Default risk exposures by counterparty type				
Sovereigns	-	-	-	-
Public sector entities	-	-	-	-
Corporates	-	1,488	-	4,484
Regulatory retail	-	8,265	-	25,155
Other exposures which are not past due	-	28	-	-
Past due exposures	-	-	-	-
	-	9,781	-	29,639
Risk-weighted amounts by counterparty type				
Sovereigns	-	-	-	-
Public sector entities	-	-	-	-
Corporates	-	1,488	-	4,484
Regulatory retail	-	6,198	-	18,866
Other exposures which are not past due	-	28	-	-
Past due exposures	-	-	-	-
	-	7,714	-	23,350

Notes to the Financial statements (continued)

17. Assets securitisation

There was no assets securitisation for which the Group is an investing institution at 31 December 2014 (2013: Nil).

18. Capital charge for market risk

	2014	2013
	HK$'000	HK$'000
Under the standardised (market risk) approach		
Foreign exchange exposures (net)	**-**	-
Interest rate exposures		
- non-securitisation exposure	**-**	10
Commodity exposures	**-**	-
Equity exposures	**-**	-
Under the internal models approach		
General foreign exchange and interest rate exposures	**45,648**	77,199
Capital charge for market risk	**45,648**	77,209

Notes to the Financial statements (continued)

18. Capital charge for market risk (continued)

Market risk regulatory capital charge is calculated under the Banking (Capital) (Amendment) Rules 2011 to incorporate capital charge for stressed VAR. The following table sets out the IMM VAR and stressed VAR[1] for the general market risk exposure calculated under the IMM approach of the Group.

	Year	At 31 December HK$'000	Minimum for the year HK$'000	Maximum for the year HK$'000	Average for the year HK$'000
IMM VAR for foreign exchange and interest rate risk	2014	1,868	1,868	4,120	3,064
	2013	3,479	3,479	7,502	5,730
IMM VAR for foreign exchange risk	2014	1,597	1,597	4,156	3,094
	2013	3,634	3,634	7,552	5,641
IMM VAR for interest rate risk	2014	765	652	2,554	1,956
	2013	1,658	274	1,688	739
Stressed VAR for foreign exchange and interest rate risk	2014	8,825	7,683	33,097	16,191
	2013	14,085	7,651	31,968	14,556
Stressed VAR for foreign exchange risk	2014	1,957	1,957	8,098	7,193
	2013	8,216	5,708	9,207	7,716
Stressed VAR for interest rate risk	2014	8,273	3,532	31,258	14,119
	2013	10,102	2,170	25,053	8,719

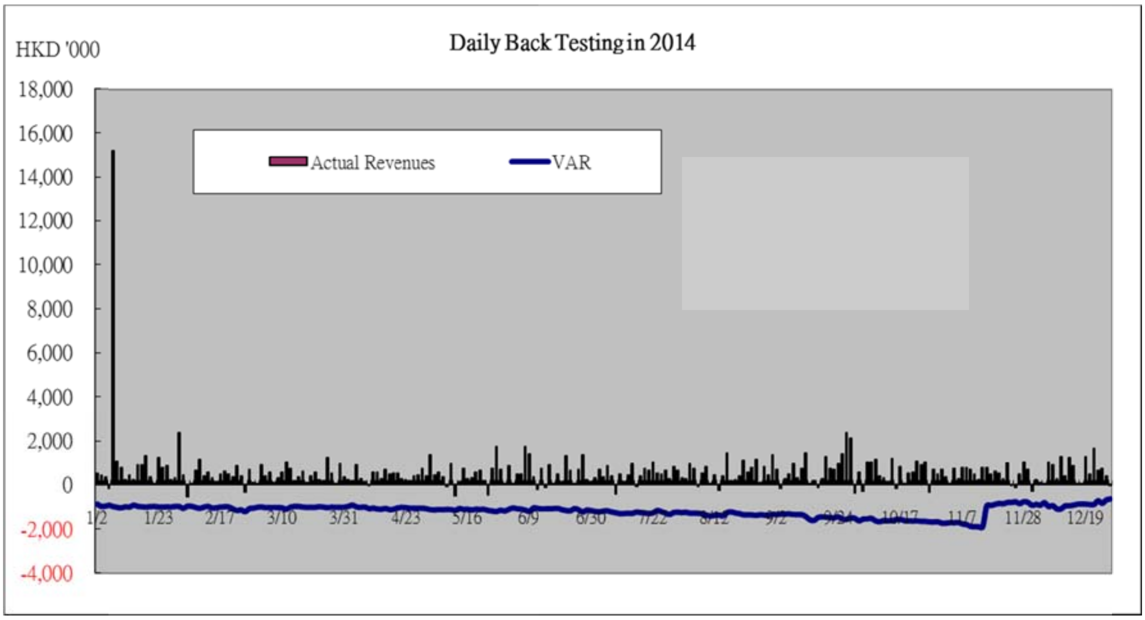
Note:

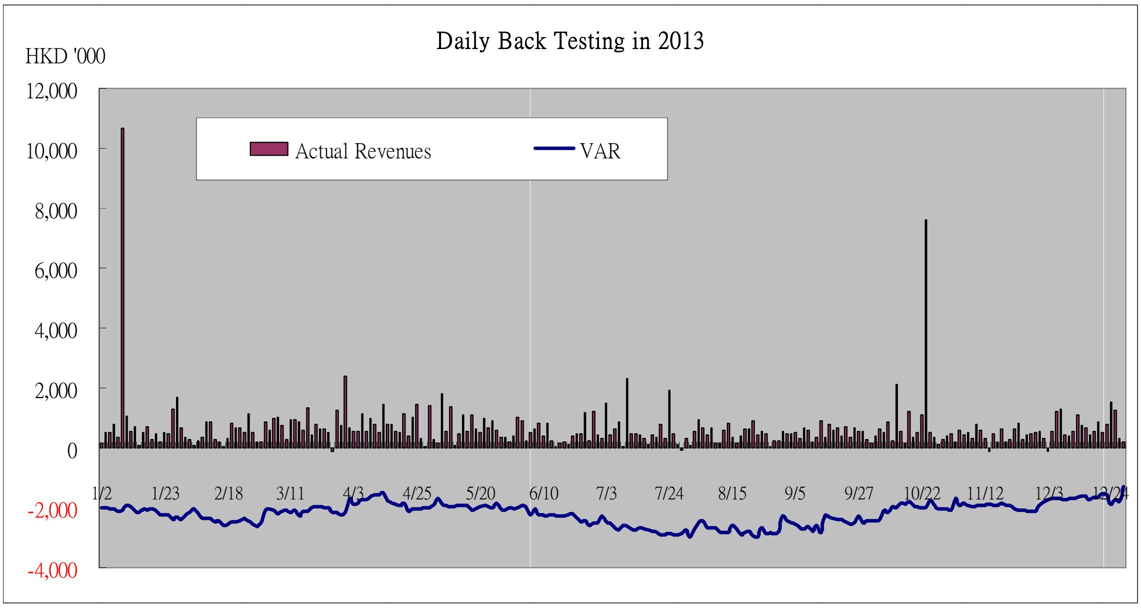
1. IMM VAR and stressed VAR measures used for market risk regulatory capital purposes are calculated to a 99% confidence level and use a 10-day holding period. The stressed VAR uses the same methodology as the VAR model and is generated with inputs calibrated to the historical market data from a continuous 12-month period of significant financial stress relevant to the Group's portfolio.

Notes to the Financial statements (continued)

18. Capital charge for market risk (continued)

The graph below shows the regulatory back-testing result of the Group's market risk under IMM approach.





There was no actual loss exceeding the VAR for the Group as shown in the back-testing results.

Notes to the Financial statements (continued)

19. Capital charge for operational risk

	2014	2013
	HK$'000	HK$'000
Capital charge for operational risk	**900,408**	775,167

The Group uses the standardised (operational risk) approach to calculate its operational risk capital charge.

20. Equity exposures in banking book

Equity holdings in other entities are accounted for in accordance with the underlying intentions of holdings at the inception of acquisition. The classifications for equity holdings taken for relationship and strategic purposes will be separated from those taken for other purposes (including capital appreciation). Investments in equity shares which are intended to be held on a continuing basis, but which do not comprise investments in subsidiaries, are classified as available-for-sale securities and are reported in the balance sheet as "Investment in securities".

For equity exposures in banking book other than subsidiaries, the Group applies the same accounting treatment and valuation methodologies as detailed in the Notes 1.9(4), 1.12, 1.13 and 1.15 to the Financial statements, further details on their valuation are outlined in Note 3.1 "Financial instruments measured at fair value" to the Financial statements. If additional investment is made subsequently such that an investee becomes an associate, joint venture or subsidiary, then the investment is reclassified in accordance with the Group's accounting policies.

Gains or losses related to equity exposures are summarised below:

	2014	2013
	HK$'000	HK$'000
Realised gains from sales	**-**	-
Unrealised gains on revaluation recognised in reserves but not through income statement	**64,576**	52,775

Corporate Governance

The Group strives to achieve high standards of corporate governance and has followed CG-1 "Corporate Governance of Locally Incorporated Authorised Institutions" of the Supervisory Policy Manual issued by the Hong Kong Monetary Authority.

Board of Directors and the Management

The Board is responsible for setting objectives and formulating long term strategies as well as managing the Group's overall business. It currently comprises seven Directors with a variety of different experience and professionalism. Among them, two are Executive Directors, while the remaining five are Non-executive Directors. Of the five Non-executive Directors, three are Independent Non-executive Directors whose indispensable function is to provide independent scrutiny. The Board meets regularly and four board meetings were held in the year with an average attendance rate of 97%. The Management, led by the Chief Executive, is responsible for formulating and implementing detailed programmes to effect the approved strategies and policies, and providing detailed reports on the Group's performance to the Board on a regular basis to enable the Board to discharge its responsibilities effectively. In order to focus its attention on strategic and material issues that have significant impact on the Group's finances and long-term development, the Board has set up four committees to oversee the major areas of the Group. Details of the committees are given below:

Executive Committee

The Executive Committee has been delegated with power directly from the Board to handle matters which require the Board's review during the adjournment of the Board. Its responsibilities include:

- approving policies, implementing plans and management measures to effect the group-wide development strategies and business plans approved by the Board;
- reviewing the progress on implementation of the strategies and business plans;
- recommending strategic proposals to the Board for its consideration and approval; and
- approving the Group's rules and regulations according to the policies imposed by the supervisory authorities and the holding company.

The members of Executive Committee during the year were Mr. Fang Hongguang (Chairman) and Mr. Chan Sai Ming. Both of them were Executive Directors of the Bank.

Corporate Governance (continued)

Audit Committee

The Committee assists the Board in fulfilling its oversight role over the Group in the following areas:

- integrity of financial statements and the financial reporting process;
- internal control system;
- performance of internal audit functions and internal auditors;
- appointment of external auditors and evaluation of external auditors' qualifications, independence and performance;
- periodic review and annual audit of the Group's financial statements;
- compliance with applicable accounting standards and legal and regulatory requirements on financial disclosures; and
- enhancement of the corporate governance framework.

The members of Audit Committee during the year were Mr. Lau Hon Chuen (Chairman), Mr. Lan Hong Tsung David and Ms. Zhu Yanlai. All were Non-executive Directors of the Bank. Among them, Mr. Lau Hon Chuen and Mr. Lan Hong Tsung David were Independent Non-executive Directors.

Risk Management Committee

The Risk Management Committee assists the Board in performing the duties in respect of the risk management of the Bank in, among others, the following areas:

- formulation of the risk appetite and risk management strategy of the Bank and determination of the Bank's risk profile;
- identification, assessment and management of material risks faced by the Bank;
- the review and assessment of the adequacy of the Bank's risk management policies, system and internal control, including the Bank's compliance with prudential, legal and regulatory requirements governing the businesses of the Bank;
- review and approval of high-level risk-related policies of the Bank; and
- review an approval of significant or high risk exposures or transactions.

The members of the Risk Management Committee during the year were Mr. Li Jiuzhong (Chairman), Mr. Fang Hongguang, Mr. Chang Hsin Kang, Mr. Lau Hon Chuen and Mr. Chan Sai Ming. All were Directors of the Bank. Among them, Mr. Chang Hsin Kang and Mr. Lau Hon Chuen were Independent Non-executive Directors.

Corporate Governance (continued)

Nomination and Remuneration Committee

The Nomination and Remuneration Committee comprises three members, including one Non-executive Director, Ms. Zhu Yanlai, and two Independent Non-executive Directors, namely Mr. Lau Hon Chuen and Mr. Lan Hong Tsung David. It was chaired by Mr. Lan Hong Tsung David, an Independent Non-executive Director of the Board. The Independent Non-executive Directors represent 66.7% of the Committee members.

The Nomination and Remuneration Committee assists the Board in performing the duties in respect of the Group in, among others, the following areas:

- human resources, remuneration strategy and incentive framework of the Group;
- selection and nomination of Directors, Board Committee members and certain senior executives as designated by the Board from time to time (defined as "Senior Management");
- structure, size and composition (including but not limited to gender, age, cultural and educational background, ethnicity, geographical location, professional experience, skills and knowledge etc.) of the Board and Board Committees;
- remuneration of Directors, Board Committee members, Senior Management and Key Personnel;
- effectiveness of the Board and Board Committees; and
- training and continuous professional development of Directors and Senior Management.

Key tasks performed by the Nomination and Remuneration Committee during 2014 included the approval, review and proposal to the Board on the following according to the responsibilities and authorities:

- formulation, review and amendment on major human resources and remuneration policies, including the review of the "Deferred Variable Remuneration Policy"; as well as the review of "Senior Management", "Key Personnel", "Key Employee Group" and "Risk Control Personnel" as delineated in the "Guideline on a Sound Remuneration System" published by Hong Kong Monetary Authority;
- performance appraisal result of the Senior Management and Key Personnel for year 2013;
- proposal on staff bonus for year 2013 and salary adjustment for year 2014 of the Senior Management and Key Personnel;
- key performance indicators of the Senior Management and Key Personnel for year 2014;
- review of the Mandate, Working Rules and Standing Agenda of the Nomination and Remuneration Committee;
- review of the Directors' Independency Policy;
- review of the Guidelines for the Annual Self Evaluation Report of the Board and Board Committees and the questionnaires for the Annual Self Evaluation of the Board and Board Committees for year 2014;
- election of Directors for 2014;
- Directors' independency report for 2013;
- self-evaluation report of the Board and Board Committees for 2013;
- consideration of the matters relating to the adjustment and appointment of the Directors of the Group;
- consideration of the appointment and resignation of Key Personnel;

There were two Nomination and Remuneration Committee meetings held during 2014. The attendance rate of the three Directors was 83.3%.

Corporate Governance (continued)

Remuneration and Incentive Mechanism

The Remuneration and Incentive Mechanism of the Group is based on the principles of "effective motivation" and "sound remuneration management". It links remuneration with performance and risk factors closely. It serves to encourage staff to enhance their performance, and at the same time, to strengthen their awareness of risk so as to achieve sound remuneration management.

The Remuneration and Incentive Policy of the Group is generally in line with the broad principles set out in the HKMA's "Guideline on a Sound Remuneration System" and applicable to Nanyang Commercial Bank Limited and all of its subsidiaries (including the branches and subsidiaries within and outside Hong Kong).

- **"Senior Management" and "Key Personnel"**

  The following groups of employees have been identified as the "Senior Management" and "Key Personnel" as defined in the HKMA's "Guideline on a Sound Remuneration System":

  - "Senior Management": The senior executives designated by the Board who are responsible for oversight of the group-wide strategy or material business lines, including Chief Executive and Deputy General Managers.

  - "Key Personnel": The employees whose individual business activities involve the assumption of material risk which may have significant impact on risk exposure, or whose individual responsibilities are directly and materially linked to the risk management, or those who have direct influence to the profit, including heads of material business lines, Head of Treasury, as well as Head of Risk Management Department.

- **Determination of the Remuneration Policy**

  To fulfill the above-mentioned principles and to facilitate effective risk management within the framework of the Remuneration Policy of the Group, Human Resources Division is responsible for proposing the Remuneration Policy of the Group and will seek consultation of the risk control units including risk management, financial management and compliance if necessary, in order to balance the needs for staff motivations, sound remuneration and prudent risk management. The proposed Remuneration Policy will be submitted to the Nomination and Remuneration Committee for review and thereafter to the Board of Directors for approval. The Nomination and Remuneration Committee and the Board of Directors will seek opinions from other Board Committees (e.g. Risk Management Committee, Audit Committee, etc.) where they consider necessary.

Corporate Governance (continued)

Remuneration and Incentive Mechanism (continued)

- **Key Features of the Remuneration and Incentive Mechanism**

1. Performance Management Mechanism

To reflect the "performance-driven" corporate culture, the Group has put in place a performance management mechanism to formalise the performance management at the levels of the Group, units and individuals. The annual targets of the Group will be cascaded down under the framework of balanced scorecard whereby the performance of the Senior Management and different units (including business units, risk control units and other units) would be assessed from the perspectives of financial, customer, building blocks/key tasks, human capital, risk management and compliance. For individual staff at different levels, annual targets of the Group will be tied to their job requirements through the performance management mechanism. Performance of individuals will be appraised on their achievement against targets, their contribution towards performance of their units and fulfilment of risk management duties and compliance, etc. Not only is target accomplishment taken into account, but the risk exposure involved during the course of work could also be evaluated and managed, ensuring security and normal operation of the Group.

2. Risk Adjustment of Remuneration

To put the principle of aligning performance and remuneration with risk into practice, based on "The Risk Adjustment Method" of BOCHK, the key risk modifiers of the bank have been incorporated into the performance management mechanism of the Group. Credit risk, market risk, interest rate risk, liquidity risk, operational risk, legal risk, compliance risk and reputation risk form the framework of "The Risk Adjustment Method". The size of the variable remuneration pool of the Group is calculated according to the risk adjusted performance results approved by the Board of BOCHK and is subject to its discretion. This method ensures the Group to fix the Group's variable remuneration pool after considering risk exposures and changes and to maintain effective risk management through the remuneration mechanism.

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Corporate Governance (continued)

Remuneration and Incentive Mechanism (continued)

- **Key Features of the Remuneration and Incentive Mechanism (continued)**

3. Performance-based and Risk-adjusted Remuneration Management

The remuneration of staff is composed of "fixed remuneration" and "variable remuneration". The proportion of one to the other for individual staff members depends on job grades, roles, responsibilities and functions of the staff with the prerequisite that balance has to be struck between the fixed and variable portion. Generally speaking, the higher the job grades and/or the greater the responsibilities, the higher will be the proportion of variable remuneration so as to encourage the staff to follow the philosophy of prudent risk management and sound long-term financial stability.

Every year, the Group will conduct periodic review on the fixed remuneration of the staff with reference to various factors like remuneration strategy, market pay trend and staff salary level, and will determine the remuneration based on the affordability of the Group as well as the performance of the Group, units and individuals. As mentioned above, performance assessment criteria include quantitative and qualitative factors, as well as financial and non-financial indicators.

According to the Group Bonus Funding Policy of BOCHK, the size of the variable remuneration pool of the Group is determined by the Board of BOCHK on the basis of the financial performance of the Group and the achievement of non-financial strategic business targets under the long-term development of the BOCHK Group. Thorough consideration is also made to the risk factors in the determination process. The size of the pool is reached based on pre-defined formulaic calculations but the Board of BOCHK can make discretionary adjustment to it if deemed appropriate under prevailing circumstances. When the BOCHK group's performance is relatively weak (e.g. failed to meet the threshold performance level), no variable remuneration will be paid out that year in principle. However, the Board of BOCHK reserves the rights to exercise its discretion.

As far as individual units and individual staff are concerned, allocation of the variable remuneration is closely linked to the performance of the units, and that of each individual staff as well as the unit he/she is attaching to, and the assessment of which should include risk modifiers. The performance and remuneration arrangement of risk control personnel are determined by the achievement of their core job responsibilities, independent from the business they oversee; for front-line risk controllers, a cross-departmental reporting and performance management system is applied to ensure the suitability of performance-based remuneration. Within the acceptable risk level of the Group, the better the performance of the unit and the individual staff, the higher will be the variable remuneration for the individual staff.

Corporate Governance (continued)

Remuneration and Incentive Mechanism (continued)

- **Key Features of the Remuneration and Incentive Mechanism (continued)**

4. Linking the payout of the variable remuneration with the time horizon of the risk to reflect the long-term value creation of the Group

To work out the principle of aligning remuneration with the time horizon of risk and to ensure that sufficient time is allowed to ascertain the associated risk and its impact before the actual payout, payout of the variable remuneration of staff is required to be deferred in cash if such amount reaches certain prescribed threshold. The Group adopts a progressive approach towards deferral. The longer the time horizon of risk in the activities conducted by the staff, the higher the job grade or the higher amount of the variable remuneration, the higher will be the proportion of deferral. Deferral period lasts for 3 years.

The vesting of the deferred variable remuneration is linked with the long term value creation of the Group. The vesting conditions are closely linked to the annual performance of the BOCHK Group in the next 3 years and the individual behaviour of the staff concerned. When the BOCHK Group's performance has met the threshold requirement, the deferred variable remuneration would be vested following the corresponding schedule. However, if a staff is found to have committed fraud, or any financial or non-financial factors used in performance measurement or variable pay determination are later proven to have been manifestly worse than originally understood in a particular year, or individual behaviour / management style pose negative impacts to the business unit and even the Group, including but not limited to improper or inadequate risk management, etc., the unvested portion of the deferred variable remuneration of the relevant staff would be forfeited.

- **Disclosure on remuneration**

The Group has fully complied with the guideline in Part 3 of the "Guideline on a Sound Remuneration System" issued by the HKMA to disclosure information in relation to our remuneration and incentive mechanism.