SHANGHAI COMMERCIAL BANK



2011
ANNUAL REPORT

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CORPORATE PROFILE

Established in November 1950, Shanghai Commercial Bank is one of the renowned local Chinese banks in Hong Kong and has a niche market position in the corporate and trade finance sectors.

The Bank has always been pursuing the motto of its founder, Mr. Kwang-pu Chen, to 'Serve the Community'. The Bank's slogan of 'For Personalized Service' and 'All in a Family' denotes the Bank's devotion to providing personalized services to its clients and promoting a harmonious relationship among its staff members.

The Bank offers a comprehensive range of retail and corporate banking services and products including deposits, securities trading, credit cards, wealth management services and corporate and personal loans.

At present, Shanghai Commercial Bank has 43 branches in Hong Kong, 1 branch in Shenzhen, 1 representative office in Shanghai, and 4 overseas branches in London, New York, Los Angeles and San Francisco.

FIVE-YEAR FINANCIAL SUMMARY

	2011	2010	2009	2008	2007
FOR THE YEAR (IN HK$ MILLION)					
Net interest income	1,982	1,893	1,735	1,966	2,036
Other operating income	1,057	1,251	1,159	958	1,569
Operating expenses	884	1,040	1,264	1,004	973
Operating profit	2,174	2,020	1,572	1,547	2,534
Profit before other comprehensive income attributable to equity holders	1,798	1,701	1,336	1,185	2,199
Dividend	860	860	800	800	1,100
AT YEAR END (IN HK$ MILLION)					
Shareholders' funds	18,022	17,114	16,034	14,833	14,886
Total assets	126,978	118,642	112,910	109,749	108,025
Total deposits	103,097	95,463	91,489	89,532	82,113
Total loans and advances	55,480	51,028	44,340	50,168	46,128
FINANCIAL RATIOS					
Capital adequacy ratio	18%	19%	19%	19%	20%
Liquidity ratio	47%	51%	55%	47%	52%
Loan to deposit ratio*	53.81%	57.11%	52.03%	58.06%	59.09%
Dividend to profit before other comprehensive income payout ratio	47.82%	50.57%	59.88%	67.49%	50.02%
Return on average assets	1.46%	1.47%	1.20%	1.09%	2.18%

* Loan to deposit ratio for Year 2011 is stated based on total loans and advances including trade financing loans to total deposits. (Year 2007 to Year 2010 was stated based on total loans and advances, trade bills and holdings of debt securities issued by corporations to total deposits.)

NOTICE OF ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that the Sixty-first Annual General Meeting of the Members of the Bank will be held at its Registered Office, 35/F., Gloucester Tower, The Landmark, 15 Queen's Road Central, Hong Kong on Friday, 20th April 2012 at 10:15 a.m. to transact the following business:

(1) To receive and consider the audited financial statements and the Reports of the Directors and of the Auditors for the year ended 31st December 2011;
(2) To declare Dividend in respect of the year 2011;
(3) To elect Directors;
(4) To approve the payment of Directors' fees for the year ended 31st December 2011;
(5) To re-appoint Auditors and to authorise the Directors to fix their remuneration.

A Member entitled to attend and vote at the Meeting is entitled to appoint a proxy to attend and vote instead of him. A proxy need not also be a Member.

The Register of Members of the Bank will be closed from Friday, 13th April 2012 to Friday, 20th April 2012, both days inclusive.

By Order of the Board
May Yuen-ling Kwok
Corporate Secretary

Hong Kong, 18th January 2012

BOARD OF DIRECTORS



Front row from left to right	Mr. Richard Jason Lloyd Yorke, Mr. David Allen Hoyt, Mr. Lincoln Chu Kuen Yung, Mr. Hung-ching Yung, Mr. Stephen Ching Yen Lee, Mr. Shen Ruolei, Mdm. Ning Li Ming.
Back row from left to right	Mr. Edward Kawah Chu, Dr. Richard Lee, Mr. David Sek-chi Kwok, Mr. Johnson Mou Daid Cha, Mr. Chen Yih Pin, Mr. Gordon Che Keung Kwong.

Lincoln Chu Kuen Yung, JP
Chairman & Non-executive Director

David Sek-chi Kwok
Chief Executive & Managing Director

Hung-ching Yung, JP

Shen Ruolei
(Ye Jun, Alternate)

David Joseph Zuercher (resigned on 15th June 2011)
(Clifford Sterling Lawrence, Alternate) (ceased on 15th June 2011)

*** Dr. Richard Lee**

*** Johnson Mou Daid Cha**
(Dr. Lam Chat Yu, Alternate)

Stephen Ching Yen Lee

Edward Kawah Chu

David Allen Hoyt
(Ignatius Wooi-kean Choong, Alternate)

Chen Yih Pin
(Yi-Jen Chiou, Alternate)

*** Gordon Che Keung Kwong**

Ning Li Ming
(Li Jian Guo, Alternate)

Richard Jason Lloyd Yorke (appointed on 15th June 2011)
(Clifford Sterling Lawrence, Alternate) (appointed on 15th June 2011)

* Independent Non-executive Directors

MANAGEMENT

EXECUTIVES

Chief Executive & Managing Director	David Sek-chi Kwok	
Director & Assistant General Manager	Edward Kawah Chu	
Assistant General Managers	Henry Koon-man To Paul Kun-kow Wong Daniel Kwok-hung Chan Burton Chi-shan Cheng Stephen Siu-fung Lee Frank Shui-sang Jin Hon-ming Mak	
Senior Managers	Pui-man Yeung Zachary Wing-kwong Kwan	Danny Kong-keung Tsang Francis Yue-cheong Wong
Managers	Albert Tak-wo Leung Vincent Chi-wing Man Thomas Chee-kin Lo Stephen Wing-hing Lai Eric Kai-chiu Fok	Annie Wai-yu Cheung Michael Yiu-wing Fung Jenny Chui-yeung Chau Tim Yuen

OVERSEAS BRANCHES

Los Angeles Branch
Executive Vice President & Manager — Ching-hsing Kao

New York Branch
Senior Vice President & Manager — Timothy Kam-tim Chan

San Francisco Branch
Senior Vice President & Manager — Philip She-hoi Lee

London Branch
Manager — Frederick Yan Chu

MAINLAND BRANCH

Shenzhen Branch
Manager — Vincent Chi-wing Man

MAINLAND REPRESENTATIVE OFFICE

Shanghai Representative Office
Chief Representative — Chen Li Ying

DIRECTORS

MR. LINCOLN CHU KUEN YUNG, JP

Aged 66. Chairman and Non-executive Director. Mr. Yung was appointed a Director of the Bank since September 1998 and was elected Chairman in December 2007. He has been a Director of The Shanghai Commercial & Savings Bank, Ltd. since March 1991, where he served as Managing Director from 1994 to 2004. He is currently the Chairman of Paofoong Insurance Company (Hong Kong) Limited, the Deputy Managing Director of Nanyang Holdings Limited and is also an Independent Non-executive Director of Tai Ping Carpets International Limited. Mr. Yung has extensive experience in the textile industry, banking and investment. He was a member of the Basic Law Consultative Committee (from 1985 to 1990) and has been involved in various government committees.

MR. DAVID SEK-CHI KWOK

Aged 58. Chief Executive and Managing Director of the Bank. Joined the Bank in October 1971. Appointed a Director in October 2001. General Manager since July 2004, and Chief Executive and Managing Director since October 2007.

MR. HUNG-CHING YUNG, JP

Aged 89. Appointed a Director of the Bank in March 1973. Managing Director of Nanyang Holdings Limited. Chairman of The Shanghai Commercial & Savings Bank, Ltd. A Director of Paofoong Insurance Company (Hong Kong) Limited and The Wing On Enterprises, Limited.

MR. SHEN RUOLEI

Aged 66. Appointed a Director of the Bank in March 1999. Executive Director of Shanghai United International Investment Limited. A Director of Bank of Shanghai.

DR. RICHARD LEE

Aged 74. Appointed a Director of the Bank in April 2001. Chairman of TAL Apparel Limited and a Director of Jardine Matheson Holdings Limited, Hongkong Land Holdings Limited and Mandarin Oriental International Limited.

MR. JOHNSON MOU DAID CHA

Aged 60. Appointed a Director of the Bank in September 2001. Director of Mingly Corporation, HKR International Limited, Hanison Construction Holdings Limited and China International Capital Corporation Limited. Member of the Council, Finance Committee and Investment Sub-committee of The Chinese University of Hong Kong.

MR. STEPHEN CHING YEN LEE

Aged 65. Appointed a Director of the Bank in June 2004. Managing Director of The Shanghai Commercial & Savings Bank, Ltd., Great Malaysia Textile Investments Private Limited, Director of COFCO Corporation and Chairman of Singapore Airlines Limited.

MR. EDWARD KAWAH CHU

Aged 56. Assistant General Manager of the Bank. Joined the Bank in December 1979. Appointed a Director in February 2005. Alternate Chief Executive since October 2007.

MR. DAVID ALLEN HOYT

Aged 56. Appointed a Director of the Bank in April 2006. Senior Executive Vice President, Wholesale Banking, Wells Fargo & Company.

MR. CHEN YIH PIN

Aged 72. Appointed a Director of the Bank in April 2006 and had served as an Alternate Director of the Bank from June 2004 to April 2006. Resident Managing Director of The Shanghai Commercial & Savings Bank, Ltd.

MR. GORDON CHE KEUNG KWONG

Aged 62. Appointed a Director of the Bank in August 2008. Chairman of the Audit Committee of the Bank since January 2009. A fellow member of the Institute of Chartered Accountants in England and Wales, and the Hong Kong Institute of Certified Public Accountants. An Independent Non-executive Director of a number of locally listed companies, including Chow Tai Fook Jewellery Group Limited, NWS Holdings Limited, Henderson Land Development Company Limited, and China COSCO Holdings Company Limited.

MDM. NING LI MING

Aged 62. Appointed a Director of the Bank in July 2009. Director of Shanghai United International Investment Limited and Shenergy Company Limited.

MR. RICHARD JASON LLOYD YORKE

Aged 44. Appointed a Director of the Bank in June 2011. Executive Vice President & Group Head International, Wells Fargo Bank, N.A. A Director of Wells Fargo International Banking Corporation and Wells Fargo Bank International, Ireland.

MR. IGNATIUS WOOI-KEAN CHOONG

Aged 50. Served as an Alternate Director of the Bank since January 1997. Appointed an Alternate Director to Mr. David Allen Hoyt in April 2006. Managing Director, Asia Investment Management, Wells Fargo Bank, N.A.

DR. LAM CHAT YU

Aged 60. Appointed an Alternate Director to Mr. Johnson Mou Daid Cha in May 2002. He has more than 30 years of experience in asset management and technology investment in Silicon Valley, California and Asia. He is a Non-executive Director of Mingly Corporation.

MR. CLIFFORD STERLING LAWRENCE

Aged 63. Served as an Alternate Director of the Bank since January 2007. Appointed an Alternate Director to Mr. Richard Jason Lloyd Yorke in June 2011. Executive Vice President, Wells Fargo Bank, N.A.

MR. YI-JEN CHIOU

Aged 54. Appointed an Alternate Director to Mr. Chen Yih Pin in February 2007. Director and President of The Shanghai Commercial & Savings Bank, Ltd.

MR. YE JUN

Aged 39. Appointed an Alternate Director to Mr. Shen Ruolei in July 2009. Director of Bank of Shanghai, Shanghai United International Investment Limited and United MetLife Insurance Company Limited.

MR. LI JIAN GUO

Aged 48. Appointed an Alternate Director to Mdm. Ning Li Ming in August 2009. Vice President of Bank of Shanghai. Director of Shanghai United International Investment Limited.

SENIOR MANAGEMENT

MR. DAVID SEK-CHI KWOK

(Biographical details are set out on page 8)

MR. EDWARD KAWAH CHU

(Biographical details are set out on page 9)

MR. HON-MING MAK

Aged 60. Assistant General Manager & Chief of Corporate Banking of the Bank. Joined the Bank in March 1971.

MR. PAUL KUN-KOW WONG

Aged 60. Assistant General Manager & Chief of Treasury of the Bank. Joined the Bank in February 1974.

MR. HENRY KOON-MAN TO

Aged 59. Assistant General Manager & Chief Financial Controller of the Bank. Joined the Bank in December 1988.

MR. BURTON CHI-SHAN CHENG

Aged 50. Assistant General Manager & Chief of Information Technology & Operations of the Bank. Rejoined the Bank in August 1996.

MR. DANIEL KWOK-HUNG CHAN

Aged 50. Assistant General Manager & Chief of Organization and Methods of the Bank. Rejoined the Bank in March 2008.

MR. STEPHEN SIU-FUNG LEE

Aged 45. Assistant General Manager & Chief of Retail Banking of the Bank. Joined the Bank in March 2010.

MR. FRANK SHUI-SANG JIN

Aged 54. Assistant General Manager & Chief of General Administration of the Bank. Joined the Bank in May 2010.

MR. PUI-MAN YEUNG

Aged 59. Chief Auditor of the Bank. Rejoined the Bank in May 1982.

CELEBRATING OUR 60 YEARS IN HONG KONG









60 YEARS in Hong Kong




60 YEARS
in Hong Kong


60 YEARS





The 12th Tripartite Partnership Conference
第十二屆滬港台“上海銀行”業務研討會

合作創新　通路造富　全球發展

三地上銀　一心為您







The Bank signed a memorandum of understanding (MOU) with China's Bank of Shanghai and Taiwan's The Shanghai Commercial & Savings Bank during the 12th Tripartite Partnership Conference held in November 2011 in Taipei with the aim of deepening and widening the strategic alliance and promoting closer exchange among the staff to build the best financial service platform for our VIP customers in the region.

本銀行與中國內地的上海銀行及台灣的上海商業儲蓄銀行於二零一一年十一月，在台北舉辦的第十二屆滬港台“上海銀行”業務研討會中簽署業務合作備忘錄，宣示深化及廣化策略聯盟業務合作，並促進人員緊密交流，共同打造跨越兩岸三地的最佳金融服務平台。


第十二屆滬港台"上海銀行"業務研討會
合作創新・通路造富・全球發展
滬港台"上海銀行"業務合作
備忘錄簽約儀式


綠色通道
三地上銀 一心為您
上海商業銀行
SHANGHAI COMMERCIAL BANK
為你開啟 兩岸三地財富之門


上海商業銀行
SHANGHAI COMMERCIAL BANK
三地市场脉动，随时为您掌控—
便捷金融服务，就在上海银行
755-8222 8606


上海商業銀行
SHANGHAI COMMERCIAL BANK

Commitment to SME Sector Growth
積極支援中小企發展

The Bank was awarded the 2011 Best SME's Partner Award organized by The Hong Kong General Chamber of Small and Medium Business and continues to be fully committed to providing a wide range of tailor-made banking solutions to SMEs.

本銀行榮獲香港中小型企業總商會頒發「二零一一年中小企業最佳拍檔獎」，並繼續致力為中小企業提供多元化的度身訂造理財方案。







Launch of JETCO Chip Card
銀通晶片提款卡

The Bank partnered with Joint Electronic Teller Services Limited (JETCO) and other member banks in upgrading their ATM machines and cards systems to utilize chip card technology for better customer protection and experience.

本銀行與銀聯通寶有限公司(「銀通」)及其他會員銀行攜手引入晶片技術並提升自動櫃員機和提款卡系統，以加強對客戶的保障。

Product Promotions
產品推廣活動

The Bank continued to drive business growth through a series of cross-selling and customer expansion campaigns.

本銀行繼續推出多項產品交叉銷售及擴大客戶群推廣活動，以推動業務持續增長。







Paofoong Insurance 寶豐保險 | 香港人壽 hong kong life | BCT 銀聯信託 | 銀和再保險 bc reinsurance | Jetco 銀通



Employee Development
員工發展

The Bank recognizes the importance of continuous career development. Every year, the Bank invites selected members of staff to participate in the Pacific Rim Bankers Program (PRBP) organized by the University of Washington's Foster School of Business in the United States. The PRBP is a unique executive education program specializing in equipping banking professionals from nations bordering the Pacific Ocean with the required knowledge to be successful in the financial industry.

本銀行一向重視員工的持續職業發展，每年會委派員工參加由美國華盛頓大學 Foster School of Business 舉辦之 Pacific Rim Bankers Program (PRBP) 。PRBP 是獨特的行政人員課程，旨在培育泛太平洋區域金融界人才。

HKIB Outstanding Financial Management Planner Awards 2011
香港銀行學會「2011傑出財富管理師大獎」

Our staff was awarded the Gold Award at the HKIB Outstanding Financial Management Planner Awards 2011 for outstanding financial planning and presentation skills.

本銀行員工憑着周詳的財務計劃書及具說服力的陳述技巧，在香港銀行學會「2011 傑出財富管理師大獎」中榮獲金獎。





Hong Kong Life Top Producers Convention 2011
香港人壽傑出業務代表會議2011

Over 100 frontline staff members attended a 4-day Hong Kong Life Top Producers Convention in Singapore in March 2011 and received accolades in various categories.

本銀行超過 100 名前線員工獲邀出席於 2011 年 3 月在新加坡舉辦，為期四天的香港人壽傑出業務代表會議並屢獲殊榮。

The Hong Kong banking industry was affected by volatility throughout 2011 amidst the ongoing uncertainties over U.S. economic growth, deterioration of market sentiments in Europe and the austerity measures in Mainland China. The relaxation of cross-border activities and Hong Kong's designation as a settlement centre for offshore Renminbi business triggered rapid loan growth. Fierce competition amongst peers for customer deposits had driven up interest costs considerably and narrowed interest margins. Fee income from equity trading was impacted by the lacklustre performance of the local stock market.

Despite the challenging operating environment, Shanghai Commercial Bank (the 'Bank'), in 2011, achieved a consolidated net profit after tax of HK$1,802 million, an increase of 5.73% or HK$97.7 million. Total deposits increased by 8% while total loans and advances saw a corresponding increase of 8.7%. Net interest income increased by 4.7% while the average net interest margin decreased by only 3 basis points, from 1.75% to 1.72%, as our overseas branches were able to maintain the interest spread at a satisfactory level. The Bank maintained its prudent approach and kept capital adequacy, liquidity and loan-to-deposit ratios at the comfortable levels of 18%, 47% and 53% respectively at the end of 2011. The return on average total assets and average equity stood at 1.46% and 10.24% respectively while the cost-to-income ratio at 29.1% compared favourably over 2010.

Net fee and commission income fell by 3.8% in 2011, with securities brokerage income being impacted the most. In order to increase revenue, initiatives to provide comprehensive and smarter personalized banking services via the mobile and internet systems would be the main focus in 2012. We recognize the importance of developing the Renminbi business in Hong Kong, and have provided integrated financial services to our customers in stock trading, wealth management, insurance, trade financing and cross-border settlement. We shall also step up our commitment to the mass affluent and high net worth customers in the Greater China region by enhancing our premium integrated banking services via the Smart Banking and Green Channel platforms. Also, we seek greater synergies to further strengthen the alliance with Bank of Shanghai in Mainland China and The Shanghai Commercial and Savings Bank in Taiwan by leveraging on the prominent tri-bank network in Hong Kong, Taiwan, Mainland China, the United States, the United Kingdom and Vietnam.

In 2011, we celebrated the Bank's 60th year in serving the community. Before the commencement of the redevelopment of the Bank's Headquarters at 10-12 Queen's Road Central, we hosted various receptions at the existing premises for our esteemed customers and guests, to introduce the design of our new building and to express our sincere gratitude for their patronage and continued support. Over 150 dedicated staff, with over 30 years' service, were given recognition for their devotion and loyalty. The new 28-storey state-of-the-art office building with eco-friendly features will become a landmark in Central and it will promote the Bank's image. During the transitional period, the Bank's various departments have been relocated to Tsimshatsui East, Kwun Tong and North Point.

The banking and financial industry will face competition in the year ahead. We remain vigilant but continue to strive for service enhancement and growth through new customers and cross-selling opportunities.

On behalf of the Board, we would like to welcome Mr. Richard Yorke, Executive Vice President & Group Head of International Group at Wells Fargo Bank, who joined our Board in June 2011. We would also like to extend our deep appreciation to the retiring Director, Mr. David Joseph Zuercher of Wells Fargo Bank, for his valuable contribution and wise counsel during his tenure as Director from 1999 to 2011.

We want to express our sincere appreciation to our Board of Directors for their guidance, and strong leadership, to our customers for their trust and continued support and to all the staff for their hard work and dedication. There would be challenges ahead but we look forward to 2012 with guarded optimism.

Lincoln Chu Kuen Yung
Chairman

David Sek-Chi Kwok
Chief Executive & Managing Director

Hong Kong, 27th February 2012

The Directors have pleasure in submitting their report together with the audited consolidated financial statements for the year ended 31st December 2011.

Principal activities

Shanghai Commercial Bank Limited (the 'Bank') and its subsidiary companies (together, the 'Group') are engaged in the provision of banking and related financial services.

Profit and appropriations

The Group's profit for the year after taxation and other comprehensive income less non-controlling interests are set out in the consolidated statement of changes in equity on page 30 of the consolidated financial statements.

The Directors recommend the payment of a final dividend of HK$43 per ordinary share totalling HK$860,000,000.

Other reserves

Movements in the other reserves of the Group and the Bank during the year are set out in Note 33 to the consolidated financial statements.

Donations

During the year donations made by the Bank and its subsidiary companies for charitable and other purposes amounted to HK$2,237,000.

Property and equipment

Details of the movements in property and equipment of the Group and the Bank are shown in Note 25 to the consolidated financial statements.

Directors

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

Hung-ching Yung	
Lincoln Chu Kuen Yung	
Shen Ruolei (Ye Jun, Alternate)	
David Joseph Zuercher	(resigned on 15th June 2011)
(Clifford Sterling Lawrence, Alternate)	(ceased on 15th June 2011)
Dr. Richard Lee	
Johnson Mou Daid Cha (Dr. Lam Chat Yu, Alternate)	
David Sek-chi Kwok	
Stephen Ching Yen Lee	
Edward Kawah Chu	
David Allen Hoyt (Ignatius Wooi-kean Choong, Alternate)	
Chen Yih Pin (Yi-Jen Chiou, Alternate)	
Gordon Che Keung Kwong	
Ning Li Ming (Li Jian Guo, Alternate)	
Richard Jason Lloyd Yorke	(appointed on 15th June 2011)
(Clifford Sterling Lawrence, Alternate)	(appointed on 15th June 2011)

In accordance with Article 104(A) of the Bank's Articles of Association, Dr. Richard Lee, Mr. David Allen Hoyt, Mr. Chen Yih Pin and Mr. Gordon Che Keung Kwong shall retire by rotation at the forthcoming Annual General Meeting and, being eligible, offer themselves for re-election.

In accordance with Article 95 of the Bank's Articles of Association, Mr. Richard Jason Lloyd Yorke shall retire at the forthcoming Annual General Meeting and, being eligible, offer himself for re-election.

Directors' interests

No contracts of significance in relation to the Group's business to which the Bank, its subsidiary companies, its fellow subsidiaries or its holding companies was a party and in which a Director of the Bank had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

At no time during the year was the Bank, its subsidiary companies, its fellow subsidiaries or its holding companies a party to any arrangements to enable the Directors of the Bank to acquire benefits by means of the acquisition of shares in, or debentures of, the Bank or any other body corporate.

Management contracts

No substantial contracts concerning the management and administration of the whole or any substantial part of the business of the Bank were entered into or existed during the year.

Financial disclosures

The Bank has followed the disclosure requirements set out in the 'Guideline on the Application of the Banking (Disclosure) Rules' under the Supervisory Policy Manual issued by the Hong Kong Monetary Authority ('HKMA') in May 2007. The Bank has complied with the capital requirements related to capital base and capital adequacy ratio stipulated by the HKMA.

Compliance with the Code of Best Practice

According to Article 123 of the Bank's Articles of Association, the Bank adopts the guidelines set out in the Code of Best Practice contained in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ('Code of Best Practice'). The Code of Best Practice was replaced by the Code on Corporate Governance Practices which became effective for accounting periods commencing on or after 1st January 2005. After taking into consideration the individual circumstances of the Bank, which is a private company, the Board of Directors of the Bank has decided to adopt only those provisions in the Code on Corporate Governance Practices that are relevant and of value to the Bank. The following three code provisions are considered not applicable to the Bank: A.5.4, C.1.2 and C.2.1.

Auditors

The consolidated financial statements have been audited by PricewaterhouseCoopers who retire and, being eligible, offer themselves for re-appointment.

On behalf of the Board
Lincoln Chu Kuen Yung
Chairman

Hong Kong, 27th February 2012

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF SHANGHAI COMMERCIAL BANK LIMITED

(Incorporated in Hong Kong with limited liability)

We have audited the consolidated financial statements of Shanghai Commercial Bank Limited (the 'Bank') and its subsidiaries (together, the 'Group') set out on pages 24 to 124, which comprise the consolidated and Bank statements of financial position as at 31st December 2011, and the consolidated and Bank income statements, the consolidated and Bank statements of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Directors' Responsibility for the Consolidated Financial Statements

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

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with section 141 of the Hong Kong Companies Ordinance and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Bank and of the Group as at 31st December 2011, and of the Bank's and the Group's profits and cash flows of the Group for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 27th February 2012

CONSOLIDATED INCOME STATEMENT

(All amounts in HK dollar thousands unless otherwise stated)

	Note	Year ended 31st December 2011	2010
Interest income	6	2,702,557	2,357,059
Interest expense	6	(720,598)	(463,622)
Net interest income		1,981,959	1,893,437
Fee and commission income	7	692,770	718,579
Fee and commission expense	7	(38,150)	(38,307)
Net fee and commission income		654,620	680,272
Dividend income	8	28,599	22,211
Net trading income	9	112,247	180,887
Net losses from financial instruments designated at fair value through profit or loss		–	(3,100)
Net losses from disposal of equipment		(843)	(1,509)
Net gains from disposal of available-for-sale investments		155,824	263,175
Other operating income	10(a)	84,763	89,022
Net earned insurance premium	10(b)	30,820	23,915
Net insurance claims incurred and movement in policyholders' liabilities		(9,374)	(4,231)
Operating expenses	11	(884,057)	(1,040,253)
Reversal/ (charge) for impairment losses on loans and advances to customers	13	19,905	(84,308)
Operating profit		2,174,463	2,019,518
Share of net profits of jointly controlled entities		16,488	18,371
Profit before income tax		2,190,951	2,037,889
Income tax expense	14	(388,837)	(333,470)
Profit for the year		1,802,114	1,704,419
Attributable to:			
Equity holders of the Bank		1,798,417	1,700,558
Non-controlling interests		3,697	3,861
		1,802,114	1,704,419
Dividends			
Final dividend proposed after the end of the reporting period	16	860,000	860,000

The notes on pages 34 to 124 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

(All amounts in HK dollar thousands unless otherwise stated)

	Note	Year ended 31st December 2011	2010
Profit for the year		**1,802,114**	1,704,419
Exchange differences on translation of foreign operations	15	**24,393**	18,446
Net gains/ (losses) on available-for-sale investments			
Fair value changes taken to equity on available-for-sale investments	15	**88,898**	456,763
Exchange differences on translation of available-for-sale investments	15	**(302)**	1,137
Fair value changes transferred to income statement on disposal and early redemption of the available-for-sale investments	15	**(155,824)**	(263,175)
Deferred income tax	15	**10,992**	(33,113)
Share of changes in equity of jointly controlled entities	15	**(103)**	161
Total comprehensive income for the year		**1,770,168**	1,884,638
Attributable to:			
Equity holders of the Bank		**1,768,479**	1,880,423
Non-controlling interests		**1,689**	4,215
		1,770,168	1,884,638

The notes on pages 34 to 124 are an integral part of these consolidated financial statements.

INCOME STATEMENT

(All amounts in HK dollar thousands unless otherwise stated)

	Note	Year ended 31st December 2011	2010
Interest income	6	2,656,480	2,293,953
Interest expense	6	(720,701)	(463,678)
Net interest income		1,935,779	1,830,275
Fee and commission income	7	671,157	691,879
Fee and commission expense	7	(31,678)	(31,019)
Net fee and commission income		639,479	660,860
Dividend income	8	75,577	91,696
Net trading income	9	112,087	180,839
Net losses from financial instruments designated at fair value through profit or loss		–	(3,100)
Net losses from disposal of equipment		(840)	(1,499)
Net gains from disposal of available-for-sale investments		155,824	262,979
Other operating income	10	99,330	106,458
Operating expenses	11	(874,007)	(1,034,837)
Reversal/ (charge) for impairment losses on loans and advances to customers	13	19,905	(84,308)
Profit before income tax		2,163,134	2,009,363
Income tax expense	14	(386,685)	(332,283)
Profit for the year		1,776,449	1,677,080
Dividends			
Final dividend proposed after the end of the reporting period	16	860,000	860,000

The notes on pages 34 to 124 are an integral part of these consolidated financial statements.

STATEMENT OF COMPREHENSIVE INCOME

(All amounts in HK dollar thousands unless otherwise stated)

	Note	Year ended 31st December 2011	2010
Profit for the year		**1,776,449**	1,677,080
Exchange differences on translation of foreign operations	15	**24,388**	18,210
Net gains/ (losses) on available-for-sale investments			
Fair value changes taken to equity on available-for-sale investments	15	**95,515**	461,469
Exchange differences on translation of available-for-sale investments	15	**(302)**	1,136
Fair value changes transferred to income statement on disposal of the available-for-sale investments	15	**(155,824)**	(262,979)
Deferred income tax	15	**10,001**	(32,938)
Total comprehensive income for the year		**1,750,227**	1,861,978

The notes on pages 34 to 124 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

(All amounts in HK dollar thousands unless otherwise stated)

	Note	As at 31st December 2011	2010 (restated)
ASSETS			
Cash and balances with banks	17	27,739,092	25,916,048
Placements with and loans and advances to banks	18	14,865,476	13,274,323
Loans and advances to customers	19(a)	55,195,656	50,706,800
Financial assets held for trading	20	444,237	610,090
Derivative financial instruments	21	70,294	61,484
Investment securities:			
– Available-for-sale	22	22,008,660	21,468,699
– Held-to-maturity	23	2,764,783	2,766,411
Investments in jointly controlled entities	24(a)	189,308	174,473
Property and equipment	25	2,040,164	608,584
Investment property	26	9,193	1,382,734
Deferred income tax assets	31	44,755	56,656
Other assets	27	1,606,222	1,615,370
TOTAL ASSETS		126,977,840	118,641,672
LIABILITIES			
Deposits and balances from banks		4,331,800	4,138,145
Deposits from customers	28	103,097,196	95,463,191
Derivative financial instruments	21	45,409	53,508
Other liabilities	29	1,208,269	1,471,382
Provisions	30	94,691	99,654
Current income tax liabilities		14,872	130,982
Deferred income tax liabilities	31	104,551	113,046
TOTAL LIABILITIES		108,896,788	101,469,908
EQUITY			
CAPITAL AND RESERVES ATTRIBUTABLE TO THE EQUITY HOLDERS			
Share capital	32	2,000,000	2,000,000
Retained earnings			
– Proposed final dividend		860,000	860,000
– Others		6,669,090	5,830,421
Other reserves	33	8,493,399	8,423,589
		18,022,489	17,114,010
Non-controlling interests in equity		58,563	57,754
TOTAL EQUITY		18,081,052	17,171,764
TOTAL EQUITY AND LIABILITIES		126,977,840	118,641,672

Approved and authorised for issue by the Board of Directors on 27th February 2012.

Lincoln Chu Kuen Yung
Chairman

Hung-ching Yung
Director

Gordon Che Keung Kwong
Director

David Sek-chi Kwok
Managing Director & Chief Executive

The notes on pages 34 to 124 are an integral part of these consolidated financial statements.

STATEMENT OF FINANCIAL POSITION

(All amounts in HK dollar thousands unless otherwise stated)

	Note	As at 31st December 2011	2010 (restated)
ASSETS			
Cash and balances with banks	17	27,739,080	25,916,043
Placements with and loans and advances to banks	18	14,865,476	13,274,323
Loans and advances to customers	19(a)	55,195,656	50,706,800
Financial assets held for trading	20	444,237	610,090
Derivative financial instruments	21	70,294	61,484
Investment securities:			
– Available-for-sale	22	21,888,699	21,250,970
– Held-to-maturity	23	662,366	757,471
Investments in jointly controlled entities	24(a)	116,000	116,000
Investments in and loans to subsidiaries	24(b)	2,086,442	2,108,934
Property and equipment	25	1,985,901	553,543
Investment properties	26	42,620	1,416,589
Deferred income tax assets	31	44,323	56,656
Other assets	27	1,420,350	1,250,005
TOTAL ASSETS		126,561,444	118,078,908
LIABILITIES			
Deposits and balances from banks		4,331,800	4,138,145
Deposits from customers	28	103,097,196	95,463,191
Derivative financial instruments	21	45,409	53,508
Other liabilities	29	990,358	1,088,753
Provisions	30	94,320	99,220
Current income tax liabilities		14,599	130,654
Deferred income tax liabilities	31	104,516	112,418
TOTAL LIABILITIES		108,678,198	101,085,889
EQUITY			
CAPITAL AND RESERVES ATTRIBUTABLE TO THE EQUITY HOLDERS			
Share capital	32	2,000,000	2,000,000
Retained earnings			
– Proposed final dividend		860,000	860,000
– Others		6,526,826	5,710,148
Other reserves	33	8,496,420	8,422,871
		17,883,246	16,993,019
TOTAL EQUITY AND LIABILITIES		126,561,444	118,078,908

Approved and authorised for issue by the Board of Directors on 27th February 2012.

Lincoln Chu Kuen Yung
Chairman

Hung-ching Yung
Director

Gordon Che Keung Kwong
Director

David Sek-chi Kwok
Managing Director & Chief Executive

The notes on pages 34 to 124 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

(All amounts in HK dollar thousands unless otherwise stated)

	Note	Attributable to the equity holders			Non-controlling interests	Total equity
		Share capital	Other reserves	Retained earnings		
Balance at 1st January 2010		2,000,000	8,247,991	5,785,596	55,419	16,089,006
Profit for the year		–	–	1,700,558	3,861	1,704,419
Other comprehensive income						
Fair value gains, net of tax:						
– available-for-sale investments	33	–	423,218	–	432	423,650
Currency translation differences	33	–	15,315	4,267	1	19,583
Net income recognised directly in equity		–	438,533	4,267	433	443,233
Share of changes in equity of jointly controlled entities	33	–	161	–	–	161
Realised on disposal of available-for-sale investments	33	–	(263,096)	–	(79)	(263,175)
Total other comprehensive income		–	175,598	4,267	354	180,219
Dividend relating to 2009		–	–	(800,000)	(1,880)	(801,880)
Balance at 31st December 2010		2,000,000	8,423,589	6,690,421	57,754	17,171,764

	Note	Attributable to the equity holders			Non-controlling interests	Total equity
		Share capital	Other reserves	Retained earnings		
Balance at 1st January 2011		**2,000,000**	**8,423,589**	**6,690,421**	**57,754**	**17,171,764**
Profit for the year		–	–	**1,798,417**	**3,697**	**1,802,114**
Other comprehensive income						
Fair value gains, net of tax:						
– available-for-sale investments	33	–	**101,898**	–	**(2,008)**	**99,890**
Currency translation differences	33	–	**23,839**	**252**	–	**24,091**
Net income recognised directly in equity		–	**125,737**	**252**	**(2,008)**	**123,981**
Share of changes in equity of jointly controlled entities	33	–	**(103)**	–	–	**(103)**
Realised on disposal of available-for-sale investments	33	–	**(155,824)**	–	–	**(155,824)**
Total other comprehensive income		–	**(30,190)**	**252**	**(2,008)**	**(31,946)**
Transfer from retained earnings	33	–	**100,000**	**(100,000)**	–	–
Dividend relating to 2010		–	–	**(860,000)**	**(880)**	**(860,880)**
Balance at 31st December 2011		**2,000,000**	**8,493,399**	**7,529,090**	**58,563**	**18,081,052**

	Year ended 31st December	
	2011	2010
Proposed dividend in retained earnings	**860,000**	860,000

The notes on pages 34 to 124 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(All amounts in HK dollar thousands unless otherwise stated)

	Year ended 31st December	
	2011	2010 (restated)
Cash flows from operating activities		
Profit before income tax	2,190,951	2,037,889
Share of net profits of jointly controlled entities	(16,488)	(18,371)
(Reversal)/ charge for impairment losses on loans and advances to customers	(19,905)	84,308
Depreciation expenses for property and equipment	59,210	72,973
Net losses from disposal of equipment	843	1,509
Net gains from disposal of available-for-sale investments	(155,824)	(263,175)
Amortisation of held-to-maturity and available-for-sale investments	55,572	65,371
Interest income on held-to-maturity and available-for-sale investments	(689,946)	(683,299)
Dividend income	(28,599)	(22,211)
Hong Kong profits tax (paid)/ refunded	(106,866)	13,325
Overseas tax paid	(91,092)	(90,174)
Cash flows from operating activities before changes in operating assets and liabilities	1,197,856	1,198,145
Changes in operating assets and liabilities:		
– Net (increase)/ decrease in cash and balances with banks with original maturity beyond three months	(1,497,797)	3,246,953
– Net (increase)/ decrease in placements with and loans and advances to banks with original maturity beyond three months	(294,153)	406,196
– Net decrease/ (increase) in financial assets held for trading	285,955	(221,064)
– Net decrease in derivative financial instruments	(16,909)	(26,792)
– Net decrease in financial assets designated at fair value	–	398,430
– Net increase in loans and advances to customers	(4,470,606)	(6,807,041)
– Net increase in other assets	(281,814)	(185,990)
– Net increase in deposits and balances from banks	193,655	571,671
– Net increase in deposits from customers	7,634,005	3,974,283
– Net decrease in other liabilities and provisions	(268,076)	(76,391)
Net cash flows from operating activities	2,482,116	2,478,400

	Note	Year ended 31st December 2011	2010 (restated)
Cash flows from investing activities			
Interest received on held-to-maturity and available-for-sale investments		688,420	661,057
Dividends received on available-for-sale investments		27,888	22,211
Dividends received from jointly controlled entities		1,550	2,660
Repayment of advances from a jointly controlled entity		–	1,300
Purchases of property and equipment		(108,867)	(18,746)
Purchases of an investment property		(9,315)	–
Proceeds from sale of equipment		206	17
Purchases of available-for-sale investments		(9,997,142)	(14,196,356)
Purchases of held-to-maturity investments		(972,194)	(378,219)
Proceeds from sale and redemption of available-for-sale investments		9,368,636	13,702,556
Proceeds from redemption of held-to-maturity investments		947,044	451,797
Net cash flows from investing activities		(53,774)	248,277
Cash flows from financing activities			
Dividend paid to the equity holders		(860,000)	(800,000)
Dividend paid to non-controlling interests		(880)	(1,880)
Net cash flows from financing activities		(860,880)	(801,880)
Net increase in cash and cash equivalents		1,567,462	1,924,797
Cash and cash equivalents at beginning of the year		25,026,574	23,387,952
Effect of exchange rate changes on cash and cash equivalents		54,785	(286,175)
Cash and cash equivalents at end of the year	34	26,648,821	25,026,574

The notes on pages 34 to 124 are an integral part of these consolidated financial statements.

1 GENERAL INFORMATION

Shanghai Commercial Bank Limited (the 'Bank') and its subsidiary companies (together, the 'Group') are engaged in the provision of banking and related financial services in Hong Kong, United States, United Kingdom and the People's Republic of China. The Group employs over 1,650 people as at 31st December 2011.

The Bank is a financial institution incorporated in Hong Kong. The address of its registered office is 35/F., Gloucester Tower, The Landmark, 15 Queen's Road Central, Hong Kong.

These consolidated financial statements are presented in thousands of units of Hong Kong Dollars (HK$'000), unless otherwise stated. These consolidated financial statements have been approved for issue by the Board of Directors on 27th February 2012.

2 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.

2.1 Basis of preparation

The consolidated financial statements of the Group and the financial statements of the Bank have been prepared in accordance with Hong Kong Financial Reporting Standards ('HKFRSs') issued by the Hong Kong Institute of Certified Public Accountants ('HKICPA'). The consolidated financial statements of the Group and the financial statements of the Bank have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale investments, financial assets designated at fair value, financial assets held for trading and derivative financial instruments at fair value.

The preparation of financial statements in conformity with HKFRSs requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in Note 4.

(a) Standard, amendments and interpretations effective beginning 1st January 2011

(i) The following standards, amendments and interpretations, which became effective in 2011 are relevant to the Group:

HKAS 24 (revised), 'Related party disclosures' is effective for annual period beginning on or after January 2011. It introduces an exemption from all of the disclosure requirements of HKAS 24 for transactions among government related entities and the government. Those disclosures are replaced with a requirement to disclose:

- The name of the government and the nature of their relationship;
- The nature and amount of any individually significant transactions; and
- The extent of any collectively-significant transactions qualitatively or quantitatively.

It also clarifies and simplifies the definition of a related party. The revised standard has no significant impact to the Group's consolidated financial statements.

Third improvements to Hong Kong Financial Reporting Standards (2010) were issued in May 2010 by the HKICPA. All improvements are effective in the financial year of 2011. These improvements include amendments to HKFRS 7, 'Financial Instruments: Disclosures', which mainly require additional qualitative and quantitative disclosures related to the credit risks arising from financial instruments, including the financial effect of collateral held as security. There were no material changes to the accounting policies as a result of these amendments.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.1 Basis of preparation (Continued)

(a) Standard, amendments and interpretations effective beginning 1st January 2011 (Continued)

(ii) The following standards, amendments and interpretations, which became effective in 2011 are not currently relevant to the Group (although they may affect the accounting for future transactions and events):

Amendment to HKAS 32, 'Classification of rights issues', is effective for annual periods beginning on or after 1st February 2010. Rights issues are now required to be classified as equity if they are issued for a fixed amount of cash regardless of the currency in which the exercise price is denominated, provided they are offered on a pro rata basis to all owners of the same class of non-derivative equity. Entities will no longer classify rights issues, for which non-derivative the exercise price is denominated in a foreign currency, as derivative liabilities with fair value changes being recorded in profit or loss. Rather, entities will be able to classify these rights in equity with no re-measurement. The scope of the amendment is narrow and does not extend to foreign-currency-denominated convertible bonds. For these instruments, the embedded option to acquire the issuer's equity will continue to be accounted for as a derivative liability with fair value changes recorded in profit or loss. The amendment is not currently applicable to the Group, as it has not made any rights issue.

Amendment to HK(IFRIC) - Int 14, 'Prepayments of a minimum funding requirement' is effective for annual periods beginning on or after 1st January 2011. Some entities that are subject to a minimum funding requirement have elected to prepay their pension contributions. The prepaid contributions are recovered through lower minimum funding requirements in future years. The previous version of HK(IFRIC) - Int 14 did not permit the recognition of an asset for any surplus arising from the voluntary prepayment of minimum funding contributions in respect of future service. This was an unintended consequence of the interpretation, which has been amended to require that an asset is recognised in these circumstances. The amendment is not currently relevant to the Group's consolidated financial statements, as it does not have a minimum funding requirement.

HK(IFRIC) - Int 19, 'Extinguishing financial liabilities with equity instruments', is effective for annual periods beginning on or after 1st July 2010. The interpretation clarifies the accounting by the debtor when the debtor renegotiates the terms of its debt with the result that the liability is extinguished through issuing its own equity instruments to the creditor (i.e. a 'debtor for equity swap'). A gain or loss recognised in profit or loss is the difference between the fair value of the equity instruments issued and the carrying amount of the financial liability. If the fair value of the equity instruments cannot be reliably measured when the fair value of the existing financial liability is used to measure the gain or loss. The amount of the gain or loss should be separately disclosed on the face of the statement of comprehensive income or in the notes. This interpretation applies to all debtors that enter into debt for equity swap transactions in full or partial settlement of a financial liability. This is not currently applicable to the Group, as it has no extinguishment of financial liabilities replaced with equity instruments currently.

(b) The following new standards, new interpretation and amendments to standards and interpretations have been issued but are not effective for the financial year beginning 1st January 2011 and have not been early adopted

The Group's and the Bank's assessment of the impact of these new standards and interpretations is set out below.

HKFRS 7 (Amendment), 'Financial Instruments: Disclosures - Offsetting Financial Assets and Financial Liabilities', is effective for annual periods beginning on or after 1st January 2015. The new disclosures, which are similar to the new US GAAP disclosure requirements, would provide users with information that is useful in (i) evaluating the effect or potential effect of netting arrangements on an entity's financial position and (ii) analysing and comparing financial statements prepared in accordance with HKFRSs and US GAAP. The Group is considering the financial impact of the amendment and the timing of its application.

HKFRS 7 (Amendment), 'Financial Instruments: Disclosures - Transition to HKFRS 9', is effective for annual periods beginning on or after 1st January 2015. The amendments provide relief from the requirement to restate comparative financial statements which was originally available only to entities that chose to apply HKFRS 9 prior to 2012. Instead, additional transition disclosures will be required to help investors to better understand the effect of initial application of the standard. The Group is considering the financial impact of the amendment and the timing of its application.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.1 Basis of preparation (Continued)

(b) The following new standards, new interpretation and amendments to standards and interpretations have been issued but are not effective for the financial year beginning 1st January 2011 and have not been early adopted (Continued)

HKFRS 9, 'Financial instruments' addresses the classification, measurement and recognition of financial assets and financial liabilities. HKFRS 9 was issued in November 2009 and October 2010. It replaces the parts of HKAS 39 that relate to the classification and measurement of financial instruments. HKFRS 9 requires financial assets to be classified into two measurement categories: those measured as at fair value and those measured at amortised cost. The determination is made at initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument. For financial liabilities, the standard retains most of the HKAS 39 requirements. The main change is that, in cases where the fair value option is taken for financial liabilities, the part of a fair value change due to an entity's own credit risk is recorded in other comprehensive income rather than the income statement, unless this creates an accounting mismatch.

Amendments to HKFRS 9 Financial Instruments was issued in December 2011 and the mandatory effective date of HKFRS 9 is deferred from 1st January 2013 to 1st January 2015 with earlier adoption still permitted. The deferral will make it possible to have the same mandatory effective date for the entire standard. New transitional disclosures are required instead of comparative restatement. The Group is considering the financial impact of the standard and the timing of its application.

HKFRS 10 'Consolidated financial statements' builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess. The group is yet to assess HKFRS 10's full impact and intends to adopt HKFRS 10 no later than the accounting period beginning on or after 1st January 2013.

HKFRS 11, 'Joint Arrangements', classifies joint arrangements as either joint operations (combining the existing concepts of jointly controlled assets and jointly controlled operations) or joint ventures (equivalent to the existing concept of a jointly controlled entity). Joint operation is a joint arrangement whereby the parties that have joint control have rights to the assets and obligations for the liabilities. Joint venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement. HKFRS 11 requires the use of equity method of accounting for interests in joint ventures thereby eliminating the proportionate consolidation method. The determination of as to whether a joint arrangement is a joint operation or a joint venture is based on the parties' rights and obligations under the arrangement, with the existence of a separate legal vehicle no longer being the key factor. Transitional provisions vary depending on how an interest is classified under HKAS 31. The effective date of HKFRS 11 is 1st January 2013, with early application permitted in certain circumstances.

As the Group accounted for its investment in jointly controlled entities using the equity method, the new standard does not have impact to the Group's financial statements.

HKFRS 12 'Disclosures of interests in other entities' includes the disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles. The Group is yet to assess HKFRS 12's full impact and intends to adopt HKFRS 12 no later than the accounting period beginning on or after 1st January 2013.

HKFRS 13 'Fair value measurement' aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across HKFRSs. The requirements do not extend the use of fair value accounting but provide guidance on how it should be applied where its use is already required or permitted by other standards within HKFRSs. The group is yet to assess HKFRS 13's full impact and intends to adopt HKFRS 13 no later than the accounting period beginning on or after 1st January 2013.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.1 Basis of preparation (Continued)

(b) The following new standards, new interpretation and amendments to standards and interpretations have been issued but are not effective for the financial year beginning 1st January 2011 and have not been early adopted (Continued)

HKAS 1 (revised), 'Presentation of Items of Other Comprehensive Income', is effective for annual periods beginning on or after 1st July 2012, with full retrospective application. Earlier application permitted. The amendments retain the option to present profit or loss and other comprehensive income in a single continuous statement or in two separate but consecutive statements. Items of other comprehensive income are required to be grouped into those that will and will not subsequently be reclassified into profit or loss. Tax on items of other comprehensive income is required to be allocated on the same basis. The measurement and recognition of items of profit or loss and other comprehensive income are not affected by the amendments.

HKAS 19, 'Employee benefits', is effective for annual periods beginning on or after 1st January 2013, with earlier application permitted. Retrospective application is required with certain exceptions. The amendments require the recognition of changes in the defined benefit obligation and in plan assets when those changes occur, eliminating the corridor approach and accelerating the recognition of past service costs. Changes in the defined benefit obligation and plan assets are disaggregated into three components: service costs, net interest on the net defined benefit liabilities (assets) and remeasurements of the net defined benefit liabilities (assets). Net interest is calculated using a high quality corporate bond yield. This may be lower than the rate currently used to calculate the expected return on plan assets, resulting in a decrease in net income. The amendments will not have significant impact on the Group's consolidated financial statements.

HKAS 27 (revised 2011), 'Separate financial statements', has been amended for the issuance of HKFRS 10 but retains the current guidance for separate financial statements. HKAS 27 (revised 2011) is effective for annual periods beginning on or after 1st January 2013, early adoption is permitted. The revised standard will not have significant impact to the Group's financial statements.

HKAS 28 (revised 2011), 'Investments in associates and joint ventures' has been amended for conforming changes based on the issuance of HKFRS 10 and HKFRS 11. HKAS 28 (revised 2011) is effective for annual periods beginning on or after 1st January 2013, early adoption is permitted. The revised standard will not have significant impact to the Group's financial statements.

HKAS 32 (Amendment), 'Financial Instruments: Presentation - Offsetting Financial Assets and Financial Liabilities', is effective for annual periods beginning on or after 1st January 2014. 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'; 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 Group is considering the financial impact of the amendment.

(c) The following new standards, new interpretation and amendments to standards and interpretations have been issued but are not effective for the financial year beginning 1st January 2011 and not relevant to the Group's operations

HKAS 12 (Amendment) 'Deferred tax: Recovery of underlying assets' introduces an exception to the principle for the measurement of deferred tax assets or liabilities arising on an investment property measured at fair value. HKAS 12 requires an entity to measure the deferred tax relating to an asset depending on whether the entity expects to recover the carrying amount of the asset through use or sale. The amendment introduces a rebuttable presumption that an investment property measured at fair value is recovered entirely by sale. The amendment is applicable retrospectively to annual periods beginning on or after 1st January 2012 with early adoption permitted. As the Group adopted cost model for the investment properties, the amendments have no impact to the Group's consolidated financial statements.

HKFRS 1 (Revised), 'First-time adoption of Hong Kong Financial Reporting Standards' was issued in December 2010. The amendments consist of two narrow amendments to HKFRS 1. The first amendment allows an entity that has been subject to severe hyperinflation to measure assets and liabilities at fair value and to use that fair value as the deemed cost of those assets and liabilities in its opening HKFRS statement of financial position.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.1 Basis of preparation (Continued)

(c) The following new standards, new interpretation and amendments to standards and interpretations have been issued but are not effective for the financial year beginning 1st January 2011 and not relevant to the Group's operations (Continued)

The second amendment removes the fixed transition dates in HKFRS 1 requirements regarding the exception to retrospective application for derecognition of financial instruments and the exemption from the initial fair value measurement of financial instruments. The fixed transition dates are replaced by 'the date of transition to HKFRSs'. As a result, a first-time HKFRS adopter is not required to restate derecognition transactions and/or initial fair value measurements that occurred before its date of transition to HKFRSs. HKFRS 1 (Revised) is effective for annual periods beginning on or after 1st July 2011. Since these amendments are not relevant to existing adopters of HKFRS, the amendment has no impact to the Group's consolidated financial statements.

HKFRS 7 (Amendment) 'Disclosures-Transfers of financial assets' introduces new disclosure requirement on transfers of financial assets. Disclosure is required by class of asset of the nature, carrying amount and a description of the risks and rewards of financial assets that have been transferred to another party yet remain on the entity's balance sheet. The gain or loss on the transferred asset and any retained interest in those assets must be given. In addition, other disclosures must enable users to understand the amount of any associated liabilities, and the relationship between the financial assets and associated liabilities. The disclosures must be presented by type of ongoing involvement. For example, the retained exposure could be presented by type of financial instrument involvement. For example, the retained exposure could be presented by type of financial instrument (such as guarantees, call or put options), or by type of transfer (such as factoring of receivables, securitisations or securities lending). The amendment is applicable to annual periods beginning on or after 1st July 2011 with early adoption permitted. The amendment has no impact to the Group's consolidated financial statements.

(d) Early adoption of standards

The Group did not early-adopt new or amended standards in 2011.

2.2 Consolidation

The consolidated financial statements include the financial statements of the Bank and all its subsidiaries made up to 31st December 2011.

(a) Subsidiaries

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. 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.

The Group uses the acquisition method of accounting to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at fair values at the acquisition date. On an acquisition-by-acquisition basis, the Group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets.

Investments in subsidiaries are accounted for at cost less impairment. Cost is adjusted to reflect changes in consideration arising from contingent consideration amendments. Cost also includes direct attributable costs of investment.

The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired is recorded as goodwill. If this is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognised directly in the statement of comprehensive income (Note 2.18).

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.2 Consolidation (Continued)

(a) Subsidiaries (Continued)

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 asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

(b) Transactions with non-controlling interests

The Group treats transactions with non-controlling interests as transactions with equity owners of the Group. For purchases from non-controlling interests, the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

When the Group ceases to have control or significant influence, any retained interest in the entity is remeasured to its fair value, with the change in carrying amount recognised in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognised in other comprehensive income in respect of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities. This may mean that amounts previously recognised in other comprehensive income are reclassified to profit or loss.

If the ownership interest in an associate is reduced but significant influence is retained, only a proportionate share of the amounts previously recognised in other comprehensive income are reclassified to profit or loss where appropriate.

(c) Jointly controlled entities

A joint venture is a contractual arrangement whereby the Group and other parties undertake an economic activity which is subject to joint control and none of the participating parties has unilateral control over the economic activity. A jointly controlled entity is a joint venture that involves the establishment of a corporation, partnership or other entity in which each venturer has an investment.

The consolidated income statement included the Group's share of the results of jointly controlled entities, and the consolidated statement of financial position included the Group's share of the net assets of the jointly controlled entities.

In the Bank's statement of financial position, the investments in jointly controlled entities are stated at cost less provision, if necessary, for impairment losses. The results of jointly controlled entities are accounted for by the Bank on the basis of dividends received.

2.3 Foreign currency translation

(a) Functional and presentation currency

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 thousands of units of Hong Kong Dollars (HK$'000), which is the Bank's functional and the Group's presentation currency.

(b) Transactions and balances

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

Monetary items denominated in foreign currency are translated with the closing rate as at the reporting date. If several exchange rates are available, the forward rate is used at which the future cash flows represented by the transaction or balance could have been settled if those cash flows had occurred. Non-monetary items measured at historical cost denominated in a foreign currency are translated with the exchange rate as at the date of initial recognition; non-monetary items in a foreign currency that are measured at fair value are translated using the exchange rates at the date when the fair value was determined.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.3 Foreign currency translation (Continued)

(b) Transactions and balances (Continued)

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

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

In the case of changes in the fair value of monetary assets denominated in foreign currency classified as available-for-sale, a distinction is made between translation differences resulting from changes in amortised cost of the security and other changes in the carrying amount of the security.

Translation differences related to changes in the amortised cost are recognised in profit or loss, and other changes in the carrying amount, except impairment, are recognised in other comprehensive income.

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

(c) Group companies and overseas branches

The results and financial position of all the Group's entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

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

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 operation is disposed of, or partially disposed of, such exchange differences that were recorded in equity are recognised in the consolidated income statement as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

2.4 Interest income and expense

Interest income and expense for all interest-bearing financial instruments, except for those classified as held for trading or designated at fair value through profit or loss, are recognised within 'interest income' and 'interest expense' in the income statement 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, where 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 cash flows considering all contractual terms of the financial instrument, but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

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 using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.5 Fee and commission income and expense

Fees and commissions are generally recognised on an accrual basis when the service has been provided. Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognised as an adjustment to the effective interest rate on the loan. Loan syndication fees are recognised as revenue when the syndication has been completed and the Group retained no part of the loan package for itself or retained a part at the same effective interest rate as the other participants. Commissions and fees arising from negotiating, or participating in the negotiation of, a transaction for a third party - such as the arrangement of the acquisition of shares or other securities or the purchase or sale of businesses - are recognised on completion of the underlying transaction. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-apportionate basis. Asset management fees related to investment funds are recognised rateably over the period the service is provided. The same principle is applied for wealth management, financial planning and custody services that are continuously provided over an extended period of time.

2.6 Dividend income

Dividends are recognised in the income statement when the entity's right to receive payment is established.

2.7 Net income from financial instruments designated at fair value through profit or loss

Net income from financial instruments designated at fair value through profit or loss includes fair value change and interest from the financial instrument designated at fair value.

2.8 Leases

(a) Operating lease

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating lease (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.

(b) Finance lease

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

Interest in leasehold land is amortised on a straight-line basis over the unexpired period of the lease term.

2.9 Property and equipment

(a) Land and bank premises

Land and buildings comprise mainly branches and offices. Leasehold land classified as finance lease and buildings are stated at historical cost, which includes expenditure that is directly attributable to the acquisition of the items, less accumulated depreciation and impairment losses. Depreciation of land and buildings is provided annually by charging a sum sufficient to write down the cost of the land and buildings systematically, based on management's appraisal of the conditions of the land and buildings, which includes estimations of the remaining useful lives of the buildings, which are not expected to exceed 40 years.

Interest in freehold land is stated at cost and included as property and equipment on the statement of financial position.

(b) Furniture, fittings and equipment

Furniture, fittings and equipment are stated at historical cost less accumulated depreciation and impairment losses. Depreciation of furniture, fittings and equipment other than computer equipment is calculated to write off the cost of the assets over their estimated useful lives on a reducing balance basis at a rate of 25% in the year of addition and at 20% per annum thereafter. Computer equipment is depreciated on a straight line basis over four years.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.9 Property and equipment (Continued)

(b) Furniture, fittings and equipment (Continued)

Subsequent costs are included in the asset's carrying amount or 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. All other repairs and maintenance are expensed in the income statement during the financial period in which they are incurred.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2.22). The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2.22).

Gains or losses on disposals are determined by comparing proceeds and the carrying amount of the relevant assets and are recognised in the income statement.

(c) Property under development

Leasehold land for properties under development is stated at historical cost, less accumulated depreciation and impairment losses, and development expenditure is stated at the aggregate amount of costs incurred up to the date of completion. For depreciation of policy of Leasehold land for properties under development, please refer to Note 2.9(a) above.

2.10 Financial assets

2.10.1 Classification

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments and available-for-sale investments. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

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

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

A financial asset is classified as held for trading if it is acquired or incurred principally for the purpose of selling or repurchasing in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of recent actual pattern of short-term profit-making. Derivatives are also categorised as held for trading unless they are designated as hedging instruments. Financial assets held for trading consist of debt instruments, including money-market paper, traded corporate and bank loans, and equity instruments, as well as financial assets with embedded derivatives. They are recognised in the consolidated statement of financial position as 'Financial assets held for trading'.

Financial instruments included in this category are recognised initially at fair value; transaction costs are taken directly to the consolidated income statement. Gains and losses arising from changes in fair value are included directly in the consolidated income statement and are reported as 'Net trading income'. Interest income and expense and dividend income on financial assets held for trading are included in 'Net trading income' or 'Dividend income', respectively. The instruments are derecognised when the rights to receive cash flows have expired or the Group has transferred substantially all the risks and rewards of ownership and the transfer qualifies for derecognition.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.10 Financial assets (Continued)

2.10.1 Classification (Continued)

(a) Financial assets at fair value through profit or loss (Continued)

The Group designates certain financial assets upon initial recognition as at fair value through profit or loss (fair value option). This designation cannot subsequently be changed. According to HKAS 39, the fair value option is only applied when the following conditions are met:

(i) the application on the fair value option reduces or eliminates an accounting mismatch that would otherwise arise; or

(ii) the financial assets are part of a portfolio of financial instruments which is risk managed and reported to senior management on a fair value basis; or

(iii) the financial assets consists of debt host and an embedded derivatives that must be separated.

To reduce accounting mismatch, the fair value option is applied to certain financial assets that are hedged with interest rate swaps but for which the hedge accounting conditions of HKAS 39 are not fulfilled.

Financial assets for which the fair value option is applied are recognised in the consolidated statement of financial position as 'Financial assets designated at fair value'. Fair value changes relating to financial assets designated at fair value through profit or loss are recognised in 'Net income from financial instruments designated at fair value through profit or loss'.

(b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than: (i) those that the entity intends to sell immediately or in the short term, which are classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss; (ii) those that the entity upon initial recognition designates as available-for-sale; or (iii) those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration.

Loans and receivables are initially recognised at fair value which is the cash given to originally or purchase the loan including any transaction costs and measured subsequently at amortised cost using the effective interest rate method. Loans and receivables are reported in the consolidated statement of financial position as placements with and loans and advances to banks or customers. Interest on loans is included in the separate consolidated income statement and is reported as net interest income. In the case of an impairment, it is reported as a deduction from the carrying value of the loan and recognised in the separate consolidated income statement as impairment losses on loans and advances to customers.

(c) Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity, other than:

(i) those that the Group upon initial recognition designates as at fair value through profit or loss;

(ii) those that the Group designates as available-for-sale investments; and

(iii) those that meet the definition of loans and receivables.

They are initially recognised at fair value including direct and incremental transaction costs and measured subsequently at amortised cost, using the effective interest method. They are derecognised when the rights to receive cash flows have expired.

Interest on held-to-maturity investments are included in the separate consolidated income statement and are reported as net interest income. In the case of an impairment, it has been reported as a deduction from the carrying value of the investment and recognised in the separate consolidated income statement as impairment charges on held-to-maturity investments.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.10 Financial assets (Continued)

2.10.1 Classification (Continued)

(d) Available-for-sale investments

Available-for-sale investments are financial assets that are intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices or that are not classified as loans and receivables, held-to-maturity investments or financial assets at fair value through profit or loss. Available-for-sale investments consist mainly of debt and equity investments.

Available-for-sale investments are initially recognised at fair value which is the cash given including any transaction costs and measured subsequently at fair value with gains and losses been recognised in reconciliation from result to total comprehensive income, except for impairment losses and foreign exchange gains and losses, until the financial assets is derecognised. If an available-for-sale investment is determined to be impaired the cumulative gain or loss previously recognised in the statement of comprehensive income is recognised in separate consolidated income statement. However, interest is calculated using the effective interest method and foreign currency gains and losses on monetary assets classified as available-for-sale investments are recognised in the separate consolidated income statement. Dividends on available-for-sale equity instruments are recognised in the separate consolidated income statement in 'Dividend income' when the Group's right to receive payment is established.

2.10.2 Reclassification of financial assets

The Group may choose to reclassify a non-derivative trading financial asset out of the held for trading category if the financial asset is no longer held for the purpose of selling it in the near term. Financial assets are permitted to be reclassified out of the held for trading category only in rare circumstances arising from a single event that is unusual and highly unlikely to recur in the near term. In addition, the Group may choose to reclassify financial assets that would meet the definition of loans and receivables out of the held for trading or available-for-sale investments categories if the Group has the intention and ability to hold these financial assets for the foreseeable future or until maturity at the date of reclassification.

Reclassifications are made at fair value as of the reclassification date. Fair value becomes the new cost or amortised cost as applicable, and no reversals of fair value gains or losses recorded before reclassification date are subsequently made. Effective interest rates for financial assets reclassified to loans and receivables and held-to-maturity investments categories are determined at the reclassification date. Further increases in estimates of cash flows adjust effective interest rates prospectively.

On reclassification of a financial asset out of the 'at fair value through profit or loss' category all embedded derivatives are re-assessed and, if necessary, separately accounted for.

2.10.3 Recognition and measurement

Regular-way purchases and sales of financial assets at fair value through profit or loss, held-to-maturity investments and available-for-sale investments are recognised on trade-date - the date on which the Group commits to purchase or sell the asset.

Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in the income statement. 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. Financial liabilities are derecognised when they are extinguished - that is, when the obligation is discharged, cancelled or expires.

Available-for-sale investments and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables and held-to-maturity investments are carried at amortised cost using the effective interest method. Gains and losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are included in the income statement in the period in which they arise. They are presented within 'net trading income' (for financial assets that are held for trading), and within 'net income from financial instruments designated at fair value through profit or loss' (for financial assets that are designated at fair value through profit or loss). Gains and losses arising from changes in the fair value of available-for-sale investments are recognised directly in other comprehensive income, until the financial asset is derecognised or impaired. At this time the cumulative gain or loss previously recognised in the equity is recognised in the income statement. However, interest calculated using the effective interest method and foreign currency gains and losses on monetary assets classified as available-for-sale investments are recognised in the income statement.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.10 Financial assets (Continued)

2.10.3 Recognition and measurement (Continued)

The fair values of quoted investments in active markets are based on current bid prices. If there is no active market for a financial asset, the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis and option pricing models, and other valuation techniques commonly used by market participants.

2.11 Impairment of financial assets

(a) Assets carried at amortised cost

The Group assesses at the end of each reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred 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.

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

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower;
- Breach of loan covenants or conditions;
- Initiation of bankruptcy proceedings;
- Deterioration of the borrower's competitive position;
- Deterioration in the value of collateral; and
- Downgrading below investment grade level.

The estimated period between a loss occurring and its identification is determined by local management for each identified portfolio. In general, the periods used vary between 3 months and 12 months; in exceptional cases, longer periods are warranted.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. 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.

For loans and receivables category, 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 investment 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 instruments 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, whether or not foreclosure is probable.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e. on the basis of the Group's grading process that considers asset type, industry, geographical location, collateral type, past due status and other relevant factors). 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.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.11 Impairment of financial assets (Continued)

(a) Assets carried at amortised cost (Continued)

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 currently exist.

Estimates of changes in future cash flows for groups of assets should reflect and be directionally consistent with changes in related observable data from period to period (for example, changes in unemployment rates, property prices, payment status, or other factors indicative of changes in the probability of losses in the Group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Group to reduce any differences between loss estimates and actual loss experience.

When a loan is uncollectible, it is written off against the related allowances for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined.

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

(b) Assets classified as available-for-sale investments

The Group assesses the end of each reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired. For debt securities, the group uses the criteria refer to in (a) above. 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 any such evidence exists for available-for-sale investments, the cumulative loss - measured as the difference between the acquisition cost (net of any principal repayment and amortisation) and the current fair value, less any impairment loss on that investment previously recognised in income statement - is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale investments increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in income statement, the impairment loss is reversed through the consolidated income statement.

(c) Renegotiated loans

Loans that are either subject to collective impairment assessment or individually significant and whose terms have been renegotiated are no longer considered to be past due but are treated as new loans. In subsequent years, the asset is considered to be past due and disclosed only if renegotiated.

2.12 Financial liabilities

Financial liabilities are classified into two categories: financial liabilities at fair value through profit or loss and other financial liabilities. All financial liabilities are classified at inception and recognised initially at fair value.

(a) Financial liabilities at fair value through profit or loss

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

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.12 Financial liabilities (Continued)

(a) Financial liabilities at fair value through profit or loss (Continued)

A financial liability is typically classified as fair value through profit or loss at inception if it meets the following criteria:

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

(ii) Part of a group of financial liabilities that are managed and evaluated on a fair value basis in accordance with a documented risk management or investment strategy and reported to key management personnel on that basis are designated at fair value through profit or loss; and

(iii) Financial instruments, such as debt securities issued, containing one or more embedded derivatives significantly modify the cash flows, are designated at fair value through profit or loss.

Financial liabilities designated as at fair value through profit or loss are designated as such at inception. Financial liabilities designated at fair value through profit or loss are carried at fair value and any gains and losses from changes in fair value are recognised in the income statement.

(b) Other financial liabilities

Other financial liabilities are recognised initially at fair value net of transaction costs incurred. Other financial liabilities are subsequently stated at amortised cost; any difference between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period of the other financial liabilities using the effective interest method.

(c) Determination of fair value

For financial instruments traded in active markets, the determination of fair values of financial assets and financial liabilities is based on quoted market prices or dealer price quotations. This includes listed equity securities and quoted debt instruments on major exchanges (for example, FTSE, NYSE) and broker quotes from Bloomberg and Reuters.

A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. If the above criteria are not met, the market is regarded as being inactive. Indications that a market is inactive are when there is a wide bid-offer spread or significant increase in the bid-offer spread or there are few recent transactions.

For all other financial instruments, fair value is determined using valuation techniques. In these techniques, fair values are estimated from observable data in respect of similar financial instruments, using models to estimate the present value of expected future cash flows or other valuation techniques, using inputs (for example, LIBOR yield curve, FX rates, volatilities and counterparty spreads) existing at the dates of the consolidated statement of financial position.

The Group uses widely recognised valuation models for determining fair values of non-standardised financial instruments of lower complexity, such as options or interest rate and currency swaps. For these financial instruments, inputs into models are generally market-observable.

For more complex instruments, the Group uses developed models, which are usually based on valuation methods and techniques generally recognised as standard within the industry. Valuation models are used primarily to value derivatives transacted in the over-the-counter market, unlisted debt securities (including those with embedded derivatives) and other debt instruments for which markets were or have become illiquid. Some of the inputs to these models may not be market observable and are therefore estimated based on assumptions.

The Group uses its own credit risk spreads in determining the current value for its derivative liabilities and all other liabilities for which it has elected the fair value option. When the Group's credit spreads widen, the Group recognises a gain on these liabilities because the value of the liabilities has decreased. When the Group's credit spread narrow, the Group recognises a loss on these liabilities because the value of the liabilities has increased.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.12 Financial liabilities (Continued)

(c) Determination of fair value (Continued)

The output of a model is always an estimate or approximation of a value that cannot be determined with certainty, and valuation techniques employed may not fully reflect all factors relevant to the positions the Group holds. Valuations are therefore adjusted, where appropriate, to allow for additional factors including model risks, liquidity risk and counterparty risk. Based on the established fair value model governance policies, and related controls and procedures applied, management believes that these valuation techniques are necessary and appropriate to fairly state the values of financial instruments carried at fair value in the consolidated statement of financial position. Price data and parameters used in the measurement procedures applied are generally reviewed carefully and adjusted, if necessary - particularly in view of the current market developments.

In cases when the fair value of unlisted equity instruments cannot be determined reliably, the instruments are carried at cost less impairment. The fair value for loans and receivables as well as liabilities to banks and customers are determined using a present value model on the basis of contractually agreed cash flows, taking into account credit quality, liquidity and costs.

The fair values of contingent liabilities and irrevocable loan commitments correspond to their carrying amounts.

2.13 Derivative financial instruments

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models and options 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, such as the conversion option in a convertible bond where it is not settled by exchanging a fixed amount of cash or another financial asset for a fixed number of own equity instrument, 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 unless the Group chooses to designate the hybrid contracts at fair value through profit or loss.

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in the income statement under net trading income. However, the gains and losses arising from changes in the fair value of derivatives that are managed in conjunction with designated financial assets or financial liabilities are included in 'net income from financial instruments designated at fair value through profit or loss' (Note 2.7).

2.14 Current and deferred income tax

The tax expense 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 in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting period in the countries where the Group's subsidiaries and jointly controlled entities operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is recognised, using the 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.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.14 Current and deferred income tax (Continued)

The principal temporary differences arise from depreciation of property and equipment, revaluation of certain financial assets and liabilities including derivative contracts, provisions for pensions and other post-retirement benefits and tax losses carried forward; and, in relation to acquisitions, on the difference between the fair values of the net assets acquired and their tax base. The rates enacted or substantively enacted at the end of the reporting period are used to determine deferred income tax. However, the deferred income tax is not accounted for 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 assets are recognised only 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 provided on temporary differences arising on investments in subsidiaries and jointly controlled entities, except for deferred income tax liability where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not be reversed in the foreseeable future.

Deferred tax related to fair value re-measurement of available-for-sale investments, which are charged or credited to other comprehensive income, is also credited or charged to other comprehensive income and is subsequently recognised in the income statement together with the deferred gain or loss.

2.15 Employee benefits

(a) Retirement benefit costs

The Group operates three retirement benefit schemes comprising of a defined contribution scheme, a Mandatory Provident Fund Scheme and a defined benefit scheme that are available to the Group's employees. However, the principal schemes that the Group contributes to are the defined contribution scheme and the Mandatory Provident Fund Scheme. The assets of the Group's Mandatory Provident Fund Scheme, the defined contribution scheme and the defined benefit scheme are held separately from those of the Group in independently administered funds.

The Group's contributions to the defined contribution scheme and the Mandatory Provident Fund Scheme are charged to the income statement.

The defined benefit scheme is funded by payments from the Group by taking recommendations of independent qualified actuaries. The defined benefit costs are assessed using the Attained Age Method and the cost of providing the benefit is charged to the income statement so as to spread the regular cost over the service lives of employees in accordance with the advice of qualified actuaries, who value the scheme once every three years.

(b) Employee leave entitlements

Employee entitlements to annual leave are recognised when they accrue to employees. Employee entitlements to sick leave and maternity leave are recognised when the absences occur.

(c) Termination benefits

Termination benefits are payable when employment is terminated by the Group before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits when it is demonstrably committed: a termination when the entity has a detailed formal plan to terminate the employment of current employees without possibility of withdrawal. In the case of an offer made to encourage voluntary redundancy the termination benefits are measured based on the number of employees expected to accept the offer. Benefits falling due more than 12 months after the end of the reporting period are discounted to present value.

2.16 Related parties

For the purposes of these consolidated financial statements, parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.17 Investment properties

Property that is held for long-term rental yields or for capital appreciation or both is classified as investment property. Investment properties are land and office buildings located in Hong Kong. Investment properties are measured at cost less subsequent accumulated depreciation and any accumulated impairment losses. Depreciation is charged so as to write off the cost of investment properties using the straight-line method over the shorter of the leases or 40 years.

2.18 Intangible assets

Intangible assets comprises separately identifiable intangible items arising from business combinations. Intangible assets are recognised at cost. The cost of an intangible asset acquired in a business combination is its fair value at the date of acquisition. Intangible assets with a definite useful life are amortised using the straight-line method over their estimated useful economic life, generally not exceeding 20 years. Intangible assets with an indefinite useful life are not amortised. Generally all identified intangible assets of the Group have a definite useful life. At the end of each reporting period, intangible assets are reviewed for indications or impairment or changes in estimated future benefits. If such indications exist, the intangible assets are analysed to assess whether their carrying amount is fully recoverable. An impairment loss is recognised if the carrying amount exceeds the recoverable amount.

The Group chooses to use the cost model for the measurement after initial recognition.

Intangible assets with indefinite useful life are annually tested for impairment and whenever there is an indication that the asset may be impaired.

(a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in intangible assets.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose identified according to HKFRS 8.

Goodwill is tested annually as well as whenever a trigger event has been observed for impairment by comparing the present value of the expected future cash flows from a cash generating unit with the carrying value of its net assets, including attributable goodwill and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

(b) Computer software

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

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

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

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

Computer software development costs recognised as assets are amortised over their estimated useful lives.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.19 Repossessed assets

Repossessed collateral assets are recorded as 'Repossessed assets' and reported in 'Other assets' and the relevant loans are derecognised. The repossessed collateral assets are measured at lower of carrying amount and fair value less cost to sell.

2.20 Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition including cash, balances with banks, placements with and loans and advances to banks, treasury bills and certificate of deposits that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

2.21 Fiduciary activities

The Group commonly acts as trustees and in other fiduciary capacities, for a fee and commission income, that result in the holding or placing of assets on behalf of individuals, trusts and other institutions. These assets and income arising thereon are excluded from these financial statements, as they are not assets of the Group.

2.22 Impairment of investment in subsidiaries, jointly controlled entities and non-financial assets

Assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. 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). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

2.23 Provisions

Provisions for restructuring costs and legal claims are recognised when: the Group has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognised as interest expense.

2.24 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 debt instrument. Such financial guarantees are given to banks, financial institutions and other bodies on behalf of customers to secure loans, overdrafts and other banking facilities.

Financial guarantees are initially recognised in the consolidated financial statements at fair value on the date the guarantee was given. The fair value of a financial guarantee at the time of signature is zero because all guarantees are agreed on arm's length terms and the value of the premium agreed corresponds to the value of the guarantee obligation. No receivable for the future premiums is recognised. Subsequent to initial recognition, the Group's liabilities under such guarantees are measured at the higher of the initial amount, less amortisation of fees recognised in accordance with HKAS 18, and the best estimate of the amount required to settle the guarantee. These estimates are determined based on experience of similar transactions and history of past losses, supplemented by the judgment of management. The fee income earned is recognised on a straight-line basis over the life of the guarantee.

Any increase in the liability relating to guarantees is reported in the consolidated income statement within other operating expenses.

3 FINANCIAL RISK MANAGEMENT

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

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

The Group has in place policies and procedures for the identification, measurement, control and monitoring of credit, liquidity, market, interest rate, foreign exchange and operational risks. Market risk includes currency risk, interest rate and other price risk. One of the major functions of the Board of Directors is to ensure that the Group establishes policies, procedures and controls to manage the various types of risk it faces. The Board of Directors has delegated its powers to the Executive Committee, the Asset and Liability Committee, the Credit Committee, the Operational Risk Management Committee and the Product Development Supervisory Committee for the supervision of major functional areas, and in particular, the Executive Committee has been delegated with the authority to oversee and guide the management of different risks. Senior management is always watchful for changes in economic, political and market conditions in which the Group operates and the inherent risks the Group faces.

The Risk Management Department is responsible for monitoring the overall risk management of the Group's operations, except for credit risk, which is managed by the Credit Committee. Reconciliation procedures are also in place to ensure that the systems capture all necessary data. Prior to implementation of any new product or service, various analyses, testing, development and planning will be performed and its proposal will be endorsed by the Product Development Supervisory Committee before submission to the management for approval. All of the above arrangements ensure that the risk management processes are operating effectively.

Delegated by the Board of Directors, the Audit Committee has an oversight role over the above management functions as a whole. Supporting the Audit Committee, the Audit Department performs regular audits to ensure compliance with the policies and procedures.

3.1 Credit risk

The Group takes on exposure to credit risk, which is the risk that a counterparty will cause a financial loss for the Group by failing to discharge an obligation. Significant changes in the economy, or in the health of a particular industry segment that represents a concentration in the Group's portfolio, could result in losses that are different from those provided for at the end of the reporting period.

The Group has in place effective credit review, monitoring and control systems including an effective loan classification system that identify, monitor, and determine loan loss provisions in a timely manner. Management therefore carefully manages its exposure to credit risk.

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

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

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. The Group has in place effective monitoring and control systems to identify, monitor and address problem credits in an accurate and timely manner. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees. The Group further mitigates credit risk by entering into netting arrangements with counterparties such as banks with which it undertakes credit activities.

The Group has issued credit related commitments including guarantees and letters of credit. These instruments carry similar credit risk as loans.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.1 Risk limit control and mitigation policies

(a) Collateral

The Group employs a range of policies and practices to mitigate credit risk. The most traditional of these methods is the taking of security for funds advanced, which is a common practice. The Group implements guidelines on the acceptability of specific classes of collateral for credit risk mitigation. The principal collateral types for loans and advances are:

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

In addition to the above, the Group will also seek for guarantee where appropriate. To minimise credit loss, the Group will seek additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances which are partially secured or unsecured.

(b) Derivatives

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

(c) Credit-related commitments

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit - which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties - carry the same credit risk as loans. Documentary and commercial letters of credit - which are written undertakings by the Group on behalf of a customer authorising a third party to draw drafts on the Group up to a stipulated amount under specific terms and conditions - are collateralised by the underlying shipments of goods to which they relate and therefore carry less risk than a direct loan.

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

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.2 Impairment and provisioning policies

The Group has established effective control systems that enable to Group to identify, monitor, and determine loan loss provisions in a timely manner. Policies and procedures are in place to ensure the aggregate amount of individually and collectively assessed loan loss provisions are adequate to absorb estimated credit losses in the loan portfolio. The table below shows the percentage of the Group's on- and off-balance sheet items relating to loans and advances and the associated impairment provision for each of the Group's internal loan classification categories:

The Group and the Bank

	2011		2010 (restated)	
	Loans and advances (%)	Impairment provision (%)	Loans and advances (%)	Impairment provision (%)
1 – pass	96.65	0.39	95.72	0.43
2 – special mentioned	1.69	0.47	2.71	0.47
3 – sub-standard	1.59	6.20	1.22	8.52
4 – doubtful	0.03	16.20	0.29	24.66
5 – loss	0.04	51.63	0.06	46.99
	100.00		100.00	

Grade 1 'Pass' represents loans for which borrowers are current in meeting commitments and full repayment of interest and principal is not in doubt.

Grade 2 'Special mentioned' represents loans with significant deficiencies and potential weakness such that if adverse conditions persist, ultimate loss for the Bank may occur.

Grade 3 'Sub-standard' represents loans in which borrowers are displaying a definable weakness that is likely to jeopardise repayment. These loans include rescheduled loans and loans where some loss of principal or interest is possible after taking account of the net realisable value of security.

Grade 4 'Doubtful' represents loans which collection in full is improbable and the Group expects to sustain a loss of interest and/ or principal after taking account of the net realisable value of security.

Grade 5 'Loss' represents loans which considered as uncollectible after exhausting all collection efforts such as realisation of collateral, initiation of legal proceedings and need to be fully or partially written off.

The credit review, monitoring and control systems assist management to determine whether objective evidence of impairment exists under HKAS 39, based on the following criteria set out by the Group:

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower;
- Breach of loan covenants or conditions;
- Initiation of bankruptcy proceedings;
- Deterioration of the borrower's competitive position; and
- Deterioration in the value of collateral.

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

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

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

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

The Group

	Maximum exposure	
	2011	2010 (restated)
Credit risk exposures relating to on-balance sheet assets are as follows:		
Balances with banks	16,944,163	17,300,684
Placements with and loans and advances to banks	14,865,476	13,274,323
Loans and advances to customers:		
Loans to individuals:		
– Overdrafts	533,500	420,292
– Credit cards	338,764	311,244
– Term loans and others	5,573,480	5,118,101
– Mortgages	6,912,793	6,764,114
Loans to corporate entities:		
– Large corporate customers and others	35,397,648	31,332,954
– Small and medium size enterprises (SMEs)	6,439,471	6,760,095
Financial assets held for trading:		
– Debt securities	321,358	494,869
Derivative financial instruments	70,294	61,484
Investment securities:		
– debt securities - available-for-sale	20,447,675	19,792,686
– debt securities - held-to-maturity	2,764,783	2,766,411
Other assets	1,606,222	1,615,370
Credit risk exposures relating to off-balance sheet items are as follows:		
– Financial guarantees	2,340,000	2,186,902
– Loan commitments and other credit related liabilities	39,058,307	46,880,506
At 31st December	153,613,934	155,080,035

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.3 Maximum exposure to credit risk before collateral held or other credit enhancements (Continued)

The Bank

	Maximum exposure	
	2011	2010 (restated)
Credit risk exposures relating to on-balance sheet assets are as follows:		
Balances with banks	16,944,163	17,300,684
Placements with and loans and advances to banks	14,865,476	13,274,323
Loans and advances to customers:		
Loans to individuals:		
– Overdrafts	533,500	420,292
– Credit cards	338,764	311,244
– Term loans and others	5,573,480	5,118,101
– Mortgages	6,912,793	6,764,114
Loans to corporate entities:		
– Large corporate customers and others	35,397,648	31,332,954
– Small and medium size enterprises (SMEs)	6,439,471	6,760,095
Financial assets held for trading:		
– Debt securities	321,358	494,869
Derivative financial instruments	70,294	61,484
Investment securities:		
– debt securities - available-for-sale	20,347,481	19,594,072
– debt securities - held-to-maturity	662,366	757,471
Other assets	1,420,350	1,250,005
Credit risk exposures relating to off-balance sheet items are as follows:		
– Financial guarantees	2,340,000	2,186,902
– Loan commitments and other credit related liabilities	39,058,307	46,880,506
At 31st December	151,225,451	152,507,116

The above tables represent a worst case scenario of credit risk exposure to the Group and the Bank at 31st December 2011 and 2010, without taking account of any collateral held or other credit enhancements attached. For on-balance sheet assets, the exposures set out above are based on net carrying amounts. For letters of guarantee issued, the maximum exposure to credit risk is the maximum amount that the bank could be required to pay if the guarantees are called upon. For loan commitments and other credit related liabilities that are irrevocable over the life of the respective facilities or revocable in the event of a significant adverse change, the maximum exposure to credit risk is disclosed as the full amount of the committed facilities.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.3 Maximum exposure to credit risk before collateral held or other credit enhancements (Continued)

Credit risk mitigation, collateral and other credit enhancements

The Group uses a variety of techniques to reduce the credit risk arising from its lending activities. Enforceable legal documentation establishes the Group's direct, irrevocable and unconditional recourse to any collateral, security or other credit enhancements provided.

The table below describes the nature of collateral held and their financial effect by class of financial asset:

Balances and placements with and loans and advances to banks	These exposures are generally considered to be low risk due to the nature of the counterparties. Collateral is generally not sought on these balances.
Securities lending	The Group has in place general guidelines on maximum loan to value ratio under securities lending. The loans and advances under securities lending are fully secured by the securities pledged.
Loans and advances	These exposures are secured, partially secured or unsecured depending on the type of collateral and type of facilities offered to customers. The major types of collateral taken include residential properties, other properties, bank deposits, stocks and shares and wealth management products. Recognised guarantees are also employed by the Group for credit enhancement. As at 31st December 2011, the collateral coverage of advances to customers is 86% (2010: 85%).
Trading debt securities	These exposures are carried at fair value which reflects the credit risk. No collateral is sought directly from the issuer or the counterparty; however this may be implicit in the terms of the instrument.
Derivative financial instruments	Master netting agreements are typically used to enable the effects of derivative assets and liabilities with the same counterparty to be offset when measuring these exposures.
Available-for-sale investment securities - debt securities	The exposures are subject to approved counterparty limit and country limit and under close monitoring in accordance with relevant policies of the Group. Impairment assessment is also conducted periodically.
Held-to-maturity investment securities - debt securities	The exposures are subject to approved counterparty limit and country limit and under close monitoring in accordance with relevant policies of the Group. Impairment assessment is also conducted periodically.
Contingent liabilities and commitments	The components and nature of contingent liabilities and commitments are disclosed in Note 35. Regarding the commitments that are unconditionally cancellable without prior notice, the Group would withdraw the credit facilities extended to borrowers in case their credit quality deteriorates. Accordingly, these commitments do not expose the Group to significant credit risk.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.4 Loans and advances

Loans and advances are summarised as follows:

The Group and the Bank

	2011	2010 (restated)
	Loans and advances to customers	Loans and advances to customers
Neither past due nor impaired	53,493,718	49,358,770
Past due but not impaired	1,065,672	867,953
Impaired	920,195	801,384
Gross	55,479,585	51,028,107
Less: allowance for impairment	(283,929)	(321,307)
Net	55,195,656	50,706,800

The total impairment provision for loans and advances is HK$283,929,000 (2010: HK$321,307,000) of which HK$69,069,000 (2010: HK$104,685,000) represents the individually impaired loans and the remaining amount of HK$214,860,000 (2010:HK$216,622,000) represents the collective assessment provision. Further information of the impairment allowance for loans and advances to a bank and to customers is provided in Note 19.

(a) Loans and advances neither past due nor impaired

The credit quality of the portfolio of loans and advances that were neither past due nor impaired can be assessed by reference to the policies and procedures adopted by the Group.

The Group and the Bank As at 31st December 2011

	Individual (retail customers)				Corporate entities		
	Overdrafts	Credit cards	Term loans and others	Mortgages	Large corporate customers and others	SMEs	Total loans and advances to customers
Grades:							
1 – pass	504,697	336,083	5,381,864	6,646,265	33,732,538	6,088,799	52,690,246
2 – special mentioned	20,091	5,575	45,862	86,739	419,520	225,685	803,472
Total	524,788	341,658	5,427,726	6,733,004	34,152,058	6,314,484	53,493,718

The Group and the Bank As at 31st December 2010 (restated)

	Individual (retail customers)				Corporate entities		
	Overdrafts	Credit cards	Term loans and others	Mortgages	Large corporate customers and others	SMEs	Total loans and advances to customers
Grades:							
1 – pass	392,339	305,786	4,893,918	6,517,322	29,730,143	6,266,948	48,106,456
2 – special mentioned	12,847	7,700	69,641	106,541	803,918	251,667	1,252,314
Total	405,186	313,486	4,963,559	6,623,863	30,534,061	6,518,615	49,358,770

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.4 Loans and advances (Continued)

(b) Loans and advances past due but not impaired

Loans and advances less than 90 days past due are not considered impaired, unless other information is available to indicate the contrary. Gross amount of loans and advances by class to customers that were past due but not impaired were as follows:

The Group and the Bank As at 31st December 2011

	Individual (retail customers)				
	Overdrafts	Credit cards	Term loans and others	Mortgages	Total
Past due up to 30 days	765	1,640	98,918	87,978	189,301
Past due 30 – 60 days	–	500	35,002	23,300	58,802
Past due 60 – 90 days	–	416	1,153	6,042	7,611
Past due over 90 days	307	–	1,880	1,846	4,033
Total	1,072	2,556	136,953	119,166	259,747
Fair value of collateral	1,468	–	215,360	213,216	430,044

	Corporate entities		
	Large corporate customers and others	SMEs	Total
Past due up to 30 days	701,284	86,016	787,300
Past due 30 – 60 days	7,364	4,592	11,956
Past due 60 – 90 days	4,006	2,663	6,669
Past due over 90 days	–	–	–
Total	712,654	93,271	805,925
Fair value of collateral	1,877,595	192,138	2,069,733

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.4 Loans and advances (Continued)

(b) Loans and advances past due but not impaired (Continued)

The Group and the Bank As at 31st December 2010

	Individual (retail customers)				
	Overdrafts	Credit cards	Term loans and others	Mortgages	Total
Past due up to 30 days	–	1,615	118,331	93,717	213,663
Past due 30 – 60 days	9	462	12,234	18,308	31,013
Past due 60 – 90 days	14,774	285	581	3,117	18,757
Past due over 90 days	–	–	1,223	3,245	4,468
Total	14,783	2,362	132,369	118,387	267,901
Fair value of collateral	15,919	–	321,265	365,659	702,843

	Corporate entities		
	Large corporate customers and others	SMEs	Total
Past due up to 30 days	465,174	62,441	527,615
Past due 30 – 60 days	8,568	15,121	23,689
Past due 60 – 90 days	48,171	577	48,748
Past due over 90 days	–	–	–
Total	521,913	78,139	600,052
Fair value of collateral	873,619	149,016	1,022,635

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

(c) Loans and advances overdue for more than 3 months

(i) Gross amount of overdue loans

The Group and the Bank

	2011		2010	
	Gross amount of overdue loans	% of total	Gross amount of overdue loans	% of total
Gross advances to customers which have been overdue for:				
– six months or less but over three months	89,316	0.16	13,766	0.03
– one year or less but over six months	158,417	0.29	58,393	0.11
– over one year	34,442	0.06	78,065	0.15
	282,175	0.51	150,224	0.29

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.4 Loans and advances (Continued)

(c) Loans and advances overdue for more than 3 months (Continued)

(ii) Value of collateral held and impairment allowances against overdue loans and advances

The Group and the Bank

	Outstanding amount of loans and advances	Current market value of collateral	Covered portion by collateral	Uncovered portion by collateral	Impairment allowances – individual assessment
31st December 2011					
Overdue loans and advances on:					
– Customers	282,175	399,172	200,863	81,312	47,841
31st December 2010					
Overdue loans and advances on:					
– Customers	150,224	192,404	109,047	41,177	21,600

Collateral held against such loans mainly include mortgages over properties.

(d) Loans and advances individually impaired

(i) Loans and advances to customers

The individually impaired loans and advances to customers before taking into consideration the cash flows from collateral held is HK$920,195,000 (2010: HK$801,384,000).

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

The Group and the Bank

	Individual				Corporate entities		Total		
	Overdrafts	Credit cards	Term loans and others	Mortgages	Large corporate customers and others	SMEs		% of total loans and advances to customers	Impairment allowances
31st December 2011									
Individually impaired loans	9,671	4,163	34,791	86,846	721,250	63,474	920,195	1.66	69,069
Fair value of collateral	29,484	–	54,553	172,383	842,327	134,985	1,233,732		
31st December 2010 (restated)									
Individually impaired loans	2,325	4,829	50,385	47,582	500,098	196,165	801,384	1.57	104,685
Fair value of collateral	6,773	–	75,999	99,859	430,697	245,206	858,534		

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.4 Loans and advances (Continued)

(e) Loans and advances renegotiated

Restructuring activities include extended payment arrangements, approved external management plans, modification and deferral of payments. Following restructuring, a previously overdue customer account is reset to a normal status and managed together with other similar accounts. Restructuring policies and practices are based on indicators or criteria which, in the judgment of local management, indicate that payment will most likely continue. These policies are kept under continuous review. Restructuring is most commonly applied to term loans, in particular customer finance loans. Renegotiated loans that would otherwise be past due or impaired totalled HK$157,799,000 at 31st December 2011 (2010: HK$319,303,000).

The Group and the Bank

	2011	2010
Loans and advances to customers – individuals:		
– Credit cards	526	3,105
– Term loans and others	2,498	11,902
– Mortgages	4,669	753
Loans and advances to customers – corporate entities:		
– SMEs	–	418
– Large corporate customers and others	150,106	303,125
Total	157,799	319,303

(f) Rescheduled advances net of amounts included in advances overdue for more than 3 months

The Group and the Bank

	2011		2010 (restated)	
		% of total loans and advances to customers		% of total loans and advances to customers
Loans and advances to customers	181,940	0.33	343,938	0.67

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.5 Debt securities

The table below presents an analysis of debt securities by rating agency designation at 31st December, based on Standard & Poor's ratings or their equivalent.

Most of the issuers of the unrated debt securities included below have rating from rating agency.

The Group As at 31st December 2011

	Financial assets held for trading	Available-for-sale investments	Held-to-maturity investments	Total
AAA	–	834,326	2,364,477	3,198,803
AA- to AA+	182,183	6,372,790	–	6,554,973
A- to A+	17,560	5,954,440	400,306	6,372,306
Lower than A-	–	330,556	–	330,556
Unrated	121,615	6,955,563	–	7,077,178
Total	321,358	20,447,675	2,764,783	23,533,816

The Bank As at 31st December 2011

	Financial assets held for trading	Available-for-sale investments	Held-to-maturity investments	Total
AAA	–	823,874	266,080	1,089,954
AA- to AA+	182,183	6,338,868	–	6,521,051
A- to A+	17,560	5,954,440	396,286	6,368,286
Lower than A-	–	330,556	–	330,556
Unrated	121,615	6,899,743	–	7,021,358
Total	321,358	20,347,481	662,366	21,331,205

The Group As at 31st December 2010

	Financial assets held for trading	Available-for-sale investments	Held-to-maturity investments	Total
AAA	166,656	2,271,590	1,827,616	4,265,862
AA- to AA+	103,773	7,597,659	579,039	8,280,471
A- to A+	71,900	5,870,362	166,850	6,109,112
Lower than A-	–	337,089	3,858	340,947
Unrated	152,540	3,715,986	189,048	4,057,574
Total	494,869	19,792,686	2,766,411	23,053,966

The Bank As at 31st December 2010

	Financial assets held for trading	Available-for-sale investments	Held-to-maturity investments	Total
AAA	166,656	2,143,310	78,069	2,388,035
AA- to AA+	103,773	7,541,143	327,544	7,972,460
A- to A+	71,900	5,867,017	162,813	6,101,730
Lower than A-	–	337,089	–	337,089
Unrated	152,540	3,705,513	189,045	4,047,098
Total	494,869	19,594,072	757,471	20,846,412

There were no overdue debt securities in the year of 2011 (2010: Nil).

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.6 Repossessed collateral

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

The Group and the Bank

	Carrying amount	
	2011	2010
Nature of assets		
Commercial property	–	1,507
Residential properties	–	40,145

At 31st December 2011, the fair value of repossessed assets of the Group and the Bank amounted to HK$22,993,000 (2010: HK$42,770,000).

Repossessed properties are sold as soon as practicable with the proceeds used to reduce the outstanding indebtedness. Repossessed properties are classified in the statement of financial position within other assets.

3.1.7 Concentration of risks of financial assets with credit risk exposure

(a) Geographical sectors

The following table breaks down the Group's main credit exposure at their carrying amounts, as categorised by geographical region as of 31st December 2011. For this table, the Group has allocated exposures to regions based on the country of domicile of its counterparties. Credit risk exposure by geographical sectors is classified according to the location of counterparties after taking into account the transfer of risk.

The Group As at 31st December 2011

	Hong Kong	Asia Pacific excluding Hong Kong	North and South America	Europe	Middle East and Africa	Total
Balances with banks	12,310,994	12,787,840	1,456,341	767,523	128	27,322,826
Placements with and loans and advances to banks	4,797,831	10,067,645	–	–	–	14,865,476
Loans and advances to customers:						
Loans to individuals:						
– Overdrafts	525,339	7,469	219	473	–	533,500
– Credit cards	336,033	2,731	–	–	–	338,764
– Term loans and others	4,400,408	291,941	875,259	5,872	–	5,573,480
– Mortgages	5,885,131	119,803	344,439	562,713	707	6,912,793
Loans to corporate entities:						
– Large corporate customers and others	25,407,439	1,286,019	8,313,002	391,188	–	35,397,648
– SMEs	5,868,011	365,380	206,080	–	–	6,439,471
Financial assets held for trading – debt securities	86,862	53,305	181,191	–	–	321,358
Derivative financial instruments	37,628	581	2,742	29,343	–	70,294
Investment securities – debt securities	7,556,279	8,036,682	4,521,518	3,097,979	–	23,212,458
Other assets	1,571,917	1,395	32,050	860	–	1,606,222
	68,783,872	33,020,791	15,932,841	4,855,951	835	122,594,290

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.7 Concentration of risks of financial assets with credit risk exposure (Continued)

(a) Geographical sectors (Continued)

The Group As at 31st December 2010 (restated)

	Hong Kong	Asia Pacific excluding Hong Kong	North and South America	Europe	Middle East and Africa	Total
Balances with banks	10,224,533	13,335,025	655,645	713,477	42	24,928,722
Placements with and loans and advances to banks	2,723,641	10,155,918	–	394,764	–	13,274,323
Loans and advances to customers:						
Loans to individuals:						
– Overdrafts	418,845	942	26	479	–	420,292
– Credit cards	307,585	3,659	–	–	–	311,244
– Term loans and others	3,901,271	137,482	1,061,275	18,073	–	5,118,101
– Mortgages	6,052,925	109,754	303,616	296,900	919	6,764,114
Loans to corporate entities:						
– Large corporate customers and others	22,399,842	1,011,755	7,718,212	203,145	–	31,332,954
– SMEs	5,901,648	290,306	531,833	34,505	1,803	6,760,095
Financial assets held for trading – debt securities	134,904	193,310	166,655	–	–	494,869
Derivative financial instruments	44,595	668	3,314	12,907	–	61,484
Investment securities – debt securities	5,765,357	7,783,683	5,638,992	3,371,065	–	22,559,097
Other assets	1,532,123	1,637	80,874	736	–	1,615,370
	59,407,269	33,024,139	16,160,442	5,046,051	2,764	113,640,665

The Bank As at 31st December 2011

	Hong Kong	Asia Pacific excluding Hong Kong	North and South America	Europe	Middle East and Africa	Total
Balances with banks	12,310,994	12,787,840	1,456,341	767,523	128	27,322,826
Placements with and loans and advances to banks	4,797,831	10,067,645	–	–	–	14,865,476
Loans and advances to customers:						
Loans to individuals:						
– Overdrafts	525,339	7,469	219	473	–	533,500
– Credit cards	336,033	2,731	–	–	–	338,764
– Term loans and others	4,400,408	291,941	875,259	5,872	–	5,573,480
– Mortgages	5,885,131	119,803	344,439	562,713	707	6,912,793
Loans to corporate entities:						
– Large corporate customers and others	25,407,439	1,286,019	8,313,002	391,188	–	35,397,648
– SMEs	5,868,011	365,380	206,080	–	–	6,439,471
Financial assets held for trading – debt securities	86,862	53,305	181,191	–	–	321,358
Derivative financial instruments	37,628	581	2,742	29,343	–	70,294
Investment securities – debt securities	5,456,338	7,985,653	4,500,507	3,067,349	–	21,009,847
Other assets	1,386,045	1,395	32,050	860	–	1,420,350
	66,498,059	32,969,762	15,911,830	4,825,321	835	120,205,807

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.7 Concentration of risks of financial assets with credit risk exposure (Continued)

(a) Geographical sectors (Continued)

The Bank As at 31st December 2010 (restated)

	Hong Kong	Asia Pacific excluding Hong Kong	North and South America	Europe	Middle East and Africa	Total
Balances with banks	10,224,533	13,335,025	655,645	713,477	42	24,928,722
Placements with and loans and advances to banks	2,723,641	10,155,918	–	394,764	–	13,274,323
Loans and advances to customers:						
Loans to individuals:						
– Overdrafts	418,845	942	26	479	–	420,292
– Credit cards	307,585	3,659	–	–	–	311,244
– Term loans and others	3,901,271	137,482	1,061,275	18,073	–	5,118,101
– Mortgages	6,052,925	109,754	303,616	296,900	919	6,764,114
Loans to corporate entities:						
– Large corporate customers and others	22,399,842	1,011,755	7,718,212	203,145	–	31,332,954
– SMEs	5,901,648	290,306	531,833	34,505	1,803	6,760,095
Financial assets held for trading – debt securities	134,904	193,310	166,655	–	–	494,869
Derivative financial instruments	44,595	668	3,314	12,907	–	61,484
Investment securities – debt securities	3,745,943	7,747,612	5,518,432	3,339,556	–	20,351,543
Other assets	1,166,758	1,637	80,874	736	–	1,250,005
	57,022,490	32,988,068	16,039,882	5,014,542	2,764	111,067,746

(b) Industry sectors

The following table breaks down the Group's main credit exposure at their carrying amounts, as categorised by the industry sectors of its counterparties.

For the industry analysis of investment securities - debt securities, refer to Note 22 and 23.

The Group and the Bank As at 31st December 2011

	Financial institutions	Manufacturing	Real estate	Wholesale and retail trade	Import and export trade	Other industries	Individuals	Total
Balances with banks	27,322,826	–	–	–	–	–	–	27,322,826
Placements with and loans and advances to banks	14,865,476	–	–	–	–	–	–	14,865,476
Loans and advances to customers:								
Loans to individuals:								
– Overdrafts	–	–	–	–	–	–	533,500	533,500
– Credit cards	–	–	–	–	–	–	338,764	338,764
– Term loans and others	–	–	–	–	–	–	5,573,480	5,573,480
– Mortgages	–	–	–	–	–	–	6,912,793	6,912,793
Loans to corporate entities:								
– Large corporate customers and others	–	2,363,312	11,806,141	959,413	7,280,163	12,988,619	–	35,397,648
– SMEs	–	656,384	2,158,512	334,134	746,860	2,543,581	–	6,439,471
	42,188,302	3,019,696	13,964,653	1,293,547	8,027,023	15,532,200	13,358,537	97,383,958

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.7 Concentration of risks of financial assets with credit risk exposure (Continued)

(b) Industry sectors (Continued)

The Group and the Bank As at 31st December 2010 (restated)

	Financial institutions	Manufacturing	Real estate	Wholesale and retail trade	Import and export trade	Other industries	Individuals	Total
Balances with banks	24,928,722	–	–	–	–	–	–	24,928,722
Placements with and loans and advances to banks	13,274,323	–	–	–	–	–	–	13,274,323
Loans and advances to customers:								
Loans to individuals:								
– Overdrafts	–	–	–	–	–	–	420,292	420,292
– Credit cards	–	–	–	–	–	–	311,244	311,244
– Term loans and others	–	–	–	–	–	–	5,118,101	5,118,101
– Mortgages	–	–	–	–	–	–	6,764,114	6,764,114
Loans to corporate entities:								
– Large corporate customers and others	–	1,913,789	11,472,658	527,321	5,314,990	12,104,196	–	31,332,954
– SMEs	–	689,702	2,514,224	257,539	849,000	2,449,630	–	6,760,095
	38,203,045	2,603,491	13,986,882	784,860	6,163,990	14,553,826	12,613,751	88,909,845

3.2 Market risk

Market risk is the risk that interest rates, foreign exchange rates, equity or commodity prices will move relative to positions taken, resulting in profits or losses. In the ordinary course of business, the Group enters into various types of financial instruments, mainly forward exchange contracts, that are mainly customer-driven and are entered into on behalf of customers. The Group market risk is managed by the Treasury Department and monitored by management under the limits and guidelines laid down in the foreign exchange risk management policy and policy on allocating transactions of financial instruments to the trading, non-trading or investment book approved by the Board of Directors.

3.2.1 Market risk measurement techniques

The measuring procedures and limit system used for market risk management have been approved by the Board of Directors. Limits on notional, stop loss and sensitivity are set for trading positions which are marked-to-market daily. The transactions included in the trading book as at 31st December 2011 and 2010 for the Group and the Bank are not significant.

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

3.2.2 Market risk sensitivity summary for 2011 and 2010

The Group uses different types of derivatives to manage foreign exchange and interest rate sensitivity primarily by hedging its underlying positions. The types of derivatives used by the Group include forward exchange rate and interest rate swap contracts which are typically made over-the-counter and are managed within limits approved by the Directors or with prior approval obtained from the Executive Committee. The policy on the use of derivatives is reviewed by the Executive Committee and recommended changes and amendments are submitted to the Board for consideration.

Interest rate risk

At 31st December 2011, if market interest rates had been 100 basis points higher (2010: 100 basis points higher) with other variables held constant, profit before tax for the year would have been HK$31,216,000 lower (2010: HK$61,002,000 lower), mainly due to an increase of interest-bearing liabilities as compared to last year, which is partly offset by a higher net interest income earned on floating rate financial instruments. Available-for-sale investment revaluation shown as other comprehensive income would have been an expense of HK$440,020,000 (2010: an expense of HK$468,816,000).

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.2 Market risk (Continued)

3.2.2 Market risk sensitivity summary for 2011 and 2010 (Continued)

Foreign exchange risk

At 31st December 2011, over 90% (2010: over 90%) of the net on-balance sheet position of the Group were denominated in HKD and USD, and these two currencies were closely pegged, there is immaterial foreign exchange risk arising from the translation of foreign-currency denominated financial assets and financial liabilities into HKD.

3.2.3 Foreign exchange risk

Foreign exchange risk is the risk that the holding of foreign currencies will affect the Group's position as a result of a change in foreign currency exchange rates. The Group takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Group's foreign exchange risk arises primarily from currency exposures originated by the Group's commercial banking businesses. The foreign exchange risk is managed by the Treasury Department and monitored by management and the Asset and Liability Committee within position limits set in the foreign exchange risk management policy approved by the Directors. The Board sets limits on the level of exposure by currency and in aggregate for both overnight and intra-day positions, which are monitored daily. The table below summarises the Group's exposure to foreign currency exchange rate risk at 31st December. Included in the table are the Group's financial instruments at carrying amounts, categorised by currency.

Concentrations of currency risk on- and off-balance sheet financial instruments

The Group As at 31st December 2011

	HK$	US$	CNY	Other	Total
Assets					
Cash and balances with banks	13,424,551	4,448,597	3,724,976	6,140,968	27,739,092
Placements with and loans and advances to banks	5,206,965	4,813,643	4,260,343	584,525	14,865,476
Loans and advances to customers	35,029,283	17,260,451	1,406,103	1,499,819	55,195,656
Financial assets held for trading	9,108	294,962	140,167	–	444,237
Derivative financial instruments	–	10,084	24,543	35,667	70,294
Investment securities:					
– Available-for-sale	8,059,562	9,882,967	462,101	3,604,030	22,008,660
– Held-to-maturity	2,098,502	666,281	–	–	2,764,783
Total	63,827,971	37,376,985	10,018,233	11,865,009	123,088,198
Liabilities					
Deposits and balances from banks	1,804,531	1,951,544	184,653	391,072	4,331,800
Deposits from customers	50,955,747	31,674,252	8,967,105	11,500,092	103,097,196
Derivative financial instruments	–	8,327	19,245	17,837	45,409
Other liabilities	729,000	341,788	47,176	54,664	1,172,628
Total	53,489,278	33,975,911	9,218,179	11,963,665	108,647,033
Net on-balance sheet position	10,338,693	3,401,074	800,054	(98,656)	14,441,165
Credit commitments	25,791,725	14,062,491	591,505	952,586	41,398,307

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.2 Market risk (Continued)

3.2.3 Foreign exchange risk (Continued)

Concentrations of currency risk on- and off-balance sheet financial instruments

The Group As at 31st December 2010 (restated)

	HK$	US$	CNY	Other	Total
Assets					
Cash and balances with banks	11,429,649	4,025,159	5,065,918	5,395,322	25,916,048
Placements with and loans and advances to banks	2,538,482	9,546,847	106,460	1,082,534	13,274,323
Loans and advances to customers	34,246,877	14,607,051	643,465	1,209,407	50,706,800
Financial assets held for trading	–	281,876	328,214	–	610,090
Derivative financial instruments	–	3,267	19,094	39,123	61,484
Investment securities:					
– Available-for-sale	8,321,453	9,751,304	18,127	3,377,815	21,468,699
– Held-to-maturity	2,001,154	765,257	–	–	2,766,411
Total	58,537,615	38,980,761	6,181,278	11,104,201	114,803,855
Liabilities					
Deposits and balances from banks	1,333,143	2,322,593	23,757	458,652	4,138,145
Deposits from customers	45,637,650	33,458,985	5,648,796	10,717,760	95,463,191
Derivative financial instruments	–	4,044	17,688	31,776	53,508
Other liabilities	1,038,476	301,702	973	104,632	1,445,783
Total	48,009,269	36,087,324	5,691,214	11,312,820	101,100,627
Net on-balance sheet position	10,528,346	2,893,437	490,064	(208,619)	13,703,228
Credit commitments	25,880,834	21,958,664	90,654	1,137,256	49,067,408

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.2 Market risk (Continued)

3.2.3 Foreign exchange risk (Continued)

Concentrations of currency risk on- and off-balance sheet financial instruments

The Bank As at 31st December 2011

	HK$	US$	CNY	Other	Total
Assets					
Cash and balances with banks	13,424,539	4,448,597	3,724,976	6,140,968	27,739,080
Placements with and loans and advances to banks	5,206,965	4,813,643	4,260,343	584,525	14,865,476
Loans and advances to customers	35,029,283	17,260,451	1,406,103	1,499,819	55,195,656
Financial assets held for trading	9,108	294,962	140,167	–	444,237
Derivative financial instruments	–	10,084	24,543	35,667	70,294
Investment securities:					
– Available-for-sale	7,942,757	9,879,811	462,101	3,604,030	21,888,699
– Held-to-maturity	–	662,366	–	–	662,366
Total	61,612,652	37,369,914	10,018,233	11,865,009	120,865,808
Liabilities					
Deposits and balances from banks	1,804,531	1,951,544	184,653	391,072	4,331,800
Deposits from customers	50,955,747	31,674,252	8,967,105	11,500,092	103,097,196
Derivative financial instruments	–	8,327	19,245	17,837	45,409
Other liabilities	546,754	341,765	47,176	54,663	990,358
Total	53,307,032	33,975,888	9,218,179	11,963,664	108,464,763
Net on-balance sheet position	8,305,620	3,394,026	800,054	(98,655)	12,401,045
Credit commitments	25,791,725	14,062,491	591,505	952,586	41,398,307

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.2 Market risk (Continued)

3.2.3 Foreign exchange risk (Continued)

Concentrations of currency risk on- and off-balance sheet financial instruments

The Bank As at 31st December 2010 (restated)

	HK$	US$	CNY	Other	Total
Assets					
Cash and balances with banks	11,429,644	4,025,159	5,065,918	5,395,322	25,916,043
Placements with and loans and advances to banks	2,538,482	9,546,847	106,460	1,082,534	13,274,323
Loans and advances to customers	34,246,877	14,607,051	643,465	1,209,407	50,706,800
Financial assets held for trading	–	281,876	328,214	–	610,090
Derivative financial instruments	–	3,267	19,094	39,123	61,484
Investment securities:					
– Available-for-sale	8,107,049	9,747,979	18,127	3,377,815	21,250,970
– Held-to-maturity	–	757,471	–	–	757,471
Total	56,322,052	38,969,650	6,181,278	11,104,201	112,577,181
Liabilities					
Deposits and balances from banks	1,333,143	2,322,593	23,757	458,652	4,138,145
Deposits from customers	45,637,650	33,458,985	5,648,796	10,717,760	95,463,191
Derivative financial instruments	–	4,044	17,688	31,776	53,508
Other liabilities	679,610	301,677	973	106,493	1,088,753
Total	47,650,403	36,087,299	5,691,214	11,314,681	100,743,597
Net on-balance sheet position	8,671,649	2,882,351	490,064	(210,480)	11,833,584
Credit commitments	25,880,834	21,958,664	90,654	1,137,256	49,067,408

3.2.4 Interest rate risk

Interest rate risk is the risk that the Group's position may be adversely affected by a change of market interest rates. The Group's interest rate risk arises primarily from the timing differences in the repricing of interest bearing assets, liabilities and commitments (repricing risk) as well as change of market rates or pricing indices at different time or by different amounts for different financial instruments (basis risk). The primary objective of interest rate risk management is to limit the potential adverse effects of interest rate movement on net interest income by closely monitoring the net repricing gap of the Group's assets and liabilities. The interest rate risk is managed by the Treasury Department and monitored by management and the Asset and Liability Committee under the limits and guidelines laid down in the interest rate risk management policy approved by the Directors.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.2 Market risk (Continued)

3.2.4 Interest rate risk (Continued)

Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. The Group takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest margins may increase as a result of such changes but may reduce losses in the event that unexpected movements arise. The Board sets limits on the level of mismatch of interest rate repricing that may be undertaken, which is monitored daily by management.

The table below summarises the Group's exposure to interest rate risks. It includes the Group's financial instruments at carrying amounts (non-derivatives), categorised by the earlier of contractual re-pricing (for example floating rate notes) or maturity dates.

The Group As at 31st December 2011

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing	Total
Assets							
Cash and balances with banks	16,627,682	–	–	–	–	11,111,410	27,739,092
Placements with and loans and advances to banks	–	8,116,584	6,670,186	–	–	78,706	14,865,476
Loans and advances to customers	44,428,506	5,982,771	4,334,011	327,543	–	122,825	55,195,656
Financial assets held for trading	–	–	121,852	108,351	89,234	124,800	444,237
Derivative financial instruments	–	–	–	–	–	70,294	70,294
Investment securities:							
– Available-for-sale	2,123,088	4,358,408	2,557,096	9,197,140	2,198,831	1,574,097	22,008,660
– Held-to-maturity	116,535	283,236	166,587	1,848,725	339,512	10,188	2,764,783
Investments in jointly controlled entities	–	–	–	–	–	189,308	189,308
Property and equipment	–	–	–	–	–	2,040,164	2,040,164
Investment property	–	–	–	–	–	9,193	9,193
Deferred income tax assets	–	–	–	–	–	44,755	44,755
Other assets	223,160	–	751,382	–	–	631,680	1,606,222
Total assets	63,518,971	18,740,999	14,601,114	11,481,759	2,627,577	16,007,420	126,977,840
Liabilities							
Deposits and balances from banks	3,590,239	710,768	–	–	–	30,793	4,331,800
Deposits from customers	58,478,407	22,446,171	13,117,730	262,164	–	8,792,724	103,097,196
Derivative financial instruments	–	–	–	–	–	45,409	45,409
Other liabilities	330,060	–	–	–	–	878,209	1,208,269
Provisions	–	–	–	–	–	94,691	94,691
Current income tax liabilities	–	–	–	–	–	14,872	14,872
Deferred income tax liabilities	–	–	–	–	–	104,551	104,551
Total liabilities	62,398,706	23,156,939	13,117,730	262,164	–	9,961,249	108,896,788
Total interest repricing gap	1,120,265	(4,415,940)	1,483,384	11,219,595	2,627,577	6,046,171	18,081,052

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.2 Market risk (Continued)

3.2.4 Interest rate risk (Continued)

The Group As at 31st December 2010 (restated)

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing	Total
Assets							
Cash and balances with banks	17,197,098	–	–	–	–	8,718,950	25,916,048
Placements with and loans and advances to banks	–	5,362,755	7,834,054	–	–	77,514	13,274,323
Loans and advances to customers	41,862,384	5,399,929	2,818,713	185,208	–	440,566	50,706,800
Financial assets held for trading	280,629	–	93,626	232,523	–	3,312	610,090
Derivative financial instruments	–	–	–	–	–	61,484	61,484
Investment securities:							
– Available-for-sale	2,129,603	4,217,340	137,152	10,105,641	3,157,181	1,721,782	21,468,699
– Held-to-maturity	122,935	321,883	900,376	1,280,096	128,645	12,476	2,766,411
Investments in jointly controlled entities	–	–	–	–	–	174,473	174,473
Property and equipment	–	–	–	–	–	608,584	608,584
Investment property	–	–	–	–	–	1,382,734	1,382,734
Deferred income tax assets	–	–	–	–	–	56,656	56,656
Other assets	448,176	–	457,382	–	–	709,812	1,615,370
Total assets	62,040,825	15,301,907	12,241,303	11,803,468	3,285,826	13,968,343	118,641,672
Liabilities							
Deposits and balances from banks	2,662,738	1,355,767	83,573	–	–	36,067	4,138,145
Deposits from customers	62,134,580	17,261,429	7,873,864	14,652	–	8,178,666	95,463,191
Derivative financial instruments	–	–	–	–	–	53,508	53,508
Other liabilities	403,020	–	–	–	–	1,068,362	1,471,382
Provisions	–	–	–	–	–	99,654	99,654
Current income tax liabilities	–	–	–	–	–	130,982	130,982
Deferred income tax liabilities	–	–	–	–	–	113,046	113,046
Total liabilities	65,200,338	18,617,196	7,957,437	14,652	–	9,680,285	101,469,908
Total interest repricing gap	(3,159,513)	(3,315,289)	4,283,866	11,788,816	3,285,826	4,288,058	17,171,764

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.2 Market risk (Continued)

3.2.4 Interest rate risk (Continued)

The Bank As at 31st December 2011

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing	Total
Assets							
Cash and balances with banks	16,627,682	–	–	–	–	11,111,398	27,739,080
Placements with and loans and advances to banks	–	8,116,584	6,670,186	–	–	78,706	14,865,476
Loans and advances to customers	44,428,506	5,982,771	4,334,011	327,543	–	122,825	55,195,656
Financial assets held for trading	–	–	121,852	108,351	89,234	124,800	444,237
Derivative financial instruments	–	–	–	–	–	70,294	70,294
Investment securities:							
– Available-for-sale	2,123,088	4,352,408	2,503,844	9,162,844	2,193,831	1,552,684	21,888,699
– Held-to-maturity	116,535	232,972	101,374	207,617	–	3,868	662,366
Investments in jointly controlled entities	–	–	–	–	–	116,000	116,000
Investments in and loans to subsidiaries	–	–	–	–	–	2,086,442	2,086,442
Property and equipment	–	–	–	–	–	1,985,901	1,985,901
Investment properties	–	–	–	–	–	42,620	42,620
Deferred income tax assets	–	–	–	–	–	44,323	44,323
Other assets	223,160	–	751,382	–	–	445,808	1,420,350
Total assets	63,518,971	18,684,735	14,482,649	9,806,355	2,283,065	17,785,669	126,561,444
Liabilities							
Deposits and balances from banks	3,590,239	710,768	–	–	–	30,793	4,331,800
Deposits from customers	58,478,407	22,446,171	13,117,730	262,164	–	8,792,724	103,097,196
Derivative financial instruments	–	–	–	–	–	45,409	45,409
Other liabilities	330,060	–	–	–	–	660,298	990,358
Provisions	–	–	–	–	–	94,320	94,320
Current income tax liabilities	–	–	–	–	–	14,599	14,599
Deferred income tax liabilities	–	–	–	–	–	104,516	104,516
Total liabilities	62,398,706	23,156,939	13,117,730	262,164	–	9,742,659	108,678,198
Total interest repricing gap	1,120,265	(4,472,204)	1,364,919	9,544,191	2,283,065	8,043,010	17,883,246

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.2 Market risk (Continued)

3.2.4 Interest rate risk (Continued)

The Bank As at 31st December 2010 (restated)

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing	Total
Assets							
Cash and balances with banks	17,197,098	–	–	–	–	8,718,945	25,916,043
Placements with and loans and advances to banks	–	5,362,755	7,834,054	–	–	77,514	13,274,323
Loans and advances to customers	41,862,384	5,399,929	2,818,713	185,208	–	440,566	50,706,800
Financial assets held for trading	280,629	–	93,626	232,523	–	3,312	610,090
Derivative financial instruments	–	–	–	–	–	61,484	61,484
Investment securities:							
– Available-for-sale	1,925,556	4,217,340	137,152	10,095,408	3,157,181	1,718,333	21,250,970
– Held-to-maturity	122,935	171,081	249,413	209,772	–	4,270	757,471
Investments in jointly controlled entities	–	–	–	–	–	116,000	116,000
Investments in and loans to subsidiaries	–	–	–	–	–	2,108,934	2,108,934
Property and equipment	–	–	–	–	–	553,543	553,543
Investment properties	–	–	–	–	–	1,416,589	1,416,589
Deferred income tax assets	–	–	–	–	–	56,656	56,656
Other assets	448,176	–	457,382	–	–	344,447	1,250,005
Total assets	61,836,778	15,151,105	11,590,340	10,722,911	3,157,181	15,620,593	118,078,908
Liabilities							
Deposits and balances from banks	2,662,738	1,355,767	83,573	–	–	36,067	4,138,145
Deposits from customers	62,134,580	17,261,429	7,873,864	14,652	–	8,178,666	95,463,191
Derivative financial instruments	–	–	–	–	–	53,508	53,508
Other liabilities	403,020	–	–	–	–	685,733	1,088,753
Provisions	–	–	–	–	–	99,220	99,220
Current income tax liabilities	–	–	–	–	–	130,654	130,654
Deferred income tax liabilities	–	–	–	–	–	112,418	112,418
Total liabilities	65,200,338	18,617,196	7,957,437	14,652	–	9,296,266	101,085,889
Total interest repricing gap	(3,363,560)	(3,466,091)	3,632,903	10,708,259	3,157,181	6,324,327	16,993,019

3.3 Liquidity risk

Liquidity risk is the risk that the Group is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfill commitments to lend. The Group's liquidity risk is managed by the Treasury Department and monitored by management and the Asset and Liability Committee in accordance with the guidelines and procedures laid down in the liquidity management policy approved by the Board of Directors, which has regard to a variety of factors, including liquidity ratio, loan to deposit ratio, liquefiable assets to be kept in Hong Kong, maturity mismatch profile, diversity and stability of the deposit base and ability to borrow in the interbank market. An adequate stock of high quality liquid assets is being maintained at all times, in order to enable the Group to meet deposit withdrawals, to repay interbank borrowings, and to make new loans and investments as and when required in a timely and cost effective manner. Liquefiable assets held comprise mainly marketable debt securities and interbank placements.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.3 Liquidity risk (Continued)

3.3.1 Liquidity risk management process

The Group's liquidity management process, as carried out within the Group and monitored by management, includes:

- Day-to-day funding, managed by monitoring future cash flows to ensure that requirements can be met. This includes replenishment of funds as they mature or are borrowed by customers. The Group maintains an active presence in global money markets to enable this to happen;
- Maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any unforeseen interruption to cash flow;
- Monitoring statement of financial position liquidity ratios against internal and regulatory requirements; and
- Managing the concentration and profile of debt maturities.

Monitoring and reporting take the form of cash flow measurement and projections for the next day, week and month respectively, as these are key periods for liquidity management. The starting point for those projections is an analysis of the contractual maturity of the financial liabilities and the expected collection date of the financial assets (Notes 3.3.4).

Management also monitors unmatched medium-term assets, the level and type of undrawn lending commitments, the usage of overdraft facilities and the impact of contingent liabilities such as standby letters of credit and guarantees.

3.3.2 Maturity analysis

The table below analyses the Group's assets and liabilities into relevant maturity groupings based on the remaining period at the end of the reporting period to the contractual maturity date.

The Group As at 31st December 2011

	Repayable on demand	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Indefinite	Total
Assets								
Cash and balances with banks	13,864,948	13,874,144	–	–	–	–	–	27,739,092
Placements with and loans and advances to banks	–	–	8,152,449	6,713,027	–	–	–	14,865,476
Loans and advances to customers	4,636,291	3,499,484	6,128,219	10,881,141	17,044,174	13,006,347	–	55,195,656
Financial assets held for trading	–	647	1,257	121,869	108,351	89,234	122,879	444,237
Derivative financial instruments	–	11,223	24,532	34,193	346	–	–	70,294
Investment securities:								
– Available-for-sale	–	632,445	401,219	3,144,792	13,578,383	2,688,082	1,563,739	22,008,660
– Held-to-maturity	–	117,614	209,434	249,474	1,848,857	339,404	–	2,764,783
Investments in jointly controlled entities	–	–	–	–	–	–	189,308	189,308
Property and equipment	–	–	–	–	105,888	1,898,763	35,513	2,040,164
Investment property	–	–	–	–	–	9,193	–	9,193
Deferred income tax assets	–	–	–	–	44,755	–	–	44,755
Other assets	267,617	488,462	6,833	41,354	797,837	2,619	1,500	1,606,222
Total assets	18,768,856	18,624,019	14,923,943	21,185,850	33,528,591	18,033,642	1,912,939	126,977,840
Liabilities								
Deposits and balances from banks	303,516	3,200,635	–	–	827,649	–	–	4,331,800
Deposits from customers	37,413,803	29,723,886	22,510,821	13,185,299	263,387	–	–	103,097,196
Derivative financial instruments	–	6,591	14,998	23,767	53	–	–	45,409
Other liabilities	43,888	720,880	78,570	358,035	6,896	–	–	1,208,269
Provisions	–	94,599	–	–	–	92	–	94,691
Current income tax liabilities	–	–	–	14,872	–	–	–	14,872
Deferred income tax liabilities	–	–	–	–	104,551	–	–	104,551
Total liabilities	37,761,207	33,746,591	22,604,389	13,581,973	1,202,536	92	–	108,896,788
Net liquidity gap	(18,992,351)	(15,122,572)	(7,680,446)	7,603,877	32,326,055	18,033,550	1,912,939	18,081,052

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.3 Liquidity risk (Continued)

3.3.2 Maturity analysis (Continued)

The Group As at 31st December 2010 (restated)

	Repayable on demand	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Indefinite	Total
Assets								
Cash and balances with banks	13,886,441	12,029,607	–	–	–	–	–	25,916,048
Placements with and loans and advances to banks	–	–	5,546,420	7,727,903	–	–	–	13,274,323
Loans and advances to customers	3,884,907	2,576,290	4,116,288	9,335,073	16,723,623	14,070,619	–	50,706,800
Financial assets held for trading	–	621	2,131	94,186	320,359	77,572	115,221	610,090
Derivative financial instruments	–	10,391	23,336	26,403	1,354	–	–	61,484
Investment securities:								
– Available-for-sale	–	357,077	536,865	1,036,483	13,888,190	3,971,316	1,678,768	21,468,699
– Held-to-maturity	–	56,044	154,381	751,786	1,804,200	–	–	2,766,411
Investments in jointly controlled entities	–	–	–	–	–	–	174,473	174,473
Property and equipment	–	–	–	–	78,030	495,023	35,531	608,584
Investment property	–	–	–	–	–	1,382,734	–	1,382,734
Deferred income tax assets	–	–	–	–	56,656	–	–	56,656
Other assets	157,130	863,156	6,185	64,740	520,040	2,619	1,500	1,615,370
Total assets	17,928,478	15,893,186	10,385,606	19,036,574	33,392,452	19,999,883	2,005,493	118,641,672
Liabilities								
Deposits and balances from banks	673,054	2,025,047	170,364	1,269,680	–	–	–	4,138,145
Deposits from customers	40,060,203	30,202,433	17,285,630	7,900,255	14,670	–	–	95,463,191
Derivative financial instruments	–	7,887	20,886	23,901	834	–	–	53,508
Other liabilities	38,268	1,047,778	70,673	310,858	3,805	–	–	1,471,382
Provisions	–	107	99,480	–	–	67	–	99,654
Current income tax liabilities	–	–	–	130,982	–	–	–	130,982
Deferred income tax liabilities	–	–	–	–	113,046	–	–	113,046
Total liabilities	40,771,525	33,283,252	17,647,033	9,635,676	132,355	67	–	101,469,908
Net liquidity gap	(22,843,047)	(17,390,066)	(7,261,427)	9,400,898	33,260,097	19,999,816	2,005,493	17,171,764

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.3 Liquidity risk (Continued)

3.3.2 Maturity analysis (Continued)

The Bank As at 31st December 2011

	Repayable on demand	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Indefinite	Total
Assets								
Cash and balances with banks	13,864,936	13,874,144	–	–	–	–	–	27,739,080
Placements with and loans and advances to banks	–	–	8,152,449	6,713,027	–	–	–	14,865,476
Loans and advances to customers	4,636,291	3,499,484	6,128,219	10,881,141	17,044,174	13,006,347	–	55,195,656
Financial assets held for trading	–	647	1,257	121,869	108,351	89,234	122,879	444,237
Derivative financial instruments	–	11,223	24,532	34,193	346	–	–	70,294
Investment securities:								
– Available-for-sale	–	632,445	394,456	3,090,956	13,543,788	2,683,082	1,543,972	21,888,699
– Held-to-maturity	–	117,614	157,243	179,896	207,613	–	–	662,366
Investments in jointly controlled entities	–	–	–	–	–	–	116,000	116,000
Investments in and loans to/ (deposit from) subsidiaries (net)	(1,101,521)	(48,527)	70,503	965,411	1,664,772	342,616	193,188	2,086,442
Property and equipment	–	–	–	–	112,386	1,854,480	19,035	1,985,901
Investment properties	–	–	–	–	–	42,620	–	42,620
Deferred income tax assets	–	–	–	–	44,323	–	–	44,323
Other assets	267,617	309,894	6,229	38,372	798,238	–	–	1,420,350
Total assets	17,667,323	18,396,924	14,934,888	22,024,865	33,523,991	18,018,379	1,995,074	126,561,444
Liabilities								
Deposits and balances from banks	303,516	3,200,635	–	–	827,649	–	–	4,331,800
Deposits from customers	37,413,803	29,723,886	22,510,821	13,185,299	263,387	–	–	103,097,196
Derivative financial instruments	–	6,591	14,998	23,767	53	–	–	45,409
Other liabilities	43,888	554,720	75,641	316,109	–	–	–	990,358
Provisions	–	94,320	–	–	–	–	–	94,320
Current income tax liabilities	–	–	–	14,599	–	–	–	14,599
Deferred income tax liabilities	–	–	–	–	104,516	–	–	104,516
Total liabilities	37,761,207	33,580,152	22,601,460	13,539,774	1,195,605	–	–	108,678,198
Net liquidity gap	(20,093,884)	(15,183,228)	(7,666,572)	8,485,091	32,328,386	18,018,379	1,995,074	17,883,246

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.3 Liquidity risk (Continued)

3.3.2 Maturity analysis (Continued)

The Bank As at 31st December 2010 (restated)

	Repayable on demand	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Indefinite	Total
Assets								
Cash and balances with banks	13,886,436	12,029,607	–	–	–	–	–	25,916,043
Placements with and loans and advances to banks	–	–	5,546,420	7,727,903	–	–	–	13,274,323
Loans and advances to customers	3,884,907	2,576,290	4,116,288	9,335,073	16,723,623	14,070,619	–	50,706,800
Financial assets held for trading	–	621	2,131	94,186	320,359	77,572	115,221	610,090
Derivative financial instruments	–	10,391	23,336	26,403	1,354	–	–	61,484
Investment securities:								
– Available-for-sale	–	354,287	422,339	1,030,578	13,812,797	3,971,316	1,659,653	21,250,970
– Held-to-maturity	–	56,044	2,155	94,391	604,881	–	–	757,471
Investments in jointly controlled entities	–	–	–	–	–	–	116,000	116,000
Investments in and loans to/ (deposit from) subsidiaries (net)	(1,004,855)	(54,271)	964,664	677,214	1,317,364	15,619	193,199	2,108,934
Property and equipment	–	–	–	–	84,728	449,763	19,052	553,543
Investment properties	–	–	–	–	-	1,416,589	–	1,416,589
Deferred income tax assets	–	–	–	–	56,656	–	–	56,656
Other assets	157,130	505,891	5,570	61,407	520,007	–	–	1,250,005
Total assets	16,923,618	15,478,860	11,082,903	19,047,155	33,441,769	20,001,478	2,103,125	118,078,908
Liabilities								
Deposits and balances from banks	673,054	2,025,047	170,364	1,269,680	–	–	–	4,138,145
Deposits from customers	40,060,203	30,202,433	17,285,630	7,900,255	14,670	–	–	95,463,191
Derivative financial instruments	–	7,887	20,886	23,901	834	–	–	53,508
Other liabilities	38,268	678,561	68,234	303,690	–	–	–	1,088,753
Provisions	–	107	99,113	–	–	–	–	99,220
Current income tax liabilities	–	–	–	130,654	–	–	–	130,654
Deferred income tax liabilities	–	–	–	–	112,418	–	–	112,418
Total liabilities	40,771,525	32,914,035	17,644,227	9,628,180	127,922	–	–	101,085,889
Net liquidity gap	(23,847,907)	(17,435,175)	(6,561,324)	9,418,975	33,313,847	20,001,478	2,103,125	16,993,019

3.3.3 Funding approach

Sources of liquidity are regularly reviewed by management to maintain a wide diversification by currency, geography, provider, product and term.

3.3.4 Non-derivative financial liabilities and assets held for managing liquidity risk

The table below presents the cash flows payable by the Group under non-derivative financial liabilities and assets held for managing liquidity risk by remaining contractual maturities at the end of the reporting period. The amounts disclosed in the table are the contractual undiscounted cash flow, whereas the Group manages the liquidity risk based on a different basis, not resulting in a significantly different analysis.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.3 Liquidity risk (Continued)

3.3.4 Non-derivative financial liabilities and assets held for managing liquidity risk (Continued)

The Group As at 31st December 2011

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Liabilities						
Deposits and balances from banks	3,504,704	1,994	21,454	827,306	–	4,355,458
Deposits from customers	67,170,839	22,568,956	13,279,732	287,165	–	103,306,692
Other liabilities	730,840	61,023	279,078	6,896	–	1,077,837
Total (contractual maturity)	71,406,383	22,631,973	13,580,264	1,121,367	–	108,739,987
Assets held for managing liquidity risk (contractual maturity)	37,464,399	15,154,848	22,291,250	38,042,702	24,982,040	137,935,239

The Group As at 31st December 2010

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Liabilities						
Deposits and balances from banks	2,698,678	171,265	1,274,171	–	–	4,144,114
Deposits from customers	70,283,293	17,311,197	7,929,560	15,783	–	95,539,833
Other liabilities	1,086,046	70,673	314,663	–	–	1,471,382
Total (contractual maturity)	74,068,017	17,553,135	9,518,394	15,783	–	101,155,329
Assets held for managing liquidity risk (contractual maturity)	33,930,560	10,587,347	20,058,936	37,523,392	26,968,952	129,069,187

The Bank As at 31st December 2011

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Liabilities						
Deposits and balances from banks	3,504,704	1,994	21,454	827,306	–	4,355,458
Deposits from customers	67,170,839	22,568,956	13,279,732	287,165	–	103,306,692
Other liabilities	566,146	61,023	250,332	–	–	877,501
Total (contractual maturity)	71,241,689	22,631,973	13,551,518	1,114,471	–	108,539,651
Assets held for managing liquidity risk (contractual maturity)	36,135,531	15,161,476	23,090,180	37,939,231	25,038,543	137,364,961

The Bank As at 31st December 2010

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Liabilities						
Deposits and balances from banks	2,698,678	171,265	1,274,171	–	–	4,144,114
Deposits from customers	70,283,293	17,311,197	7,929,560	15,783	–	95,539,833
Other liabilities	716,829	68,234	303,690	–	–	1,088,753
Total (contractual maturity)	73,698,800	17,550,696	9,507,421	15,783	–	100,772,700
Assets held for managing liquidity risk (contractual maturity)	32,510,502	11,277,798	20,019,689	37,494,801	27,059,775	128,362,565

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.3 Liquidity risk (Continued)

3.3.4 Non-derivative financial liabilities and assets held for managing liquidity risk (Continued)

Assets available to meet all of the liabilities and to cover outstanding loan commitments include cash, central bank balances, items in the course of collection and treasury bills; loans and advances to banks; and loans and advances to customers. In addition, debt securities and treasury bills have been pledged to secure liabilities. The Group would also be able to meet unexpected net cash outflows by selling securities and accessing additional funding sources such as asset-backed markets.

3.3.5 Derivative liabilities

(a) Derivatives settled on a net basis

There is no derivatives that will be settled on a net basis as at 31st December 2011 and 2010.

(b) Derivatives settled on a gross basis

The Group's derivatives that will be settled on a gross basis include foreign exchange derivatives: currency forward exchange contracts.

The table below analyses the Group's derivative financial instruments that will be settled on a gross basis into relevant maturity groupings based on the remaining period at the end of the reporting period to the contractual maturity date. Contractual maturities are assessed to be essential for an understanding of the timing of the cashflows on all derivatives. Some of the Group's derivatives are subject to collateral requirements. Cash flows for those derivatives could occur earlier than the contractual maturity. The amounts disclosed in the table are the contractual undiscounted cash flows.

The Group and the Bank As at 31st December 2011

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Derivatives held for trading:						
Foreign exchange derivatives						
– Outflow	2,391,016	2,993,356	8,362,923	35,269	–	13,782,564
– Inflow	(2,395,896)	(3,003,550)	(8,374,607)	(35,577)	–	(13,809,630)

The Group and the Bank As at 31st December 2010

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Derivatives held for trading:						
Foreign exchange derivatives						
– Outflow	1,009,280	574,787	3,445,046	94,835	–	5,123,948
– Inflow	(1,011,895)	(578,325)	(3,450,693)	(93,747)	–	(5,134,660)

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.3 Liquidity risk (Continued)

3.3.6 Off-balance sheet items

(a) Loan and other commitments

The dates of the contractual amounts of the Group's off-balance sheet financial instruments (Note 35(c)) that commit it to extend credit to customers and other facilities, are summarised in the table below.

(b) Acceptances and other financial facilities

Acceptances and other financial facilities, are also included below based on the conditions existing at the reporting date as to what contractual payments are required.

(c) Operating lease commitments

Where a group company is the lessee, the future minimum lease payments under non-cancellable operating leases, as disclosed in Note 35(b), are summarised in the table below.

(d) Capital commitments

Capital commitments for the acquisition of equipment (Note 35(a)) are summarised in the table below.

The Group As at 31st December 2011

	No later than 1 year	1-5 years	Over 5 years	Total
Loan and other commitments	32,813,516	2,839,836	8,408	35,661,760
Guarantees, acceptances and other financial facilities				
– Acceptances	830,599	–	–	830,599
– Guarantees and standby letters of credit	2,098,367	234,285	7,348	2,340,000
– Documentary and commercial letters of credit	2,565,948	–	–	2,565,948
Operating lease commitments	88,621	190,075	70	278,766
Capital commitments	120,243	–	–	120,243
Total	38,517,294	3,264,196	15,826	41,797,316

The Group As at 31st December 2010

	No later than 1 year	1-5 years	Over 5 years	Total
Loan and other commitments	42,031,753	1,856,822	21,441	43,910,016
Guarantees, acceptances and other financial facilities				
– Acceptances	584,352	–	–	584,352
– Guarantees and standby letters of credit	1,988,782	190,530	7,590	2,186,902
– Documentary and commercial letters of credit	2,386,138	–	–	2,386,138
Operating lease commitments	86,544	206,375	32,251	325,170
Capital commitments	133,126	10,600	–	143,726
Total	47,210,695	2,264,327	61,282	49,536,304

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.3 Liquidity risk (Continued)

3.3.6 Off-balance sheet items (Continued)

(d) Capital commitments (Continued)

The Bank As at 31st December 2011

	No later than 1 year	1-5 years	Over 5 years	Total
Loan and other commitments	32,813,516	2,839,836	8,408	35,661,760
Guarantees, acceptances and other financial facilities				
– Acceptances	830,599	–	–	830,599
– Guarantees and standby letters of credit	2,098,367	234,285	7,348	2,340,000
– Documentary and commercial letters of credit	2,565,948	–	–	2,565,948
Operating lease commitments	89,818	190,075	70	279,963
Capital commitments	122,939	–	–	122,939
Total	38,521,187	3,264,196	15,826	41,801,209

The Bank As at 31st December 2010

	No later than 1 year	1-5 years	Over 5 years	Total
Loan and other commitments	42,031,753	1,856,822	21,441	43,910,016
Guarantees, acceptances and other financial facilities				
– Acceptances	584,352	–	–	584,352
– Guarantees and standby letters of credit	1,988,782	190,530	7,590	2,186,902
– Documentary and commercial letters of credit	2,386,138	–	–	2,386,138
Operating lease commitments	88,346	207,576	32,251	328,173
Capital commitments	136,400	10,600	–	147,000
Total	47,215,771	2,265,528	61,282	49,542,581

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.4 Fair value of financial assets and liabilities

(a) Financial instruments not measured at fair value

The table below summarises the carrying amounts and fair values of those financial assets and liabilities not presented on the Group's statement of financial position at their fair value.

The Group

	Carrying value		Fair value	
	2011	2010 (restated)	2011	2010 (restated)
Financial assets				
Balances with banks	27,322,826	24,928,722	27,322,826	24,928,722
Placements with and loans and advances to banks	14,865,476	13,274,323	14,865,476	13,274,323
Loans and advances to customers:				
Loans to individuals:				
– Overdrafts	533,500	420,292	533,500	420,292
– Credit cards	338,764	311,244	338,764	311,244
– Term loans and others	5,573,480	5,118,101	5,573,480	5,118,101
– Mortgages	6,912,793	6,764,114	6,912,793	6,764,114
Loans to corporate entities:				
– Large corporate customers and others	35,397,648	31,332,954	35,397,648	31,332,954
– SMEs	6,439,471	6,760,095	6,439,471	6,760,095
Investment securities – Held-to-maturity	2,764,783	2,766,411	2,800,071	2,798,071
Financial liabilities				
Deposits and balances from banks	4,331,800	4,138,145	4,331,800	4,138,145
Deposits from customers	103,097,196	95,463,191	103,097,196	95,463,191

The Bank

	Carrying value		Fair value	
	2011	2010 (restated)	2011	2010 (restated)
Financial assets				
Balances with banks	27,322,826	24,928,722	27,322,826	24,928,722
Placements with and loans and advances to banks	14,865,476	13,274,323	14,865,476	13,274,323
Loans and advances to customers:				
Loans to individuals:				
– Overdrafts	533,500	420,292	533,500	420,292
– Credit cards	338,764	311,244	338,764	311,244
– Term loans and others	5,573,480	5,118,101	5,573,480	5,118,101
– Mortgages	6,912,793	6,764,114	6,912,793	6,764,114
Loans to corporate entities:				
– Large corporate customers and others	35,397,648	31,332,954	35,397,648	31,332,954
– SMEs	6,439,471	6,760,095	6,439,471	6,760,095
Investment securities – Held-to-maturity	662,366	757,471	658,316	758,624
Financial liabilities				
Deposits and balances from banks	4,331,800	4,138,145	4,331,800	4,138,145
Deposits from customers	103,097,196	95,463,191	103,097,196	95,463,191

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.4 Fair value of financial assets and liabilities (Continued)

(a) Financial instruments not measured at fair value (Continued)

(i) Placements with and loans and advances to banks

Placement with and loans and advances to banks includes inter-bank placements. The fair value of floating rate placements and overnight deposits is their carrying amount. The estimated fair value of fixed interest bearing deposits is based on discounted cash flows using prevailing money-market interest rates for debts with similar credit risk and remaining maturity.

(ii) Loans and advances to customers

Loans and advances are net of provisions for impairment. The estimated fair value of loans and advances represents the discounted amount of estimated future cash flows expected to be received. Expected cash flows are discounted at current market rates to determine fair value.

(iii) Investment securities

The fair value for held-to-maturity assets is based on market prices or broker/dealer price quotations. Where this information is not available, fair value is estimated using quoted market prices for securities with similar credit, maturity and yield characteristics.

(iv) Deposits and balances from banks and deposits from customers

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand. Hence, the carrying amount at statement of financial position approximates their fair value.

The estimated fair value of fixed interest-bearing deposits and other borrowings not quoted in an active market is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

(b) Fair value hierarchy

HKFRS 7 specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect the Group's market assumptions. These two types of inputs have created the following fair value hierarchy:

– Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes listed equity securities and debt instruments on exchanges (for example, Hong Kong Stock Exchange, London Stock Exchange, Frankfurt Stock Exchange, New York Stock Exchange) and exchanges traded derivatives like futures (for example, Nasdaq, S&P 500).

– Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices). This level includes the majority of the OTC derivative contracts, traded loans and issued structured debt. The sources of input parameters like HIBOR and LIBOR yield curve or counterparty credit risk are Bloomberg and Reuters.

– Level 3 – Inputs for the asset or liability that are not based on observable market data (unobservable inputs). This level includes equity investments and debt instruments with significant unobservable components.

This hierarchy requires the use of observable market data when available. The Group considers relevant and observable market prices in its valuations where possible.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.4 Fair value of financial assets and liabilities (Continued)

(b) Fair value hierarchy (Continued)

Assets and liabilities measured at fair value:

The Group As at 31st December 2011

	Level 1	Level 2	Level 3	Total
Description				
Financial assets at fair value through profit and loss				
Financial assets held for trading				
Debt securities	181,191	140,167	–	321,358
Equity securities	116,452	–	–	116,452
Others	6,427	–	–	6,427
Derivative financial instruments				
Currency forward exchange contracts	–	70,294	–	70,294
Available-for-sale investments				
Investment securities – debt	8,765,631	11,679,290	2,754	20,447,675
Investment securities – equity	98,259	–	1,462,726	1,560,985
Total Assets	9,167,960	11,889,751	1,465,480	22,523,191
Financial liabilities at fair value through profit and loss				
Derivative financial instruments				
Currency forward exchange contracts	–	45,409	–	45,409
Total Liabilities	–	45,409	–	45,409

The Group As at 31st December 2010

	Level 1	Level 2	Level 3	Total
Description				
Financial assets at fair value through profit and loss				
Financial assets held for trading				
Debt securities	166,655	328,214	–	494,869
Equity securities	115,221	–	–	115,221
Derivative financial instruments				
Currency forward exchange contracts	–	60,468	–	60,468
Cross-currency interest rate swaps contracts	–	1,016	–	1,016
Available-for-sale investments				
Investment securities – debt	7,806,443	11,983,489	2,754	19,792,686
Investment securities – equity	195,460	–	1,480,553	1,676,013
Total Assets	8,283,779	12,373,187	1,483,307	22,140,273
Financial liabilities at fair value through profit and loss				
Derivative financial instruments				
Currency forward exchange contracts	–	52,473	–	52,473
Cross-currency interest rate swaps contracts	–	1,035	–	1,035
Total Liabilities	–	53,508	–	53,508

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.4 Fair value of financial assets and liabilities (Continued)

(b) Fair value hierarchy (Continued)

The Bank As at 31st December 2011	Level 1	Level 2	Level 3	Total
Description				
Financial assets at fair value through profit and loss				
Financial assets held for trading				
Debt securities	181,191	140,167	–	321,358
Equity securities	116,452	–	–	116,452
Others	6,427	–	–	6,427
Derivative financial instruments				
Currency forward exchange contracts	–	70,294	–	70,294
Available-for-sale investments				
Investment securities – debt	8,762,446	11,582,281	2,754	20,347,481
Investment securities – equity	78,492	–	1,462,726	1,541,218
Total Assets	9,145,008	11,792,742	1,465,480	22,403,230
Financial liabilities at fair value through profit and loss				
Derivative financial instruments				
Currency forward exchange contracts	–	45,409	–	45,409
Total Liabilities	–	45,409	–	45,409

The Bank As at 31st December 2010	Level 1	Level 2	Level 3	Total
Description				
Financial assets at fair value through profit and loss				
Financial assets held for trading				
Debt securities	166,655	328,214	–	494,869
Equity securities	115,221	–	–	115,221
Derivative financial instruments				
Currency forward exchange contracts	–	60,468	–	60,468
Cross-currency interest rate swaps contracts	–	1,016	–	1,016
Available-for-sale investments				
Investment securities – debt	7,803,098	11,788,220	2,754	19,594,072
Investment securities – equity	176,345	–	1,480,553	1,656,898
Total Assets	8,261,319	12,177,918	1,483,307	21,922,544
Financial liabilities at fair value through profit and loss				
Derivative financial instruments				
Currency forward exchange contracts	–	52,473	–	52,473
Cross-currency interest rate swaps contracts	–	1,035	–	1,035
Total Liabilities	–	53,508	–	53,508

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.4 Fair value of financial assets and liabilities (Continued)

(b) Fair value hierarchy (Continued)

There were no significant transfers of financial assets between level 1 and level 2 fair value hierarchy classifications.

The following table presents the changes in level 3 instruments for the year ended 31st December 2010 and 31st December 2011 respectively.

The Group and the Bank

	Available-for-sale investments		Total assets
	Investment securities – equity	Investment securities – debt	
At 1st January 2010	1,371,583	2,754	1,374,337
Total gains			
– Profit or loss	3,139	–	3,139
– Other comprehensive income	80,273	–	80,273
Purchases	551,477	–	551,477
Settlements	(529,427)	–	(529,427)
Exchange differences	3,508	–	3,508
At 31st December 2010	1,480,553	2,754	1,483,307
Total gains for the year included in income statement for assets held at 31st December 2010	–	–	–
At 1st January 2011	**1,480,553**	**2,754**	**1,483,307**
Total gains			
– Profit or loss	**1,454**	**–**	**1,454**
– Other comprehensive income	**38,817**	**–**	**38,817**
Purchases	**269,423**	**–**	**269,423**
Settlements	**(326,155)**	**–**	**(326,155)**
Exchange differences	**(1,366)**	**–**	**(1,366)**
At 31st December 2011	**1,462,726**	**2,754**	**1,465,480**
Total gains for the year included in income statement for assets held at 31st December 2011	**–**	**–**	**–**

Total gains or losses for the year included in profit or loss as well as total gains or losses relating to assets/ liabilities held at the end of the reporting period are presented in 'Net gain from disposal/ redemption of available-for-sale investments' and 'Interest income'.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.5 Capital management

The Group's policy is to maintain a strong capital base to support the development of the Group's business and to ensure compliance with the statutory capital adequacy ratio requirement, a requirement used to assess the capital adequacy of banks. Capital is allocated to the various activities of the Group depending on the risk taken by each business division. Where the subsidiaries or branches are directly regulated by other regulators, they are required to maintain capital according to the rules of those regulators.

The Group's objectives when managing capital, which is a broader concept than the 'equity' on the face of statement of financial position, are:

– To comply with the capital requirements under the Banking (Capital) Rules of the Banking Ordinance;

– To safeguard the Group's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders;

– To support the Group's stability and growth;

– To allocate capital in an efficient and risk based approach to optimise risk adjusted return to the shareholders; and

– To maintain a strong capital base to support the development of its business.

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

The HKMA requires each bank or banking group to maintain a ratio of total regulatory capital to the risk-weighted asset (the capital adequacy ratio) at or above the minimum of 8%. In addition, those individual banking subsidiaries or similar financial institutions not incorporated in Hong Kong are also directly regulated and supervised by their local banking supervisors, which may differ from country to country. Subsidiaries of the Group are also subject to statutory capital requirements from other regulatory authorities, such as the Securities and Futures Commission.

The regulatory capital requirements are strictly observed when managing economic capital. The Group's regulatory capital is managed by its central Group Treasury and comprises two tiers:

– Core capital: share capital, general reserve, statutory reserve, non-controlling interests arising on consolidation from interests in permanent shareholders' equity, retained earnings and reserves created by appropriations of retained earnings; and

– Supplementary capital: qualifying collective impairment allowances and unrealised gains arising on the fair valuation of equity instruments held as available-for-sale.

The table below summarises the ratios and the composition of regulatory capital of the Group for the years ended 31st December. During those two years, the individual entities within the Group and the Group complied with all of the externally imposed capital requirements by the HKMA.

	2011	2010
Capital adequacy ratio	18%	19%
Core capital ratio	18%	19%

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.5 Capital management (Continued)

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

The Group		
	2011	2010
Core capital:		
Paid up ordinary share capital	2,000,000	2,000,000
Reserves	12,096,361	11,354,793
Income statement	1,777,148	1,677,177
Less: net deferred tax assets	(74,990)	(89,422)
	15,798,519	14,942,548
Other deductions from core capital	(902,705)	(917,656)
Core capital after deductions	14,895,814	14,024,892
Supplementary capital:		
Collective impairment allowances for loans and advances	214,859	216,622
Regulatory reserve	462,370	362,370
Revaluation reserves for available-for-sale investments	368,816	396,364
	1,046,045	975,356
Other deductions from supplementary capital	(902,705)	(917,656)
Supplementary capital after deductions	143,340	57,700
Total capital base	15,039,154	14,082,592
Risk-weighted assets:		
Credit risk	75,819,963	68,527,493
Market risk	1,257,200	976,650
Operational risk	5,258,800	5,218,950
Total risk-weighted assets	82,335,963	74,723,093
Which consist of:		
On-balance sheet	77,896,965	70,872,914
Off-balance sheet	4,438,998	3,850,179

3.6 Operational risk management

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. It is inherent in all material products, activities, processes and systems. The Operational Risk Management Committee oversees the Group's operational risk to ensure the operations are in accordance with the controls and procedures laid down in the operational risk management policy approved by the Directors. The Risk Management Department is responsible for the central operational risk management function. Policies and procedures have been established to control exposures to identified operational risk factors. Insurance policies are taken to mitigate unforeseeable operational risks. A Business Continuity Plan is established to ensure the Group's ability to operate on an ongoing basis and limit losses in the event of severe business disruption, particularly where the Group's physical, telecommunication, or information technology infrastructures have been damaged or made inaccessible.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS IN APPLYING ACCOUNTING POLICIES

4.1 Critical accounting estimates and assumptions

The Group's financial statements and its financial result are influenced by accounting policies, assumptions, estimates, and management judgement which necessarily have to be made in the course of preparation of the consolidated financial statements.

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events.

Accounting policies and management's judgements for certain items are especially critical for the Group's results and financial situation due to their materiality in amount.

(i) Impairment allowances on loans and advances

The Group reviews its loan portfolios to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the income statement, the Group makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

(ii) Impairment of available-for-sale investments

The Group follows the guidance of HKAS 39 to determine when available-for-sale investments are impaired. This determination requires judgement. In making this judgement, the Group evaluates among other factors, the duration and extent to which the fair value of an investment is less than its cost; and the financial health of and near-term business outlook for the investee, including factors such as industry and sector performance, changes in technology and operational and financing cash flows.

(iii) Held-to-maturity investments

The Group follows the guidance of HKAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires significant judgment. In making this judgment, the Group evaluates its intention and ability to hold such investments to maturity. If the Group fails to keep these investments to maturity other than for the specific circumstances - for example, selling an insignificant amount close to maturity - it will be required to reclassify the entire class as available-for-sale investments. The investments would therefore be measured at fair value not amortised cost.

(iv) Income taxes

The Group is subject to income taxes in numerous jurisdictions. Significant judgment is required in determining the worldwide provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current and deferred income tax and deferred tax assets and liabilities in the period in which such determination is made.

(v) Retirement benefits

The present value of the retirement benefit obligations depends on a number of factors that are determined on an actuarial basis using a number of assumptions. Any changes in these assumptions will impact the carrying amount of pension obligations. The assumptions used in determining the net cost (income) for pensions include the discount rate. The Group determines the appropriate discount rate at the end of each year. This is the interest rate that should be used to determine the present value of estimated future cash outflows expected to be required to settled the pension obligations. In determining the appropriate discount rate, the Group considers the interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid and that have terms to maturity approximating the terms of the related pension liability. Other key assumptions for pension obligations are based in part on current market conditions.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS IN APPLYING ACCOUNTING POLICIE (CONTINUED)

4.1 Critical accounting estimates and assumptions (Continued)

(vi) Amount recoverable from the Lehman Brothers minibonds

On 22nd July 2009, the Group and other distributing banks agreed with the Securities and Futures Commission and the Hong Kong Monetary Authority to make an offer to eligible customers to repurchase their holdings in all outstanding Minibonds subscribed through the Group ('the Repurchase Scheme'). The Group's charge to the 2009 income statement in respect of the Lehman Brothers minibonds ('Minibonds') took into account the aggregate amount paid under the Repurchase Scheme and the recoverable amount from the Minibonds.

During the year, HK$146 million was recovered from the realisation of collateral of Minibonds. Further recovery from the Minibonds is uncertain and dependent on a number of factors including outcomes of certain legal matters. Given the existence of these uncertainties, the amount to be recovered by the Group for the remaining Minibonds may be higher than that carrying amount in the consolidated financial statements.

4.2 Critical judgements in applying the Group's accounting policies

Distinction between investment properties and owner-occupied properties

The Group determines whether a property qualifies as investment property. In making its judgment, the Group considers whether the property generates cash flows largely independently of the other assets held by an entity. Owner-occupied properties generate cash flows that are attributable not only to property but also to other assets used in the production or supply process.

Some properties comprise a portion that is held to earn rentals or for capital appreciation and another portion that is held for use in the production or supply of goods or services or for administrative purposes. If these portions can be sold separately (or leased out separately under a finance lease), the Group accounts for the portions separately. If the portions cannot be sold separately, the property is accounted for as investment property only if an insignificant portion is held for use in the production or supply of goods or services or for administrative purposes. Judgment is applied in determining whether ancillary services are so significant that a property does not qualify as investment property. The Group considers each property separately in making its judgment.

5 BUSINESS ACTIVITIES ANALYSIS

(a) By business activities

The Group is engaged predominantly in banking and related financial activities. It comprises retail and corporate banking, bills, treasury and other classes of business.

Retail banking - incorporating private banking services, private customer current accounts, savings, deposits, investment savings products, custody, credit and debit cards, consumer loans and mortgages; and

Corporate banking - incorporating direct debit facilities, current accounts, deposits, overdrafts, loans and other credit facilities.

Bills - incorporating import services, export services, invoice financing and invoice discounting.

Treasury - responsible for managing the capital, liquidity, and the interest rate and foreign exchange positions of the Group.

The 'Others' business mainly comprises remittance, share dealing, provision of trustee, wealth management and insurance agency services.

For the purpose of class of business analysis, the allocation of revenue, besides the direct revenue generated by the business, also includes the benefits of funding resources derived from the other businesses by way of internal fund transfer pricing mechanisms. Cost allocation is based on the direct cost incurred by the class of business and internal allocation of management overheads. Asset allocation is based on the assets directly attributable to the class of business and internal allocation of assets.

5 BUSINESS ACTIVITIES ANALYSIS (CONTINUED)

(a) By business activities (Continued)

The Group 2011

	Retail and corporate banking	Bills	Treasury	Others	Total
Net interest income	1,310,701	87,704	583,554	–	1,981,959
Net fee and commission income	128,785	128,558	306	396,971	654,620
Net trading income	–	–	112,247	–	112,247
Disposal/ fair value gain on other investments	–	–	155,824	–	155,824
Profit before income tax	895,617	148,781	753,468	393,085	2,190,951
Operating assets	51,387,132	6,481,163	68,335,930	773,615	126,977,840
Reversal of impairment losses on loans and advances to customers	(12,315)	(7,590)	–	–	(19,905)

The Group 2010

	Retail and corporate banking	Bills	Treasury	Others	Total
Net interest income (restated)	1,255,325	81,323	556,789	–	1,893,437
Net fee and commission income	118,244	130,469	–	431,559	680,272
Net trading income	–	–	180,887	–	180,887
Disposal/ fair value gain on other investments	–	–	260,075	–	260,075
Profit before income tax	815,349	157,658	826,533	238,349	2,037,889
Operating assets	47,987,674	4,777,504	64,305,687	1,570,807	118,641,672
Charge/ (reversal) for impairment losses on loans and advances to customers	92,719	(8,411)	–	–	84,308

(b) By geographical activities

The Group 2011

	Total assets	Total liabilities	Contingent liabilities and commitments	Total operating income	Profit before income tax	Capital expenditure
Hong Kong & PRC	114,724,763	101,561,873	38,778,688	2,680,054	1,907,341	117,686
Europe	2,613,085	2,746,216	74,854	27,060	9,776	62
America	9,639,992	4,588,699	2,544,765	331,501	273,834	434
Total	126,977,840	108,896,788	41,398,307	3,038,615	2,190,951	118,182

The Group 2010

	Total assets	Total liabilities	Contingent liabilities and commitments	Total operating income	Profit before income tax	Capital expenditure
Hong Kong & PRC	106,985,923	94,261,333	47,277,247	2,816,732	1,888,357	18,308
Europe	2,292,395	2,695,754	56,875	20,834	5,761	176
America	9,363,354	4,512,821	1,733,286	306,513	143,771	262
Total	118,641,672	101,469,908	49,067,408	3,144,079	2,037,889	18,746

6 NET INTEREST INCOME

Interest income

	The Group		The Bank	
	2011	2010 (restated)	2011	2010 (restated)
Cash and balances with banks	563,730	426,321	563,730	426,321
Investment securities				
– Available-for-sale	578,337	550,956	575,252	541,030
– Held-to-maturity	56,037	66,972	12,717	13,477
Loans and advances				
– To customers	1,495,108	1,304,861	1,495,436	1,305,176
Others	9,345	7,949	9,345	7,949
	2,702,557	2,357,059	2,656,480	2,293,953

Interest expense

	The Group		The Bank	
	2011	2010	2011	2010
Deposits and balances from banks	20,110	21,869	20,110	21,869
Deposits from customers	696,810	438,675	696,913	438,731
Others	3,678	3,078	3,678	3,078
	720,598	463,622	720,701	463,678

Included within interest income

	The Group		The Bank	
	2011	2010	2011	2010
Interest income on listed investments	314,087	303,678	270,641	249,923
Interest income on unlisted investments	320,287	314,250	317,328	304,584
Interest income accrued on impaired financial assets	9,072	7,452	9,072	7,452

7 NET FEE AND COMMISSION INCOME

Fee and commission income

	The Group		The Bank	
	2011	2010	2011	2010
Commissions from bills	122,428	124,174	122,428	124,174
Nominees, custodian and securities brokerage commissions	237,180	277,511	211,313	246,482
Commissions from wealth management products	75,923	78,620	75,923	78,620
Commissions from remittance	51,730	52,115	51,730	52,115
Facility fees	68,863	62,780	68,863	62,780
Fees from credit cards	49,616	44,346	49,616	44,346
Commissions from retail banking	40,920	40,129	40,920	40,129
Commissions from insurance	33,311	27,268	42,356	36,353
Commissions from loans and advances	7,702	6,880	7,702	6,880
Trust and other commissions	5,097	4,756	306	–
	692,770	718,579	671,157	691,879

Fee and commission expense

	The Group		The Bank	
	2011	2010	2011	2010
Commissions on bills	3,334	3,206	3,334	3,206
Nominees, custodian and securities brokerage commissions paid	15,576	17,014	10,058	10,795
Commissions on retail banking	18,376	17,843	17,422	16,774
Fees on credit cards	115	106	115	106
Commissions on remittance	749	138	749	138
	38,150	38,307	31,678	31,019

	The Group		The Bank	
	2011	2010	2011	2010
Of which :				
Net fee income, other than amounts included in determining the effective interest rate, arising from financial assets or financial liabilities that are not held for trading nor designated at fair value				
– fee income	248,609	238,180	248,609	238,180
– fee expense	3,449	3,312	3,449	3,312
Net fee income on trust and other fiduciary activities where the Group holds or invests on behalf of its customers				
– fee income	21,721	20,696	21,068	20,051

The Group provides custody, trustee and advisory services to third parties. Those assets that are held in a fiduciary capacity are not included in these financial statements.

8 DIVIDEND INCOME

	The Group		The Bank	
	2011	2010	2011	2010
Dividend income from investment in securities				
– listed investments	2,421	2,405	1,729	1,810
– unlisted investments	26,178	19,806	26,178	19,806
	28,599	22,211	27,907	21,616
Dividend income from jointly controlled entities				
– unlisted investments	–	–	1,550	2,660
Dividend income from subsidiary companies				
– unlisted investments	–	–	46,120	67,420
	28,599	22,211	75,577	91,696

9 NET TRADING INCOME

	The Group		The Bank	
	2011	2010	2011	2010
Foreign exchange	119,808	116,957	119,830	116,909
Interest rate instruments	16,217	40,753	16,217	40,753
Equities	(28,529)	16,576	(28,711)	16,576
Other trading income	4,751	6,601	4,751	6,601
	112,247	180,887	112,087	180,839

'Foreign exchange' net trading income includes gains and losses from spot and forward contracts, swaps and translated foreign currency assets and liabilities, which are not designated as qualifying hedging relationship. 'Interest rate instruments' includes the results of trading in instruments in government securities, corporate debt securities and money market instruments. 'Equities' trading income includes the results of trading in equity securities in local and overseas markets.

10 OTHER INCOME

(a) Other operating income

	The Group		The Bank	
	2011	2010	2011	2010
Gross rental income from investment properties	9,913	28,523	11,680	30,127
Others	74,850	60,499	87,650	76,331
	84,763	89,022	99,330	106,458

The Group's direct operating expenses of HK$2,062,000 (2010: HK$3,558,000) arising from investment properties that generated rental income were included in operating expenses.

The Bank's direct operating expenses of HK$2,377,000 (2010: HK$3,872,000) arising from investment properties that generated rental income were included in operating expenses.

(b) Net earned insurance premium

	The Group	
	2011	2010
Insurance premium revenue	38,960	31,759
Insurance premium ceded to reinsurers	(8,140)	(7,844)
	30,820	23,915

The related net insurance claims incurred and movement in policyholders' liabilities of HK$9,374,000 (2010: HK$4,231,000) was shown after netted off with the insurance claims and loss adjustment expenses recovered from reinsurers of HK$203,000 (2010: HK$393,000).

11 OPERATING EXPENSES

	The Group		The Bank	
	2011	2010	2011	2010
Auditors' remuneration				
Statutory audit services	5,474	5,410	4,971	4,930
Non-statutory audit and other services (Note a)	3,925	5,305	3,710	5,136
Advertising costs	18,366	19,613	18,146	19,157
Depreciation expenses for property and equipment	59,210	72,973	64,358	79,711
Direct operating expenses arising from an investment property that did not generate rental income	362	766	362	766
Employee benefit expenses				
Wages and salaries and other costs (Note b)	609,168	590,953	590,159	574,439
Pension costs - defined contribution schemes	32,199	31,288	31,521	30,730
Pension costs - defined benefit schemes	31	30	31	30
Premises and equipment expense, excluding depreciation				
Rental of premises	93,027	54,191	95,153	56,247
Building expenses	11,971	14,412	11,971	14,412
Building management fee	9,761	6,323	9,508	6,069
Other operating expenses				
Computer rental and licence	12,033	11,133	11,581	10,888
Credit card business promotion	15,598	12,630	15,598	12,630
Credit card service fee	10,163	9,560	10,163	9,560
Insurance	10,149	10,387	9,926	10,184
Legal and consultancy	16,419	8,261	15,222	9,143
Postage	12,850	12,498	12,820	12,471
Printing and stationery	8,431	9,062	8,417	8,699
Repair and maintenance	16,297	15,556	23,998	22,557
Telephone and communications	26,411	24,465	24,883	24,363
Travelling and transportation	5,511	4,478	5,422	4,329
Water, heat and light	14,243	12,381	14,021	12,156
Others (Note c)	(107,542)	108,578	(107,934)	106,230
	884,057	1,040,253	874,007	1,034,837

(Note a)

Included in the non-statutory audit and other services is the fee paid for the full scope audit of the Group's financial information for the 6 months ended June for the group reporting to the ultimate holding company in Taiwan under its local statutory requirements.

(Note b)

Employee benefit expenses include directors' emoluments (Note 12). The number of persons employed by the Group as at 31st December 2011 was 1,657 (31st December 2010: 1,679).

(Note c)

During the year, there was a HK$146 million (2010: Nil) recovery arising from the realisation of collateral of Minibonds and a reversal of provision of HK$14 million (Provision of HK$60 million for 2010) in respect of other wealth management products.

12 DIRECTORS' EMOLUMENTS

The Group and the Bank	2011	2010
Fees	3,200	3,200
Basic salaries, allowances and bonus	24,903	22,631
Contributions to pension schemes	781	685
	28,884	26,516

13 REVERSAL/(CHARGE) FOR IMPAIRMENT LOSSES ON LOANS AND ADVANCES TO CUSTOMERS

The Group and the Bank	2011	2010
Trade bills	14,860	(10,661)
Loans and advances to customers	5,045	(73,647)
	19,905	(84,308)
Net reversal/ (charge) of impairment losses on loans and advances to customers		
– Individually assessed	18,281	(44,431)
– Collectively assessed	1,624	(39,877)
	19,905	(84,308)
Of which		
– new allowances	(90,643)	(142,142)
– releases	64,769	47,498
– recoveries	45,779	10,336
Net reversal/ (charge) to income statement	19,905	(84,308)

Included in the amount above was the release of HK$1,786,000 (2010: Nil) in relation to a loan which had been partially written off in previous years and being transferred to other assets.

14 INCOME TAX EXPENSE

Hong Kong profits tax has been provided at the rate of 16.5% (2010: 16.5%) on the estimated assessable profit for the year. Taxation on overseas profits has been calculated on the estimated assessable profit for the year at the rates of taxation prevailing in the countries in which the Group operates.

The amount of taxation charged/ (credited) to the income statement represents:

	The Group		The Bank	
	2011	2010	2011	2010
Current income tax:				
– Hong Kong profits tax	266,982	279,034	265,163	277,634
– Overseas taxation	106,792	71,741	106,414	71,741
– Adjustments in respect of prior years	(533)	(2,757)	(522)	(2,538)
Total current income tax	373,241	348,018	371,055	346,837
Deferred income tax:				
– Hong Kong deferred tax	3,325	(2,058)	3,359	(2,064)
– Overseas deferred tax	12,271	(12,490)	12,271	(12,490)
Total deferred income tax	15,596	(14,548)	15,630	(14,554)
Income tax expense	388,837	333,470	386,685	332,283

14 INCOME TAX EXPENSE (CONTINUED)

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the tax rates of the countries in which the Group operates as follows:

	The Group		The Bank	
	2011	2010	2011	2010
Profit before tax	2,190,951	2,037,889	2,163,134	2,009,363
Tax calculated at domestic tax rates applicable to profits in the respective countries	425,277	367,134	423,457	362,427
Tax effects of:				
Income not subject to tax	(33,261)	(38,566)	(33,299)	(39,475)
Expenses not deductible for tax purposes	4,585	11,393	4,280	15,603
Net effect of investments in partnerships	(7,231)	(3,734)	(7,231)	(3,734)
Adjustment in respect of prior years	(533)	(2,757)	(522)	(2,538)
Tax expense	388,837	333,470	386,685	332,283

The income tax rate applicable to the majority of the Group and its subsidiaries' 2011 income is 16.5% (2010: 16.5%).

For enhancing tax efficient purpose, the Bank has entered into aircraft leverage lease arrangement, involving special purpose partnerships in which the Bank is the general partner. As of 31st December 2011, the unamortised carrying cost of the investments in such partnerships, which was included in 'Other assets', amounted to HK$961,559,000 (2010: HK$909,355,000). The Bank's tax benefit in these special purpose partnerships are amortised over the life of the individual partnerships.

15 INCOME TAX EFFECTS RELATING TO COMPONENTS OF OTHER COMPREHENSIVE INCOME

The Group

	2011			2010		
	Before-tax amount	Tax (expense)/ benefit	Net-of-tax amount	Before-tax amount	Tax (expense)/ benefit	Net-of-tax amount
Foreign currency translation differences	24,393	–	24,393	18,446	–	18,446
Fair value gains/ (losses) on available-for-sale financial assets	(67,228)	10,992	(56,236)	194,725	(33,113)	161,612
Share of changes in equity of jointly controlled entities	(103)	–	(103)	161	–	161
Other comprehensive income for the year (net presentation)	(42,938)	10,992	(31,946)	213,332	(33,113)	180,219

The Bank

	2011			2010		
	Before-tax amount	Tax (expense)/ benefit	Net-of-tax amount	Before-tax amount	Tax (expense)/ benefit	Net-of-tax amount
Foreign currency translation differences	24,388	–	24,388	18,210	–	18,210
Fair value gains/ (losses) on available-for-sale financial assets	(60,611)	10,001	(50,610)	199,626	(32,938)	166,688
Other comprehensive income for the year (net presentation)	(36,223)	10,001	(26,222)	217,836	(32,938)	184,898

16 DIVIDEND

The dividends payable to equity holders of the Bank attributable to the previous financial year, approved and paid during the years ended 2011 and 2010 were HK$860,000,000 (HK$43 per share) and HK$800,000,000 (HK$40 per share) respectively. A dividend in respect of 2011 of HK$43 per share, amounting to a total dividend of HK$860,000,000 is to be proposed at the Annual General Meeting on 20th April 2012. These consolidated financial statements do not reflect this dividend payable.

The Group		
	2011	2010
Dividends proposed to equity holders of the Bank attributable to the year		
Proposed final dividend of HK$43 (2010: HK$43) per ordinary share	860,000	860,000

17 CASH AND BALANCES WITH BANKS

	The Group		The Bank	
	2011	2010 (restated)	2011	2010 (restated)
Cash in hand	416,266	987,326	416,254	987,321
Balances with central banks and Hong Kong Monetary Authority	10,378,663	7,628,038	10,378,663	7,628,038
Balances with banks	16,944,163	17,300,684	16,944,163	17,300,684
	27,739,092	25,916,048	27,739,080	25,916,043

As at 31st December 2011, there was HK$1,500,000 (2010: HK$1,500,000) deposited in the name of the Director of Accounting Services Treasury Hong Kong placed by a subsidiary company in the Bank to comply with statutory requirement.

As at 31st December 2011, there were HK$339,526,000 (2010: HK$96,159,000) of statutory deposits with the central bank in the country the Group is operating the business for the purpose of complying with the local statutory requirements of the country.

18 PLACEMENTS WITH AND LOANS AND ADVANCES TO BANKS

The Group and the Bank		
	2011	2010 (restated)
Placements with banks maturing between one and twelve months	12,996,790	11,646,456
Loans and advances to banks maturing between one and twelve months	1,868,686	1,627,867
	14,865,476	13,274,323

As of 31st December 2011, HK$130,290,000 (2010: HK$127,207,000) was deposited with state banks in the People's Republic of China to comply with the local statutory requirement. No impairment allowance was necessary to be provided against the banks.

19 LOANS AND ADVANCES TO CUSTOMERS

(a) Analysis of loans and advances to customers

The Group and the Bank	2011	2010 (restated)
Loans and advances to individuals		
– Overdrafts	535,531	422,294
– Credit cards	348,377	320,677
– Term loans and others	5,599,470	5,146,313
– Mortgages	6,939,016	6,789,832
Loans and advances to corporate entities		
– Large corporate customers and others	35,585,962	31,556,072
– SMEs	6,471,229	6,792,919
Gross loans and advances to customers	55,479,585	51,028,107
Less: impairment allowances		
– Individually assessed	(69,069)	(104,685)
– Collectively assessed	(214,860)	(216,622)
	55,195,656	50,706,800
Gross trade bills and other eligible bills, included within loans and advances to customers*	3,159,470	1,787,911
Less: impairment allowances on trade bills		
– Collectively assessed	(1,422)	(16,282)
	3,158,048	1,771,629

The Group accepted listed securities at fair value of HK$2,976,549,000 (2010: HK$3,422,796,000) as collateral for shares financing facilities included in 'Term loans and others', which it is permitted to sell or re-pledge in the event of default by the owner of the collateral.

As of 31st December 2011, certain of our branches in the United States have pledged their real estate loans of HK$62,216,000 (2010: HK$64,925,000) to the State of California and with the Comptroller of the Currency in compliance with the regulatory requirements.

*Amount of HK$688,380,000 and HK$1,627,867,000 previously grouped in trade bills as at 31st December 2010 has been reclassified to 'Cash and balances with Banks - Balances with banks' and 'Placement with and loans and advances to banks - Loans and advances to banks maturing between one and twelve months' respectively to conform with the current year's presentation. Interest income from trade bills of HK$36,223,000 have been reclassified from 'Interest income - loans and advances to customers' to 'Interest income - cash and balances with banks' accordingly. Related financial risk management disclosures in Note 3 have been restated accordingly.

19 LOANS AND ADVANCES TO CUSTOMERS (CONTINUED)

(b) Reconciliation of allowance account for losses on loans and advances to customers

The Group and the Bank

	Impairment allowances – Individual assessment				
	Overdrafts	Credit cards	Term loans and others	Mortgages	Total
Movement in impairment allowances on loans and advances to individuals					
Balance at 1st January 2011	323	1,595	8,821	339	11,078
Impairment losses	(135)	3,101	(4,443)	(3,021)	(4,498)
Loans written off as uncollectible	(135)	(4,142)	(83)	–	(4,360)
Recoveries of advances written off in previous years	4	760	472	2,938	4,174
At 31st December 2011	57	1,314	4,767	256	6,394
Balance at 1st January 2010	262	2,302	21,349	2,900	26,813
Impairment losses	58	3,537	(13,815)	(4,930)	(15,150)
Loans written off as uncollectible	–	(5,073)	(394)	–	(5,467)
Recoveries of advances written off in previous years	3	829	1,681	2,369	4,882
At 31st December 2010	323	1,595	8,821	339	11,078

	Impairment allowances – Individual assessment		
	Large corporate customers and others	SMEs	Total
Movement in impairment allowances on loans and advances to corporate entities			
Balance at 1st January 2011	84,897	8,710	93,607
Impairment losses	(11,708)	(289)	(11,997)
Loans written off as uncollectible	(57,918)	(2,629)	(60,547)
Recoveries of advances written off in previous years	39,832	1,773	41,605
Exchange adjustments	7	–	7
At 31st December 2011	55,110	7,565	62,675
Balance at 1st January 2010	89,613	21,303	110,916
Impairment losses	64,590	(5,009)	59,581
Loans written off as uncollectible	(71,536)	(9,165)	(80,701)
Recoveries of advances written off in previous years	3,873	1,581	5,454
Exchange adjustments	(1,643)	–	(1,643)
At 31st December 2010	84,897	8,710	93,607

	Impairment allowances – Collective assessment				
	Overdrafts	Credit cards	Term loans and others	Mortgages	Total
Movement in impairment allowances on loans and advances to individuals					
Balance at 1st January 2011	1,679	7,838	19,391	25,379	54,287
Impairment losses	295	461	1,839	635	3,230
Exchange adjustments	–	–	(7)	(47)	(54)
At 31st December 2011	1,974	8,299	21,223	25,967	57,463
Balance at 1st January 2010	1,751	6,202	16,229	25,944	50,126
Impairment losses	(72)	1,636	3,140	(539)	4,165
Exchange adjustments	–	–	22	(26)	(4)
At 31st December 2010	1,679	7,838	19,391	25,379	54,287

19 LOANS AND ADVANCES TO CUSTOMERS (CONTINUED)

(b) Reconciliation of allowance account for losses on loans and advances to customers (Continued)

The Group and the Bank

	Impairment allowances – Collective assessment		
	Large corporate customers and others	SMEs	Total
Movement in impairment allowances on loans and advances to corporate entities			
Balance at 1st January 2011	138,221	24,114	162,335
Impairment losses	(4,934)	80	(4,854)
Exchange adjustments	(83)	(1)	(84)
At 31st December 2011	133,204	24,193	157,397
Balance at 1st January 2010	100,108	26,386	126,494
Impairment losses	37,986	(2,274)	35,712
Exchange adjustments	127	2	129
At 31st December 2010	138,221	24,114	162,335

20 FINANCIAL ASSETS HELD FOR TRADING

The Group and the Bank

	2011	2010
Debt securities		
Listed outside Hong Kong	181,191	166,655
Unlisted	140,167	328,214
Total debt securities	321,358	494,869
Equity securities		
Listed in Hong Kong	9,108	–
Listed outside Hong Kong	107,344	115,221
Total equity securities	116,452	115,221
Other financial assets held for trading	6,427	–
Total financial assets held for trading	444,237	610,090
Included within debt securities are:		
Other government bonds	182,183	227,411
Certificate of deposits held	121,615	152,540
Other debt securities	17,560	114,918
	321,358	494,869
Financial assets held for trading are analysed by issuers as follows:		
Sovereigns	182,183	227,411
Banks	154,710	270,395
Corporates	107,344	112,284
	444,237	610,090

21 DERIVATIVE FINANCIAL INSTRUMENTS

The Group uses the following derivative instruments for non-hedging purposes:

Currency forwards represent commitments to purchase foreign and domestic currency, including undelivered spot transactions. **Foreign currency and interest rate futures** are contractual obligations to receive or pay a net amount based on changes in currency rates or interest rates or to buy or sell foreign currency or a financial instrument on a future date at a specified price, established in an organised financial market. The credit risk is negligible, as futures contracts are collateralised by cash or marketable securities, and changes in the futures contract value are settled daily with the exchange. **Forward rate agreements** are individually negotiated interest rate futures that call for a cash settlement at a future date for the difference between a contracted rate of interest and the current market rate, based on a notional principal amount.

Currency and interest rate swaps are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of currencies or interest rates (for example, fixed rate for floating rate) or a combination of all these (i.e. cross-currency interest rate swaps). No exchange of principal takes place, except for certain currency swaps. The Group's credit risk represents the potential cost to replace the swap contracts if counterparties fail to perform their obligation. This risk is monitored on an ongoing basis with reference to the current fair value, a proportion of the notional amount of the contracts and the liquidity of the market. To control the level of credit risk taken, the Group assesses counterparties using the same techniques as for its lending activities.

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the statement of financial position but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and, therefore, do not indicate the Group's exposure to credit or price risks. The derivative instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in market interest rates or foreign exchange rates relative to their terms. The aggregate contractual or notional amount of derivative financial instruments on hand, the extent to which instruments are favourable or unfavourable, and thus the aggregate fair values of derivative financial assets and liabilities, can fluctuate significantly from time to time. The fair values of derivative instruments held are set out below.

At 31st December 2011

	Contract amount	The Group and the Bank Fair values	
		Assets	Liabilities
Derivatives held for trading			
Foreign exchange derivatives			
Currency forward exchange contracts	13,809,630	70,294	(45,409)
Total derivative assets/ (liabilities) held for trading	13,809,630	70,294	(45,409)
Total recognised derivative financial assets/ (liabilities)	13,809,630	70,294	(45,409)

21 DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)

At 31st December 2010

	Contract amount	The Group and the Bank Fair values	
		Assets	Liabilities
Derivatives held for trading			
Foreign exchange derivatives			
Currency forward exchange contracts	4,347,507	60,468	(52,473)
Cross-currency interest rate swaps contracts	785,416	1,016	(1,035)
Total derivative assets/ (liabilities) held for trading	5,132,923	61,484	(53,508)
Total recognised derivative financial assets/ (liabilities)	5,132,923	61,484	(53,508)

	The Group and the Bank Credit risk weighted amount	
	2011	2010
Exchange rate contracts	93,747	72,778

The contract amounts of these instruments indicate the volume of transactions outstanding as at the end of the reporting period, they do not represent the amounts at risk.

The credit risk weighted amounts as at 31st December 2011 and 2010 are the amounts that have been calculated in accordance with the Banking (Capital) Rules of the Banking Ordinance.

The Group did not enter into any bilateral netting arrangements during the year and accordingly the amounts disclosed are shown on a gross basis.

The Group uses the following derivative strategies:

– Trading purposes (customer needs)

The Group offers its customers derivatives in connection with their risk-management actions to transfer, modify or reduce their interest rate, foreign exchange and other market/credit risks or for their own trading purposes. As part of this process, the Group considers the customers' suitability for the risk involved, and the business purpose for the transaction. The Group also manages its derivative-risk positions through offsetting trade activities, controls focused on price verification, and daily reporting of positions to senior managers.

– Trading purposes (own account)

The Group trades derivatives for its own account. These derivatives entered into in order to take proprietary long positions. Trading limits and price verification controls are key aspects of this activity.

22 AVAILABLE-FOR-SALE INVESTMENTS

	The Group		The Bank	
	2011	2010	2011	2010
Debt securities:				
Listed in Hong Kong	1,332,068	1,195,895	1,332,068	1,195,895
Listed outside Hong Kong	7,433,563	6,610,549	7,430,378	6,607,204
Unlisted	11,682,044	11,986,242	11,585,035	11,790,973
	20,447,675	19,792,686	20,347,481	19,594,072
Equity securities:				
Listed in Hong Kong	60,582	136,729	40,815	117,614
Listed outside Hong Kong	37,677	58,731	37,677	58,731
Unlisted	1,462,726	1,480,553	1,462,726	1,480,553
	1,560,985	1,676,013	1,541,218	1,656,898
	22,008,660	21,468,699	21,888,699	21,250,970
Included within debt securities are:				
Certificates of deposit held	6,568,933	2,815,172	6,538,337	2,804,699
Other government bonds	180,762	21,065	180,762	21,065
Other debt securities	13,697,980	16,956,449	13,628,382	16,768,308
	20,447,675	19,792,686	20,347,481	19,594,072
Available-for-sale investments are analysed by issuers as follows:				
Sovereigns	180,762	21,065	180,762	21,065
Public sector entities	250,940	756,621	250,940	756,621
Banks	18,669,457	17,190,813	18,567,972	16,983,210
Corporates	2,907,501	3,500,200	2,889,025	3,490,074
	22,008,660	21,468,699	21,888,699	21,250,970

The movement in available-for-sale investments is summarised as follow:

The Group		
	2011	2010
As at 1st January	21,468,699	20,225,698
Exchange differences	(30,378)	304,320
Additions	9,997,853	14,260,783
Gains from changes in fair value	88,898	456,763
Disposals (sale and redemption)	(9,488,738)	(13,766,983)
Amortisation	(31,490)	(38,374)
Others	3,816	26,492
As at 31st December	22,008,660	21,468,699
Net gains from available-for-sale investments comprise:		
Disposal of available-for-sale investments	155,824	263,175

22 AVAILABLE-FOR-SALE INVESTMENTS (CONTINUED)

The Bank	2011	2010
As at 1st January	21,250,970	19,879,810
Exchange differences	(30,376)	304,307
Additions	9,964,352	14,260,364
Gains from changes in fair value (Note 33)	95,515	461,469
Disposals (sale and redemption)	(9,367,207)	(13,648,856)
Amortisation	(30,981)	(33,460)
Others	6,426	27,336
As at 31st December	21,888,699	21,250,970
Net gains from available-for-sale investments comprise:		
Disposal of available-for-sale investments	155,824	262,979

23 HELD-TO-MATURITY INVESTMENTS

	The Group		The Bank	
	2011	2010	2011	2010
Debt securities:				
Listed in Hong Kong	2,119,682	2,040,167	39,112	39,121
Listed outside Hong Kong	645,101	726,244	623,254	718,350
Unlisted	–	–	–	–
	2,764,783	2,766,411	662,366	757,471
Market value of listed securities	2,800,071	2,798,071	658,316	758,624
Included within debt securities are:				
Other government bonds	2,307,538	2,268,159	226,968	267,114
Other debt securities	457,245	498,252	435,398	490,357
	2,764,783	2,766,411	662,366	757,471
Held-to-maturity investments are analysed by issuer as follows:				
Sovereigns	2,307,538	2,268,159	226,968	267,114
Public sector entities	39,112	39,121	39,112	39,121
Banks	414,113	455,144	396,286	451,236
Corporates	4,020	3,987	–	–
	2,764,783	2,766,411	662,366	757,471

As of 31st December 2011, certain of the United States branches have pledged held-to-maturity investments amounting to HK$148,049,000 (2010: HK$189,048,000) to the State of California and with the Comptroller of the Currency in compliance with local regulatory requirements.

Listed debt securities at amortised cost of HK$2,080,571,000 (2010: HK$2,001,045,000) of Exchange Fund Notes was pledged to the Hong Kong Monetary Authority as at 31st December 2011 to facilitate settlement operations with no related liabilities at the year end.

23 HELD-TO-MATURITY INVESTMENTS (CONTINUED)

The movement in held-to-maturity investments is summarised as follow:

The Group

	2011	2010
At 1st January	2,766,411	2,868,942
Exchange differences	(406)	2,295
Additions	972,194	378,219
Redemption	(947,044)	(451,797)
Amortisation	(24,082)	(26,997)
Others	(2,290)	(4,251)
At 31st December	2,764,783	2,766,411

The Bank

	2011	2010
At 1st January	757,471	901,715
Exchange differences	(406)	2,275
Additions	55,012	131,703
Redemption	(148,153)	(271,797)
Amortisation	(1,158)	(1,324)
Others	(400)	(5,101)
At 31st December	662,366	757,471

24 INVESTMENTS IN AND LOANS TO JOINTLY CONTROLLED ENTITIES AND SUBSIDIARIES

(a) Investments in jointly controlled entities

The Group

	2011	2010
At 1st January	174,473	159,901
Share of results, net of tax	16,488	18,371
Dividends paid	(1,550)	(2,660)
Decrease of advances	–	(1,300)
Other equity movement: available-for-sale reserve	(103)	161
At 31st December	189,308	174,473

The Bank

	2011	2010
Unlisted shares, at cost	116,000	116,000

24 INVESTMENTS IN AND LOANS TO JOINTLY CONTROLLED ENTITIES AND SUBSIDIARIES (CONTINUED)

(a) Investments in jointly controlled entities (Continued)

The Group's interest in its jointly controlled entities, which are unlisted, are as follows:

2011

Name	Place of incorporation	Assets	Liabilities	Revenues	Profit/ (loss)	% interest held
Joint Electronic Teller Services Limited	Hong Kong	376,030	2,795	82,039	34,774	20% of 'A' shares [1]
Bank Consortium Holding Limited	Hong Kong	564,429	209,725	364,403	95,453	14.29% of 'A' shares
BC Reinsurance Limited	Hong Kong	436,337	267,237	146,273	(37,262)	21% [1]
Hong Kong Life Insurance Limited	Hong Kong	5,272,010	4,890,387	879,767	63,217	16.67%
i-Tech Solutions Limited	Hong Kong	6,639	304	6,385	97	50%
		6,655,445	5,370,448	1,478,867	156,279	

2010

Name	Place of incorporation	Assets	Liabilities	Revenues	Profit/ (loss)	% interest held
Joint Electronic Teller Services Limited	Hong Kong	361,784	3,948	85,432	38,795	20% of 'A' shares [1]
Bank Consortium Holding Limited	Hong Kong	495,463	235,811	288,419	56,838	14.29% of 'A' shares
BC Reinsurance Limited	Hong Kong	435,925	224,563	129,595	20,965	21% [1]
Hong Kong Life Insurance Limited	Hong Kong	4,279,106	3,960,406	855,282	32,462	16.67%
i-Tech Solutions Limited	Hong Kong	6,488	251	6,279	(259)	50%
		5,578,766	4,424,979	1,365,007	148,801	

[1] During the year, the Bank has received 2.88% and 21% (2010: 2.88% and 21%) of the dividends paid by the Joint Electronic Teller Service Limited and BC Reinsurance Limited respectively.

Note: The balances with the jointly controlled entities arising from normal business transactions are included in Note 37.

(b) Investments in subsidiaries

The Bank

	2011	2010
Investments, at cost:		
Unlisted shares	193,188	193,199
Loans to subsidiary companies	3,050,789	2,978,635
Amounts due from subsidiary companies	813	281
Amounts due to subsidiary companies	(1,158,348)	(1,063,181)
	2,086,442	2,108,934

24 INVESTMENTS IN AND LOANS TO JOINTLY CONTROLLED ENTITIES AND SUBSIDIARIES (CONTINUED)

(b) Investments in subsidiaries (Continued)

The following is a list of the principal subsidiaries at 31st December 2011:

Name	Place of incorporation	Principal activities and place of operation	Particulars of issued share capital	Percentage of ordinary share capital held
Shanghai Commercial Bank (Nominees) Limited	Hong Kong	Nominee services Hong Kong	100 ordinary shares of HK$100 each	*100%
Shanghai Commercial Bank Trustee Limited	Hong Kong	Trustee services Hong Kong	1,000 ordinary shares of HK$10,000 each	*60%
Shacom Futures Limited	Hong Kong	Commodities trading Hong Kong	100,000 ordinary shares of HK$100 each	*100%
Shacom Investment Limited	Hong Kong	Investment in Exchange Fund Bills and Notes Hong Kong	10,000 ordinary shares of HK$100 each	*100%
Shacom Property Holdings (BVI) Limited	British Virgin Islands	Property holding British Virgin Islands	2 ordinary shares of US$1 each	*100%
Shacom Property (NY) Inc.	United States of America	Property holding United States of America	10 ordinary shares of US$1 each	*100%
Shacom Property (CA) Inc.	United States of America	Property holding United States of America	10 ordinary shares of US$1 each	*100%
Shacom Assets Investments Limited	Hong Kong	Investment in notes and bonds Hong Kong	10,000 ordinary shares of HK$1 each	*100%
Infinite Financial Solutions Limited	Hong Kong	I.T. application services provider Hong Kong	500,000 ordinary shares of US$1 each	*80%
Shacom Insurance Brokers Limited	Hong Kong	Insurance broker Hong Kong	1,000,000 ordinary shares of HK$1 each	*100%
Shacom Securities Limited	Hong Kong	Securities brokerage services Hong Kong	1,000,000 ordinary shares of HK$100 each	*100%
Hai Kwang Property Management Company Limited	Hong Kong	Property management Hong Kong	2 ordinary shares of HK$1 each	*100%
Paofoong Insurance Company (Hong Kong) Limited	Hong Kong	Insurance Hong Kong	500,000 ordinary shares of HK$100 each	*60%
Right Honour Investments Limited	British Virgin Islands	Property holding British Virgin Islands	1 ordinary shares of US$1 each	*100%
Glory Step Investments Limited	British Virgin Islands	Property holding British Virgin Islands	1 ordinary shares of US$1 each	100%
Silver Wisdom Investments Limited	British Virgin Islands	Property holding British Virgin Islands	1 ordinary shares of US$1 each	100%

* Shares held directly by the Bank.

(c) Loans to subsidiaries

The loans to subsidiaries are secured, interest free and have no fixed term of repayment. The fair values of loans to subsidiaries are HK$3,050,789,000 (2010: HK$2,978,635,000). The carrying amounts of the loans approximate their fair values.

25 PROPERTY AND EQUIPMENT

The Group

	Leasehold land	Bank premises	Furniture, fittings and equipment	Property under development: Leasehold land	Property under development: Development cost	Total
At 1st January 2010						
Cost	325,589	467,222	610,769	–	–	1,403,580
Accumulated depreciation	(61,387)	(186,352)	(517,443)	–	–	(765,182)
Net book amount	264,202	280,870	93,326	–	–	638,398
Year ended December 2010						
Opening net book amount	264,202	280,870	93,326	–	–	638,398
Additions	–	–	18,746	–	–	18,746
Disposals/ write-off						
Cost	–	–	(24,870)	–	–	(24,870)
Accumulated depreciation	–	–	23,344	–	–	23,344
Depreciation charge	(4,820)	(8,847)	(32,561)	–	–	(46,228)
Exchange rate adjustments	–	(851)	45	–	–	(806)
Closing net book amount	259,382	271,172	78,030	–	–	608,584
At 31st December 2010						
Cost	325,589	466,163	604,213	–	–	1,395,965
Accumulated depreciation	(66,207)	(194,991)	(526,183)	–	–	(787,381)
Net book amount	259,382	271,172	78,030	–	–	608,584
Year ended December 2011						
Opening net book amount	259,382	271,172	78,030	–	–	608,584
Additions	15,719	15,719	65,732	–	11,697	108,867
Transfers						
Cost	(2,500)	777	(777)	2,500	–	–
Accumulated depreciation	46	(766)	766	(46)	–	–
Transfers from investment property (Note 26)						
Cost	–	–	–	1,381,406	–	1,381,406
Accumulated depreciation	–	–	–	(5,770)	–	(5,770)
Disposals/ write-off						
Cost	–	(4,155)	(70,399)	–	–	(74,554)
Accumulated depreciation	–	4,155	69,350	–	–	73,505
Depreciation charge	(4,837)	(9,252)	(37,075)	(826)	–	(51,990)
Exchange rate adjustments	–	(145)	261	–	–	116
Closing net book amount	267,810	277,505	105,888	1,377,264	11,697	2,040,164
At 31st December 2011						
Cost	338,808	478,284	599,058	1,383,906	11,697	2,811,753
Accumulated depreciation	(70,998)	(200,779)	(493,170)	(6,642)	–	(771,589)
Net book amount	267,810	277,505	105,888	1,377,264	11,697	2,040,164

25 PROPERTY AND EQUIPMENT (CONTINUED)

The Bank

	Leasehold land	Bank premises	Furniture, fittings and equipment	Property under development: Leasehold land	Property under development: Development cost	Total
At 1st January 2010						
Cost	297,513	422,618	671,058	–	–	1,391,189
Accumulated depreciation	(60,467)	(178,224)	(566,963)	–	–	(805,654)
Net book amount	237,046	244,394	104,095	–	–	585,535
Year ended December 2010						
Opening net book amount	237,046	244,394	104,095	–	–	585,535
Additions	–	–	21,826	–	–	21,826
Disposals/ write-off						
Cost	–	–	(24,825)	–	–	(24,825)
Accumulated depreciation	–	–	23,309	–	–	23,309
Depreciation charge	(4,589)	(8,206)	(39,743)	–	–	(52,538)
Exchange rate adjustments	–	170	66	–	–	236
Closing net book amount	232,457	236,358	84,728	–	–	553,543
At 31st December 2010						
Cost	297,513	422,835	667,708	–	–	1,388,056
Accumulated depreciation	(65,056)	(186,477)	(582,980)	–	–	(834,513)
Net book amount	232,457	236,358	84,728	–	–	553,543
Year ended December 2011						
Opening net book amount	232,457	236,358	84,728	–	–	553,543
Additions	15,719	15,719	71,140	–	11,697	114,275
Transfers						
Cost	(2,500)	777	(777)	2,500	–	–
Accumulated depreciation	46	(766)	766	(46)	–	–
Transfers from investment property (Note 26)						
Cost	–	–	–	1,381,406	–	1,381,406
Accumulated depreciation	–	–	–	(5,770)	–	(5,770)
Disposals/ write-off						
Cost	–	(4,155)	(70,314)	–	–	(74,469)
Accumulated depreciation	–	4,155	69,267	–	–	73,422
Depreciation charge	(4,608)	(8,594)	(42,682)	(826)	–	(56,710)
Exchange rate adjustments	–	(55)	259	–	–	204
Closing net book amount	241,114	243,439	112,387	1,377,264	11,697	1,985,901
At 31st December 2011						
Cost	310,731	435,094	668,056	1,383,906	11,697	2,809,484
Accumulated depreciation	(69,617)	(191,655)	(555,669)	(6,642)	–	(823,583)
Net book amount	241,114	243,439	112,387	1,377,264	11,697	1,985,901

25 PROPERTY AND EQUIPMENT (CONTINUED)

The Group's interests in leasehold land and land use rights represent operating leases and their net book value are analysed as follows:

	The Group		The Bank	
	2011	2010	2011	2010
In Hong Kong held on:				
Leases of over 50 years	1,487,556	97,501	1,460,860	70,576
Leases of between 10 to 50 years	157,518	161,881	157,518	161,881
	1,645,074	259,382	1,618,378	232,457

Interests in freehold land outside Hong Kong are included as bank premises above amounted to HK$36,670,000 as at 31st December 2011 (2010: HK$36,757,000) for the Group, and HK$19,035,000 (2010: HK$19,052,000) for the Bank.

26 INVESTMENT PROPERTIES

The Group

	Leasehold land	Buildings	Total
As 1st January 2010			
Cost	1,381,406	62,739	1,444,145
Accumulated depreciation	(3,297)	(31,369)	(34,666)
Net book amount	1,378,109	31,370	1,409,479
Year ended December 2010			
Opening net book amount	1,378,109	31,370	1,409,479
Depreciation charge	(1,649)	(25,096)	(26,745)
Closing net book amount	1,376,460	6,274	1,382,734
At 31st December 2010			
Cost	1,381,406	62,739	1,444,145
Accumulated depreciation	(4,946)	(56,465)	(61,411)
Net book amount	1,376,460	6,274	1,382,734
Year ended December 2011			
Opening net book amount	1,376,460	6,274	1,382,734
Additions	4,658	4,657	9,315
Transfers to property under development (Note 25)			
Cost	(1,381,406)	–	(1,381,406)
Accumulated depreciation	5,770	–	5,770
Write-off			
Cost	–	(62,739)	(62,739)
Accumulated depreciation	–	62,739	62,739
Depreciation charge	(830)	(6,390)	(7,220)
Closing net book amount	4,652	4,541	9,193
At 31st December 2011			
Cost	4,658	4,657	9,315
Accumulated depreciation	(6)	(116)	(122)
Net book amount	4,652	4,541	9,193

26 INVESTMENT PROPERTIES (CONTINUED)

The Bank

	Leasehold land	Buildings	Total
As 1st January 2010			
Cost	1,409,482	70,658	1,480,140
Accumulated depreciation	(4,217)	(32,161)	(36,378)
Net book amount	1,405,265	38,497	1,443,762
Year ended December 2010			
Opening net book amount	1,405,265	38,497	1,443,762
Depreciation charge	(1,879)	(25,294)	(27,173)
Closing net book amount	1,403,386	13,203	1,416,589
At 31st December 2010			
Cost	1,409,482	70,658	1,480,140
Accumulated depreciation	(6,096)	(57,455)	(63,551)
Net book amount	1,403,386	13,203	1,416,589
Year ended December 2011			
Opening net book amount	**1,403,386**	**13,203**	**1,416,589**
Additions	**4,658**	**4,657**	**9,315**
Transfers to property under development (Note 25)			
Cost	**(1,381,406)**	**–**	**(1,381,406)**
Accumulated depreciation	**5,770**	**–**	**5,770**
Write-off			
Cost	**–**	**(62,739)**	**(62,739)**
Accumulated depreciation	**–**	**62,739**	**62,739**
Depreciation charge	**(1,060)**	**(6,588)**	**(7,648)**
Closing net book amount	**31,348**	**11,272**	**42,620**
At 31st December 2011			
Cost	**32,734**	**12,576**	**45,310**
Accumulated depreciation	**(1,386)**	**(1,304)**	**(2,690)**
Net book amount	**31,348**	**11,272**	**42,620**

The Group's investment property was revalued for a value of HK$7,500,000, and the Bank's investment properties were revalued for a total value of HK$87,500,000 as at 31st December 2011 by an independent, professionally qualified valuer on an open market value basis.

As at 31st December 2010, the Board of Directors consider that the fair values of the Group's investment property and the Bank's investment properties are not materially different from the purchase costs. The investment property of the Group located adjacent to the Bank's Head Office are being re-developed jointly with the Bank's Head Office building and had been transferred to property under development (Note 25) during the year.

The carrying value of investment properties shown above comprise leasehold land and buildings situated in Hong Kong, which are held on long-term leases.

27 OTHER ASSETS

	The Group		The Bank	
	2011	2010	2011	2010
Repossessed assets	19,825	41,652	19,825	41,652
Accounts receivable and prepayments *	1,497,379	1,513,137	1,316,293	1,152,609
Others	89,018	60,581	84,232	55,744
	1,606,222	1,615,370	1,420,350	1,250,005

* As stated in Note 14, there are unamortised carrying cost of investment in special purpose partnerships included in accounts receivable and prepayments.

28 DEPOSITS FROM CUSTOMERS

The Group and the Bank

	2011			
	Large Corporate Customers	SMEs	Retail	Total
Demand deposits and current accounts	5,002,293	1,319,564	2,559,028	8,880,885
Savings deposits	8,426,083	2,362,071	17,425,952	28,214,106
Time, call and notice deposits	29,032,067	1,260,904	35,320,526	65,613,497
Deposits from Hong Kong Government Exchange Fund	388,708	–	–	388,708
	42,849,151	4,942,539	55,305,506	103,097,196

The Group and the Bank

	2010			
	Large Corporate Customers	SMEs	Retail	Total
Demand deposits and current accounts	4,160,716	1,295,983	2,921,423	8,378,122
Savings deposits	9,646,784	1,790,994	19,786,638	31,224,416
Time, call and notice deposits	23,074,293	1,175,623	31,221,749	55,471,665
Deposits from Hong Kong Government Exchange Fund	388,988	–	–	388,988
	37,270,781	4,262,600	53,929,810	95,463,191

Included in customer accounts were deposits of HK$1,269,060,000 (2010: HK$1,134,275,000) held as collateral for irrevocable commitments. The fair value of these deposits approximates the carrying amount.

Deposit amounting to HK$65,824,405,000 (2010: HK$55,407,522,000) are at fixed interest rates, HK$37,094,991,000 (2010: HK$39,602,539,000) are at managed interest rates and all other deposits, amounting to HK$177,800,000 (2010: HK$453,130,000) are at variable rates.

29 OTHER LIABILITIES

	The Group		The Bank	
	2011	2010 (restated)	2011	2010
Margin deposits	344,269	349,196	344,269	349,196
Accounts payable and accruals	396,109	538,110	283,248	186,318
Liabilities for insurance contracts (Note)	35,641	25,599	–	–
Others	432,250	558,477	362,841	553,239
	1,208,269	1,471,382	990,358	1,088,753

Note: Amounts recoverable from reinsurance of liabilities under insurance contracts issued amounting to HK$1,267,000 (2010: HK$762,000) are included in 'Other assets' in Note 27.

30 PROVISIONS

	The Group		The Bank	
	2011	2010	2011	2010
At 1st January	99,654	94,500	99,220	93,924
Additional provisions charged to income statement	163,285	169,122	161,418	167,641
Utilised during the year	(168,248)	(163,968)	(166,318)	(162,345)
At 31st December	94,691	99,654	94,320	99,220
Current	94,599	99,587	94,320	99,220
Non-current	92	67	–	–

Majority of the 2011 and 2010 balances represents provision for staff gratuity.

31 DEFERRED INCOME TAX

The movement in deferred income tax assets and liabilities during the year, without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

Deferred income tax liabilities

	The Group				
	Impairment allowances	Accelerated tax depreciation	Fair value gains	Others	Total
At 1st January 2010	36,011	(3,666)	(112,630)	(2,423)	(82,708)
(Charged)/ credited to the income statement	(1,234)	3,908	–	(616)	2,058
Charged to equity	–	–	(33,113)	–	(33,113)
Reclassification to current income tax liabilities	–	–	–	717	717
At 31st December 2010	34,777	242	(145,743)	(2,322)	(113,046)
(Charged)/ credited to the income statement	380	(2,512)	–	(1,193)	(3,325)
Credited to equity	–	–	10,001	–	10,001
Reclassification to current income tax liabilities	–	–	–	1,260	1,260
Reclassification to deferred income tax assets	–	–	559	–	559
At 31st December 2011	35,157	(2,270)	(135,183)	(2,255)	(104,551)

31 DEFERRED INCOME TAX (CONTINUED)

Deferred income tax liabilities

	The Bank				
	Impairment allowances	Accelerated tax depreciation	Fair value gains	Others	Total
At 1st January 2010	36,011	(3,605)	(112,244)	(2,423)	(82,261)
(Charged)/ credited to the income statement	(1,234)	3,914	–	(616)	2,064
Charged to equity	–	–	(32,938)	–	(32,938)
Reclassification from deferred income tax assets	–	–	–	717	717
At 31st December 2010	34,777	309	(145,182)	(2,322)	(112,418)
(Charged)/ credited to the income statement	380	(2,546)	–	(1,193)	(3,359)
Credited to equity	–	–	10,001	–	10,001
Reclassifcation to current income tax liabilities	–	–	–	1,260	1,260
At 31st December 2011	35,157	(2,237)	(135,181)	(2,255)	(104,516)

Deferred income tax assets

	The Group				
	Impairment allowances	Accelerated tax depreciation	Fair value loss	Others	Total
At 1st January 2010	31,735	(1,224)	–	13,468	43,979
(Charged)/ credited to the income statement	8,001	(12)	–	4,501	12,490
Exchange differences	115	(8)	–	80	187
At 31st December 2010	39,851	(1,244)	–	18,049	56,656
(Charged)/ credited to the income statement	(7,922)	2,992	–	(7,341)	(12,271)
Credited to equity	–	–	991	–	991
Exchange differences	(52)	(5)	–	(5)	(62)
Reclassification from deferred income tax liabilities	–	–	(559)	–	(559)
At 31st December 2011	31,877	1,743	432	10,703	44,755

Deferred income tax assets

	The Bank				
	Impairment allowances	Accelerated tax depreciation	Fair value loss	Others	Total
At 1st January 2010	31,735	(1,224)	–	13,468	43,979
(Charged)/ credited to the income statement	8,001	(12)	–	4,501	12,490
Exchange differences	115	(8)	–	80	187
At 31st December 2010	39,851	(1,244)	–	18,049	56,656
(Charged)/ credited to the income statement	(7,922)	2,992	–	(7,341)	(12,271)
Exchange differences	(52)	(5)	–	(5)	(62)
At 31st December 2011	31,877	1,743	–	10,703	44,323

31 DEFERRED INCOME TAX (CONTINUED)

The deferred taxation (charged)/ credited to equity during the year is as follows:

	The Group		The Bank	
	2011	2010	2011	2010
Available-for-sale investment revaluation reserve/ (deficit)				
– Reserves in shareholders' equity (Note 33)	10,596	(33,043)	10,001	(32,938)
– Reserves in non-controlling interests	396	(70)	–	–
	10,992	(33,113)	10,001	(32,938)

32 SHARE CAPITAL

The Group and the Bank

	2011	2010
Authorised:		
30,000,000 shares of HK$100 each	3,000,000	3,000,000
Issued and fully paid:		
20,000,000 shares of HK$100 each	2,000,000	2,000,000

33 OTHER RESERVES

The Group

	Regulatory reserve	Available-for-sale investment revaluation reserve	General reserve	Total
Balance at 1st January 2010	362,370	573,934	7,311,687	8,247,991
Change in fair value of available-for-sale investments	–	456,261	–	456,261
Realised on disposal of available-for-sale investments	–	(263,096)	–	(263,096)
Effect of deferred taxation (Note 31)	–	(33,043)	–	(33,043)
Currency translation differences	–	1,136	14,179	15,315
Share of investment revaluation reserve of jointly controlled entities	–	161	–	161
Balance at 31st December 2010	362,370	735,353	7,325,866	8,423,589
Balance at 1st January 2011	362,370	735,353	7,325,866	8,423,589
Change in fair value of available-for-sale investments	–	91,302	–	91,302
Realised on disposal of available-for-sale investments	–	(155,824)	–	(155,824)
Effect of deferred taxation (Note 31)	–	10,596	–	10,596
Currency translation differences	–	(302)	24,141	23,839
Transfer from retained earnings	100,000	–	–	100,000
Share of investment revaluation reserve of jointly controlled entities	–	(103)	–	(103)
Balance at 31st December 2011	462,370	681,022	7,350,007	8,493,399

33 OTHER RESERVES (CONTINUED)

The Bank

	Regulatory reserve	Available-for-sale investment revaluation reserve	General reserve	Total
Balance at 1st January 2010	362,370	568,032	7,311,602	8,242,004
Change in fair value of available-for-sale investments (Note 22)	–	461,469	–	461,469
Realised on disposal of available-for-sale investments (Note 22)	–	(262,979)	–	(262,979)
Effect of deferred taxation (Note 31)	–	(32,938)	–	(32,938)
Currency translation differences	–	1,136	14,179	15,315
Balance at 31st December 2010	362,370	734,720	7,325,781	8,422,871
Balance at 1st January 2011	362,370	734,720	7,325,781	8,422,871
Change in fair value of available-for-sale investments (Note 22)	–	95,515	–	95,515
Realised on disposal of available-for-sale investments (Note 22)	–	(155,824)	–	(155,824)
Effect of deferred taxation (Note 31)	–	10,001	–	10,001
Currency translation differences	–	(302)	24,159	23,857
Transfer from retained earnings	100,000	–	–	100,000
Balance at 31st December 2011	462,370	684,110	7,349,940	8,496,420

Nature and purpose of reserves:

(a) Regulatory reserve

The regulatory reserve is maintained to satisfy the provisions of the Hong Kong Banking Ordinance for prudent supervision purpose. Any movements in the regulatory reserve are made in consultation with the Hong Kong Monetary Authority.

(b) Available-for-sale investment revaluation reserve

Reserve for fair value changes of available-for-sale investments represent the cumulative net change in the fair value of available-for-sale investments until the financial assets are derecognised or impaired as stated in the accounting policy for financial assets. (Note 2.10 and Note 2.11)

(c) General reserve

General reserve comprises previous years' transfers from retained earnings, translation reserve and inner reserve.

34 CASH AND CASH EQUIVALENTS

For the purposes of the statement of cash flows, cash and cash equivalents comprises the following balances with less than three months' maturity from the date of acquisition, deposits that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

	2011	2010 (restated)
Cash and balances with banks	24,561,638	24,236,391
Placements with and loans and advances to banks	2,087,183	790,183
	26,648,821	25,026,574

35 CONTINGENT LIABILITIES AND COMMITMENTS

(a) Capital commitments

Capital expenditure at the end of the reporting period but not yet incurred is as follows:

	The Group		The Bank	
	2011	2010	2011	2010
Property and equipment				
Contracted but not provided for	35,128	54,870	37,824	57,133
Authorised but not contracted for	85,115	88,856	85,115	89,867
	120,243	143,726	122,939	147,000

(b) Operating lease commitments

Where a group company is the lessee, the future minimum lease payments under non-cancellable operating leases are as follows:

	The Group		The Bank	
	2011	2010	2011	2010
No later than 1 year	88,621	86,544	89,818	88,346
Later than 1 year and no later than 5 years	190,075	206,375	190,075	207,576
Later than 5 years	70	32,251	70	32,251
	278,766	325,170	279,963	328,173

Where a group company is the lessor, the future minimum lease receivables under non-cancellable operating leases are as follows:

	The Group		The Bank	
	2011	2010	2011	2010
No later than 1 year	556	6,466	556	6,466
Later than 1 year and no later than 5 years	–	172	–	172
	556	6,638	556	6,638

(c) Credit commitments

The contract amounts of the Group's off-balance sheet financial instruments that commit it to extend credit to customers:

The Group and The Bank		
	2011	2010
Direct credit substitutes	2,330,130	2,177,614
Trade-related contingencies	3,406,417	2,979,778
Other commitments with an original maturity of:		
– under 1 year	1,128,087	1,575,238
– 1 year and over	2,848,244	1,878,263
– unconditionally cancellable	31,685,429	40,456,515
	41,398,307	49,067,408

The credit risk weighted amount of credit commitments is HK$4,345,251,000 (2010: HK$3,777,401,000).

(d) Other contingent liabilities

The Group is involved in legal actions which are in relation to its normal business operations. No material provision was made for those actions against the Group because the management believes that the Group has defences against the claimants or the amounts involved in those actions are not expected to be material.

36 LOANS TO OFFICERS

Particulars of loans made by the Bank to officers and companies related to officers and disclosed pursuant to Section 161B of the Hong Kong Companies Ordinance are as follows:

	Balance outstanding at 31st December		Maximum balance during the year	
	2011	2010	2011	2010
Aggregate amount outstanding in respect of principal and interest	720,627	537,136	737,016	689,520

37 RELATED PARTY TRANSACTIONS

A number of banking transactions were entered into with related parties by the Group or the Bank in the normal course of business and at arm's length basis. These include loans, deposits, trade finance transactions and foreign currency transactions. The volumes of related party transactions, outstanding balances at the year end, and related expense and income for the year are as follows:

Included in the following statement of financial position captions are balances with the ultimate holding company:

The Group and the Bank		
	2011	2010
Cash and balances with banks	468,022	10,058
Available-for-sale investments	96,855	115,811
	564,877	125,869
Deposits and balances from banks at 1st January	524,279	454,557
Deposits and balances from banks received during the year	190,076	71,732
Deposits and balances from banks repaid during the year	(67,679)	(2,010)
Deposits and balances from banks at 31st December	646,676	524,279
Interest income on deposits placed at and loans to the ultimate holding company	5,556	279
Interest expense on deposits from the ultimate holding company	3,980	1,491
Contingent liabilities and other commitments	262,469	253,125

Included in the following statement of financial position captions are balances with subsidiary companies of the ultimate holding company:

The Group and the Bank		
	2011	2010
Deposits from customers at 1st January	305,308	304,876
Deposits from customers received during the year	7,022	2,797
Deposits from customers repaid during the year	(2,169)	(2,365)
Deposits from customers at 31st December	310,161	305,308
Interest expense on deposits from the subsidiary companies of the ultimate holding company	2,001	1,774

37 RELATED PARTY TRANSACTIONS (CONTINUED)

Included in the following statement of financial position captions are balances with other shareholders:

The Group and the Bank	2011	2010
Cash and balances with banks	40,441	44,164
Available-for-sale and held-to-maturity investments	586,355	774,504
	626,796	818,668
Loans and advances to customers at 1st January	–	1,426
Loans and advances to customers repaid during the year	–	(1,426)
Loans and advances to customers at 31st December	–	–
Collectively assessed impairment allowances	–	–
Deposits from customers at 1st January	19,082	131,894
Deposits from customers received during the year	113,523	19,613
Deposits from customers repaid during the year	(11,048)	(132,425)
Deposits from customers at 31st December	121,557	19,082
Interest income on loans and advances to other shareholders	2,292	3,027
Interest expenses on deposits from other shareholders	523	382

Included in the following statement of financial position captions are balances with jointly controlled entities:

The Group and the Bank	2011	2010
Loans and advances to customers at 1st January	43,553	53,792
Loans and advances to customers repaid during the year	(5,953)	(10,239)
Loans and advances to customers at 31st December	37,600	43,553
Collectively assessed impairment allowances	150	174
Deposits from customers at 1st January	194,477	251,461
Deposits from customers received during the year	149,381	40,043
Deposits from customers repaid during the year	(47,275)	(97,027)
Deposits from customers at 31st December	296,583	194,477
Interest income on loans and advances to the jointly controlled entities	333	392
Interest expenses on deposits from the jointly controlled entities	1,695	660
Contingent liabilities and other commitments	2,000	2,000

Amounts due from/ (to) subsidiary companies are included in Note 24(b) and amounts due from jointly controlled entities are included in Note 24(a).

37 RELATED PARTY TRANSACTIONS (CONTINUED)

Included in the following statement of financial position captions are balances with the Directors and their relatives:

The Group and the Bank

	2011	2010
Loans and advances to customers at 1st January	222,954	293,531
Loans and advances to customers granted during the year	167,021	7,725
Loans and advances to customers repaid during the year	(7,247)	(78,302)
Loans and advances to customers at 31st December	382,728	222,954
Collectively assessed impairment allowances	1,557	892
Deposits from customers at 1st January	90,452	146,411
Deposits from customers received during the year	38,728	43,644
Deposits from customers repaid during the year	(28,504)	(99,603)
Deposits from customers at 31st December	100,676	90,452
Interest income on loans and advances to the Directors and their relatives	6,864	5,642
Interest expenses on deposits from the Directors and their relatives	568	357
Contingent liabilities and other commitments	24,954	38,466

Included in the following statement of financial position captions are balances with companies controlled by the Directors and their relatives:

The Group and the Bank

	2011	2010
Loans and advances to customers at 1st January	296,989	409,343
Loans and advances to customers granted during the year	31,242	69,008
Loans and advances to customers repaid during the year	(6,737)	(181,362)
Loans and advances to customers at 31st December	321,494	296,989
Collectively assessed impairment allowances	1,286	1,188
Deposits from customers at 1st January	223,180	741,032
Deposits from customers received during the year	74,348	34,510
Deposits from customers repaid during the year	(69,826)	(552,362)
Deposits from customers at 31st December	227,702	223,180
Interest income on loans and advances to the companies controlled by the Directors and their relatives	12,073	12,003
Interest expenses on deposits from the companies controlled by the Directors and their relatives	2,007	846
Contingent liabilities and other commitments	244,280	335,068

37 RELATED PARTY TRANSACTIONS (CONTINUED)

Included in the following statement of financial position captions are balances with the key management personnel, other than Directors of the Bank and the ultimate holding company and their relatives:

The Group and the Bank	2011	2010
Loans and advances to customers at 1st January	10,603	14,920
Loans and advances to customers granted during the year	1,424	1,439
Loans and advances to customers repaid during the year	(2,364)	(5,756)
Loans and advances to customers at 31st December	9,663	10,603
Collectively assessed impairment allowances	80	42
Deposits from customers at 1st January	18,775	13,996
Deposits from customers received during the year	20,782	8,312
Deposits from customers repaid during the year	(9,677)	(3,533)
Deposits from customers at 31st December	29,880	18,775
Interest income on loans and advances to the key management personnel of the Bank and the ultimate holding company and their relatives	721	569
Interest expenses on deposits from the key management personnel of the Bank and the ultimate holding company and their relatives	252	37
Contingent liabilities and other commitments	5,498	5,926

Included in the following statement of financial position captions are balances with companies controlled by the key management personnel, other than Directors of the Bank and the ultimate holding company and their relatives:

The Group and the Bank	2011	2010
Deposits from customers at 1st January	–	11,841
Deposits from customers repaid during the year	–	(11,841)
Deposits from customers at 31st December	–	–
The compensation of Directors and key management personnel of the Bank: Salaries and other short-term employee benefits	52,910	52,384

Note: The aggregate movement of revolving loans is shown in its net position during the year.

38 ULTIMATE HOLDING COMPANY

The ultimate holding company is The Shanghai Commercial & Savings Bank, Ltd.

39 COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the current year's presentation.

The following information is disclosed as part of the accompanying information to the consolidated financial statements and does not form part of the audited financial statements.

1 Liquidity ratio

	2011	2010
Liquidity ratio	47%	51%

The liquidity ratio is calculated as the simple average of each calendar month's average liquidity ratio for the twelve months of the financial year of the Bank's overseas and Hong Kong offices computed in accordance with the Banking (Disclosure) Rules.

2 Non-bank mainland exposures

As at 31st December 2011

	On-balance sheet exposure	Off-balance sheet exposure	Total	Individually assessed impairment allowances
Types of counterparties				
Mainland entities	1,876,989	355,778	2,232,767	–
Companies and individuals outside Mainland where the credit is granted for use in Mainland	2,260,451	313,802	2,574,253	12,677
Other counterparties the exposures to whom are considered by the Group to be non-bank Mainland exposures	148,842	207,493	356,335	1,075
	4,286,282	877,073	5,163,355	13,752

As at 31st December 2010

	On-balance sheet exposure	Off-balance sheet exposure	Total	Individually assessed impairment allowances
Types of counterparties				
Mainland entities	1,761,992	21,623	1,783,615	–
Companies and individuals outside Mainland where the credit is granted for use in Mainland	3,252,575	944,108	4,196,683	18,149
Other counterparties the exposures to whom are considered by the Group to be non-bank Mainland exposures	113,849	157,881	271,730	1,085
	5,128,416	1,123,612	6,252,028	19,234

3 Currency concentrations

The Group

Equivalent in Hong Kong dollars	2011 Spot assets	Spot liabilities	Forward purchases	Forward sales	Net long/ (short) position	Net structural position
US Dollars	39,234,000	(39,118,000)	7,462,000	(8,464,000)	(886,000)	3,412,000
Pound Sterling	2,031,000	(2,032,000)	45,000	(29,000)	15,000	10,000
Yuan Renminbi	10,189,000	(9,507,000)	3,871,000	(3,900,000)	653,000	107,000
Canadian Dollars	1,744,000	(1,746,000)	31,000	(18,000)	11,000	–
Australian dollar	6,455,000	(6,587,000)	1,221,000	(1,177,000)	(88,000)	–
Other currencies and gold	3,059,000	(3,065,000)	300,000	(306,000)	(12,000)	–
	62,712,000	(62,055,000)	12,930,000	(13,894,000)	(307,000)	3,529,000

Equivalent in Hong Kong dollars	2010 Spot assets	Spot liabilities	Forward purchases	Forward sales	Net long/ (short) position	Net structural position
US Dollars	40,877,000	(40,870,000)	3,876,000	(4,656,000)	(773,000)	3,193,000
Pound Sterling	1,815,000	(1,811,000)	37,000	(27,000)	14,000	5,000
Yuan Renminbi	6,153,000	(5,961,000)	1,242,000	(1,171,000)	263,000	74,000
Canadian Dollars	1,436,000	(1,446,000)	32,000	(14,000)	8,000	–
Australian dollar	5,290,000	(5,362,000)	415,000	(372,000)	(29,000)	–
Other currencies and gold	3,589,000	(3,671,000)	448,000	(365,000)	1,000	–
	59,160,000	(59,121,000)	6,050,000	(6,605,000)	(516,000)	3,272,000

Net structural position includes structural positions of the Bank's overseas branches, banking subsidiaries and other subsidiaries substantially involved in foreign exchange. Structural assets and liabilities include:

– investments in property and equipment, net of depreciation;

– capital and statutory reserves of overseas branches; and

– investments in overseas subsidiaries and related company.

The above disclosure is based on the significance of the Group's foreign currency exposures of the current year.

4 Loans and advances to customers

(a) Gross advances to customers by loan usage

The Group

	2011		2010	
	Gross advances	Amount covered by collateral/ other security	Gross advances	Amount covered by collateral/ other security
Loans for use in Hong Kong				
Industrial, commercial and financial				
– Property development	1,916,158	1,049,683	2,820,335	948,978
– Property investment	11,519,801	10,698,444	11,947,671	11,156,783
– Financial concerns	70,471	69,178	278,883	277,213
– Stockbrokers	16,048	14,249	10,015	–
– Wholesale and retail trade	1,010,922	633,777	879,732	753,337
– Manufacturing	1,778,685	1,100,288	1,543,525	895,996
– Transport and transport equipment	793,162	347,681	736,772	257,070
– Information technology – telecommunication	2,159	861	149,720	148,717
– Hotels, boarding houses and catering	941,579	927,034	846,265	827,552
– Others	4,183,634	2,951,769	2,915,025	1,665,101
Individuals				
– Loans for the purchase of flats in the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	263,119	261,995	316,398	315,051
– Loans for the purchase of other residential properties	4,269,934	4,261,578	4,685,462	4,685,462
– Credit card advances	323,162	–	301,200	158
– Others	5,739,932	5,519,857	4,794,679	4,744,455
Trade finance	5,932,944	2,974,036	5,224,429	2,814,117
Loans for use outside Hong Kong *	13,558,405	11,884,108	11,790,085	10,856,997
	52,320,115	42,694,538	49,240,196	40,346,987

* Included in 'Loans for use outside Hong Kong' were advances to individuals of HK$2,826,247,000 (2010: HK$2,581,377,000).

4 Loans and advances to customers (Continued)

(b) Impairment allowances on loans and advances by loan usage

For those industry sectors to which the Bank's total amount of loans and advances constitute not less than 10% of the Bank's total amount of loans and advances, the amount of impaired loans and advances which are individually determined to be impaired are analysed as follows:

The Group

	2011			
	Individually assessed to be impaired	Overdue	Individual impairment allowance	Collective impairment allowance
Industrial, commercial and financial – Property investment	27,319	152,581	111	45,970

	2010			
	Individually assessed to be impaired	Overdue	Individual impairment allowance	Collective impairment allowance
Industrial, commercial and financial – Property investment	51,698	152,059	966	47,583
Individuals – Loans for the purchase of other residential properties	36,564	91,225	299	18,596
	88,262	243,284	1,265	66,179

The Group

	2011		
	New provisions	Loans written off as uncollectible	Recoveries of advances written off in previous years
Industrial, commercial and financial – Property investment	–	–	440

	2010		
	New provisions	Loans written off as uncollectible	Recoveries of advances written off in previous years
Industrial, commercial and financial – Property investment	921	313	1,256
Individuals – Loans for the purchase of other residential properties	6	–	2,369
	927	313	3,625

5 Segmental information

(a) Overdue and impaired loans by geographical areas

The Group

	2011		
	Individually assessed to be impaired	Individual impairment allowance	Collective impairment allowance
Hong Kong	323,791	38,212	–
North America	596,404	30,857	–
	920,195	69,069	–

	2011		
	Overdue	Individual impairment allowance	Collective impairment allowance
Hong Kong	684,902	31,425	2,242
Asia Pacific excluding Hong Kong	25,633	16	83
North America	678,702	17,496	2,003
Western Europe	24,130	–	97
	1,413,367	48,937	4,425

The Group

	2010		
	Individually assessed to be impaired	Individual impairment allowance	Collective impairment allowance
Hong Kong	332,250	39,673	–
North America	469,136	65,012	–
	801,386	104,685	–

	2010		
	Overdue	Individual impairment allowance	Collective impairment allowance
Hong Kong	550,831	20,757	1,580
Asia Pacific excluding Hong Kong	16,807	–	67
North America	606,487	5,032	1,705
Western Europe	25,669	–	103
	1,199,794	25,789	3,455

5 Segmental information (Continued)

(b) Cross-border claims

The information on cross-border claims discloses exposures to foreign counterparties on which the ultimate risk lies, and is derived according to the location of the counterparties after taking into account any transfer of risk.

The Group

	2011			
	Banks and other financial institutions	Public sector entities	Others	Total
Asia Pacific excluding Hong Kong	32,685,000	161,000	1,705,000	34,551,000
North America	2,821,000	181,000	353,000	3,355,000
Western Europe	3,751,000	78,000	303,000	4,132,000

	2010			
	Banks and other financial institutions	Public sector entities	Others	Total
Asia Pacific excluding Hong Kong	27,404,000	60,000	1,176,000	28,640,000
North America	2,918,000	167,000	981,000	4,066,000
Western Europe	4,538,000	78,000	230,000	4,846,000

6 Corporate governance

(a) The Bank has fully complied with the requirements set out in the guideline on 'Corporate Governance of Locally Incorporated Authorized Institutions' issued by the Hong Kong Monetary Authority.

(b) Key specialised committees established under the Board of Directors (the 'Board')

(i) Executive Committee

The Executive Committee meets monthly and operates as a general management committee under the direct authority of the Board to review the management and performance of the Bank. The members of the Executive Committee are Mr. David Sek-chi Kwok (Chairman), Mr. Hung-ching Yung, Mr. Shen Ruolei, Mr. Richard Jason Lloyd Yorke and Mr. Edward Kawah Chu.

(ii) Audit Committee

The Audit Committee meets quarterly to consider the nature and scope of audit reviews, as well as to review the Bank's financial statements, the findings of both internal and external auditors and the effectiveness of the internal control systems of the Bank. The members of the Audit Committee are Mr. Gordon Che Keung Kwong (Chairman), Mr. Lincoln Chu Kuen Yung and Dr. Richard Lee.

(iii) Remuneration Committee

The Remuneration Committee meets at least once a year to oversee the implementation of a sound remuneration policy including the recommendations to the Board on the remuneration of the directors and senior management of the Bank. The members of the Remuneration Committee are Mr. Hung-ching Yung (Chairman), Dr. Richard Lee and Mr. Johnson Mou Daid Cha.

(iv) Asset and Liability Committee

The Asset and Liability Committee meets at least monthly to oversee the Bank's operations relating to interest rate risk, liquidity risk, foreign exchange risk and etc. and in particular to ensure that the Bank has adequate funds to meet its obligations. The members of the Asset and Liability Committee are Mr. David Sek-chi Kwok (Chairman), Mr. Edward Kawah Chu, Mr. Henry Koon-man To, Mr. Paul Kun-kow Wong, Mr. Stephen Siu-fung Lee, Mr. Frank Shui-sang Jin, Mr. Hon-ming Mak, and Mr. Danny Kong-keung Tsang.

(v) Credit Committee

The Credit Committee meets at least monthly to ensure that the Bank's credit policies are adequate and lending activities are conducted in accordance with established policies and relevant laws and regulations. The Credit Committee is also responsible for establishing credit policies, monitoring loan portfolio quality, ensuring compliance with statutory and internal lending limits, and evaluating credit applications and making credit decisions. The members of the Credit Committee are Mr. David Sek-chi Kwok (Chairman), Mr. Edward Kawah Chu, Mr. Stephen Siu-fung Lee, Mr. Frank Shui-sang Jin, Mr. Hon-ming Mak, Mr. Danny Kong-keung Tsang, Mr. Ho-kei Wan and Mr. Sau-man Hui.

(vi) Operational Risk Management Committee

The Operational Risk Management Committee meets at least bi-monthly to establish and to review operational risk management policies, processes and procedures for managing operational risk in all of the Bank's material products, activities, processes and systems. The Operational Risk Management Committee is also responsible for overseeing the identification, assessment, monitoring and control of operational risk exposures. The members of the Operational Risk Management Committee are Mr. David Sek-chi Kwok (Chairman), Mr. Edward Kawah Chu, Mr. Daniel Kwok-hung Chan, Mr. Burton Chi-shan Cheng, Mr. Stephen Siu-fung Lee, Mr. Frank Shui-sang Jin, Mr. Hon-ming Mak, Mr. Pui-man Yeung, Mr. Zachary Wing-kwong Kwan, Mr. Danny Kong-keung Tsang and Mr. Francis Yue-cheong Wong.

7 Capital charges for credit, market and operational risks

The capital adequacy ratio in Note 3.5 to the financial statements represents the consolidated ratio that comprises the positions of the Bank and subsidiaries for regulatory purposes as at 31st December computed in accordance with the Banking (Capital) Rules. For accounting purposes, the basis of consolidation is described in Note 2.2 to the consolidated financial statements.

7 Capital charges for credit, market and operational risks (Continued)

The capital requirements for each class of exposures are summarised as follows:

(a) Capital charge for credit risk

Capital requirement	2011	2010
Sovereign exposures	35,970	1,414
Public Sector Entity exposures	4,645	12,732
Bank exposures	1,592,651	1,311,702
Securities Firm exposures	642	401
Corporate exposures	2,469,871	2,312,267
Cash items	9,616	7,281
Regulatory Retail exposures	266,676	258,029
Residential Mortgage Loans	558,576	593,029
Other exposures which are not past due exposures	729,977	644,387
Past due exposures	41,853	32,943
Total capital charge for on-balance sheet exposures	5,710,477	5,174,185
Direct credit substitutes	183,169	171,197
Trade-related contingencies	53,892	46,988
Other commitments	110,559	84,007
Exchange rate contracts	7,500	5,822
Total capital charge for off-balance sheet exposures	355,120	308,014
Total capital charge for credit risk	6,065,597	5,482,199

This disclosure is made by multiplying the Group's risk-weighted amount derived from the relevant calculation approach by 8%, not the institution's actual 'regulatory capital'.

(b) Capital charge for market risk

Capital charge	2011	2010
Interest rate exposures (including options)	14,762	26,486
Equity exposures (including options)	17,174	17,966
Foreign exchange exposures (including gold and options)	68,640	33,680
Capital charge for market risk	100,576	78,132

The Bank uses the Standardised Approach for calculating market risk.

(c) Capital charge for operational risk

	2011	2010
Capital charge for operational risk	420,704	417,516

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

8 Risk management

(a) Credit risk

(i) Credit risk exposures

Standard & Poor's Ratings Services, Moody's Investors Service, Fitch Ratings and Rating and Investment, Inc. are the ECAIs that the institution has used in relation to each and all classes of credit risk exposures below. The process it used to map ECAI issuer ratings to exposures booked in its banking book is a process as prescribed in Part 4 of the Banking (Capital) Rules.

The Group As at 31st December 2011

	Total exposures	Exposures after recognised credit risk mitigation		Risk-weighted amounts		Total risk-weighted amounts	Total exposure covered by recognised collateral	Total exposure covered by recognised guarantees or recognised credit derivative contracts
		Rated	Unrated	Rated	Unrated			
A. On-balance Sheet								
1 Sovereign	14,786,610	14,786,610	–	449,624	–	449,624	–	–
2 Public Sector Entity	290,329	290,329	–	58,066	–	58,066	–	–
3 Multilateral Development Bank	28,279	28,279	–	–	–	–	–	–
4 Bank	50,239,298	45,938,126	4,301,172	18,076,229	1,831,913	19,908,142	–	–
5 Securities Firm	16,045	–	16,045	–	8,023	8,023	–	–
6 Corporate	32,539,033	3,317,270	29,221,763	1,651,625	29,221,763	30,873,388	20,299,513	845,666
7 Cash Items	442,849	–	1,609,809	–	120,193	120,193	–	–
8 Regulatory Retail	4,444,600	–	4,444,600	–	3,333,451	3,333,451	3,463,127	–
9 Residential Mortgage Loan	10,913,655	–	10,913,655	–	6,982,200	6,982,200	9,836,362	–
10 Other exposures which are not Past Due Exposures	9,124,710	–	9,124,710	–	9,124,710	9,124,710	4,764,550	–
11 Past Due Exposures	516,785	–	516,785	–	523,168	523,168	501,141	–
B. Off-balance Sheet								
1 Off-balance sheet exposures other than OTC derivative transactions or credit derivative contracts	4,661,153	433,383	4,227,770	176,517	4,168,734	4,345,251	–	299,469
2 OTC derivative transactions	206,469	153,613	52,856	48,483	45,264	93,747	–	–

The Group As at 31st December 2010

	Total exposures	Exposures after recognised credit risk mitigation		Risk-weighted amounts		Total risk-weighted amounts	Total exposure covered by recognised collateral	Total exposure covered by recognised guarantees or recognised credit derivative contracts
		Rated	Unrated	Rated	Unrated			
A. On-balance Sheet								
1 Sovereign	9,917,262	9,917,262	–	17,677	–	17,677	–	–
2 Public Sector Entity	795,742	795,742	–	159,148	–	159,148	–	–
3 Multilateral Development Bank	128,279	128,279	–	–	–	–	–	–
4 Bank	47,933,991	43,195,465	4,738,526	14,393,079	2,003,196	16,396,275	–	–
5 Securities Firm	10,015	–	10,015	–	5,008	5,008	–	–
6 Corporate	31,098,552	4,376,408	26,722,144	2,181,194	26,722,144	28,903,338	18,673,499	1,280,624
7 Cash Items	989,611	–	2,036,218	–	91,015	91,015	–	–
8 Regulatory Retail	4,300,482	–	4,300,482	–	3,225,362	3,225,362	3,888,956	–
9 Residential Mortgage Loan	11,385,547	–	11,385,547	–	7,412,868	7,412,868	10,184,304	–
10 Other exposures which are not Past Due Exposures	8,054,835	–	8,054,835	–	8,054,835	8,054,835	4,321,158	–
11 Past Due Exposures	403,494	–	403,494	–	411,788	411,788	313,584	–
B. Off-balance Sheet								
1 Off-balance sheet exposures other than OTC derivative transactions or credit derivative contracts	4,027,750	302,358	3,725,392	114,661	3,662,740	3,777,401	–	137,328
2 OTC derivative transactions	113,509	46,831	66,678	12,380	60,398	72,778	–	–

8 Risk management (Continued)

(a) Credit risk (Continued)

(ii) Counterparty credit risk exposures

The following table summarises the Group's main credit exposures arises from OTC derivative transactions:

The Group	2011 OTC derivative transactions	2010 OTC derivative transactions
OTC derivative:		
Gross total positive fair value	70,294	61,484
Credit equivalent amount	206,469	113,509
Risk weighted amounts	93,747	72,778

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

The Group	2011 OTC derivative transactions	2010 OTC derivative transactions
Notional amounts:		
– Banks	10,623,343	3,351,224
– Corporates	2,329,721	1,713,374
– Others	856,566	68,325
	13,809,630	5,132,923
Credit equivalent amounts/ net credit exposures:		
– Banks	153,613	46,831
– Corporates	43,815	64,680
– Others	9,041	1,998
	206,469	113,509
Risk-weighted amounts:		
– Banks	48,483	12,380
– Corporates	38,249	58,423
– Others	7,015	1,975
	93,747	72,778

8 Risk management (Continued)

(b) Asset securitisation

There are no such exposures for the year ended 31st December 2011 and 2010.

(c) Equity exposures in banking book

Gains related to equity exposures are as follows:

The Group	2011	2010
Realised gains from sales during the year	20,502	20,751
Unrealised revaluation gains at year ended:		
– Amount included in reserves but not through income statement	987,466	996,261
– Amount added to core/ supplementary capital	446,545	448,443

(d) Interest rate exposures in banking book

2011

	Currency				
Equivalent in Hong Kong Dollars	Hong Kong Dollars	US Dollars	Chinese Renminbi	Others	Total
Interest rate risk shock (200 basis points upward) Increase/ (decline) in earnings	23,172	(78,142)	(9,890)	(3,815)	(68,675)

2010

	Currency				
Equivalent in Hong Kong Dollars	Hong Kong Dollars	US Dollars	Chinese Renminbi	Others	Total
Interest rate risk shock (200 basis points upward) Increase/ (decline) in earnings	27,029	(134,560)	18,082	(22,790)	(112,239)

For 2011 and 2010, the effect of decline in earnings and increase in earnings with interest rate risk shock of 200 basis points downward are contra to that with interest rate risk shock of 200 basis points upward.

9 Disclosure on Remuneration

GUIDING PRINCIPLES

The Bank is committed to sustaining long-term capital preservation and financial strength for the benefits of all stakeholders. The Remuneration Policy of the Bank is designed to promote fairness and consistency in the compensation approach; to attract, motivate and retain talents, as well as to help achieve the business goals under prudent risk management principles.

The Remuneration Policy applies to the Bank in Hong Kong and its subsidiaries, where appropriate. While the basic principles are applicable to foreign branches, they are also subject to their local regulatory requirements in respective jurisdictions.

REMUNERATION COMMITTEE

The Remuneration Committee is established with written Terms of Reference defining its authority and duties to oversee the formulation and implementation of a sound remuneration policy by the Bank, and to ensure its consistency with the best practices and applicable legal and regulatory requirements.

Directly appointed by the Board of the Bank, majority of the members of the Committee are Independent Non-executive Directors. The Committee is chaired by Mr. Hung-ching Yung. The other members are Dr. Richard Lee and Mr. Johnson Mou Daid Cha.

The Remuneration Committee reviews the remuneration policy and its structure of the Bank at least annually and had held two meetings in 2011.

9 Disclosure on Remuneration (Continued)

REMUNERATION OF DIRECTORS AND SENIOR MANAGEMENT

The Remuneration Committee is responsible for making recommendations to the Board on the formulation and review of the remuneration packages for the Directors, the Chief Executive and Senior Management, with reference to the Bank's financial condition and future prospect, risk management framework, reward and people strategies. Such packages are subject to the final approval of the Board.

No individual Director/ Staff or any of his/ her alternates shall be involved in deciding his/ her own remuneration package.

REMUNERATION STRUCTURE

The remuneration package is a combination of fixed and variable remuneration. Fixed remuneration consists of basic salary, allowances, double pay and pension contribution. Variable remuneration takes into account the overall performance of the Bank and various business units, individual performance measured against the established key performance indicators, adherence to risk management policies, compliance with legal and regulatory requirements and ethical standards. The variable remuneration is awarded in the form of cash bonus.

A proportion of the variable remuneration will be deferred and the vesting criteria of the deferred payment are subject to the impact of financial and non-financial factors over a period of time.

PERFORMANCE MEASUREMENTS AND THE DISTRIBUTION OF VARIABLE REMUNERATION

The Bank maintains a performance evaluation scheme to ensure individual staff performance would be differentiated into various levels, and be adequately and effectively evaluated. Final approval of the discretionary bonus is determined by various quantitative and qualitative assessment criteria set out in the performance appraisal system.

The employees within risk control functions are remunerated independently. The performance of business units where they oversee does not affect their remuneration.

When deciding the remuneration measures, the Bank shall also take into account certain key risk factors such as its asset quality, liquidity position, business environments, respective staff performance, the overall business results as well as long-term financial position. The timing and the portion of the performance-related bonus distribution are vested in the Remuneration Committee and finally with the Board.

DEFERRAL ARRANGEMENTS

In view of the Bank's existing business model and organization structure, a portion of the discretionary bonus payment of senior management will be deferred and may be subject to a vesting period for a number of years in order to align with long-term value creation and the time horizons of risk.

SENIOR MANAGEMENT AND KEY PERSONNEL REMUNERATION

Aggregate quantitative information on remuneration for the Bank's senior management and key personnel for the financial year of 2011:

Senior Management		
Total value of remuneration awards for the current financial year	Non-deferred	Deferred
Fixed remuneration		
• Cash-based	25,532	Nil
Variable remuneration		
• Cash-based	23,787	2,643
Deferred remuneration		
• Vested cash		822
• Unvested cash		4,272

Notes:

(i) The unvested deferred remuneration relates to the 2010 and 2011 variable remuneration.

(ii) No senior management and key personnel has been awarded with guaranteed bonus, new sign-on or severance payment for the financial year 2011.

(iii) Number of senior management staff: 13.

(iv) Number of key personnel other than those senior management described above: Nil.

BRANCHES AND SUBSIDIARY COMPANIES

Management and Administration

35/F., Gloucester Tower, The Landmark, 15 Queen's Road Central, Hong Kong
Telephone: (852) 2841 5415
Fax: (852) 2810 4623
Telex: 73650 SCBK HX
SWIFT: SCBK HK HH
Web Site: http://www.shacombank.com.hk

Hong Kong Island Branches

Retail Banking Operations - Central	Basement, Manning House, 48 Queen's Road Central
Aberdeen Branch	118 Aberdeen Main Road, Aberdeen
Causeway Bay Branch	18 Pennington Street, Causeway Bay
Hennessy Road Branch	Shop LG16, C. C. Wu Building, 302 Hennessy Road, Wanchai
North Point Branch	486 King's Road, North Point
President Theatre Branch	Shop A, G/F., 517 Jaffe Road, Causeway Bay
Shaukiwan Branch	136 Shaukiwan Main Street East, Shaukiwan
Sheung Wan Branch	19-25 Jervois Street, Sheung Wan
Siu Sai Wan Branch	Shop 9, G/F., Harmony Garden, 9 Siu Sai Wan Road, Chai Wan
Taikoo Shing Branch	G502 Tai Yue Avenue, Taikoo Shing, Quarry Bay
Victoria Centre Branch	G7 Victoria Centre, 15 Watson Road, Causeway Bay
Wanchai Branch	19-21 Hennessy Road, Wanchai
West Point Branch	47 Catchick Street, West Point

Kowloon Branches

Jordan Road Branch	Shop 2, G/F., Sino Cheer Plaza, 23 Jordan Road, Jordan
Kowloon Bay Branch	Telford House, 16 Wang Hoi Road, Kowloon Bay
Kowloon Tong Branch	G28 Franki Centre, 320 Junction Road, Kowloon Tong
Kwun Tong Branch	57-61 Hong Ning Road, Kwun Tong
Laichikok Branch	Shops 5-8, G/F., Lai Kwan Court, 438 Castle Peak Road
Mei Foo Sun Chuen (Stage 1) Branch	29D Broadway, Mei Foo Sun Chuen, Laichikok
Mei Foo Sun Chuen (Stage 4) Branch	83B Broadway, Mei Foo Sun Chuen, Laichikok
Mongkok Branch	666 Nathan Road, Mongkok
Ping Shek Estate Branch	115 Tsuen Shek House, Ping Shek Estate, Ngau Chi Wan
Sanpokong Branch	28 Hong Keung Street, Sanpokong
Sham Shui Po Branch	141 Cheung Sha Wan Road, Sham Shui Po
Tokwawan Branch	60 Tokwawan Road, Tokwawan
Tsimshatsui Branch	7 Hankow Road, Tsimshatsui
Tsimshatsui East Branch	G27 Houston Centre, 63 Mody Road, Tsimshatsui East
Waterloo Road Branch	84K Waterloo Road, Homantin
Whampoa Garden Branch	Shop 9, Palm Mansions, Whampoa Garden, Site 4, Hunghom
Wong Tai Sin Branch	Shop LG4, Lung Cheung Plaza, 136 Lung Cheung Road, Wong Tai Sin

New Territories and Outlying Island Branches

Kingswood Villa Branch	Shop G08, G/F., Phase 2, Kingswood Ginza, 18 Tin Yan Road, Tin Shui Wai
Kwai Chung Branch	Shop 3, Hutchison Estate, 482 Castle Peak Road, Kwai Chung
Ma On Shan Branch	Shop 308, Level 3, Ma On Shan Plaza, 608 Sai Sha Road, Ma On Shan
Shatin Branch	Shop 70B, Level 3, Shatin Centre, Wang Pok Street, Shatin
Sheung Shui Branch	82 San Fung Avenue, Sheung Shui
Tai Po Branch	Shop 54, Level 1, Uptown Plaza, 9 Nam Wan Road, Tai Po
Texaco Road Branch	Shops B128-131, East Asia Commercial Centre, 36-60 Texaco Road, Tsuen Wan
Tseung Kwan O Branch	Shops G1-2, G/F., Metro City Plaza III, The Metropolis, 8 Mau Yip Road, Tseung Kwan O
Tsuen Wan Branch	405 Castle Peak Road, Tsuen Wan
Tuen Mun Branch	Shop 2183, 2/F., Tuen Mun Town Plaza Phase 1, 1 Tuen Shing Street, Tuen Mun
Tung Chung Branch	Shops 1-2, Block 5, Tung Chung Crescent, Tung Chung, Lantau
TVB Office	2/F., Workshop Block, TVB City, 77 Chun Choi Street, Tseung Kwan O Industrial Estate
Yuen Long Branch	17 Hong Lok Road, Yuen Long

Overseas Branches

London Branch	65 Cornhill, London, EC3V 3NB, U.K.
Los Angeles Branch	383 East Valley Boulevard, Alhambra, CA 91801, U.S.A.
New York Branch	125 East 56th Street, New York, NY 10022, U.S.A.
San Francisco Branch	231 Sansome Street, San Francisco, CA 94104, U.S.A.

Mainland Branch

Shenzhen Branch	Room 01-03, 20/F, Tower One, Kerry Plaza, No.1 Zhong Xin Si Road, Futian District, Shenzhen 518048, China

Mainland Representative Office

Shanghai Representative Office	Room 916, 9/F., China Merchants Tower, 161 Lu Jia Zui Road (E), Pu Dong, Shanghai 200120, P.R.C.

Wholly-owned Subsidiary Companies

Glory Step Investments Limited
Hai Kwang Property Management Company Limited
Right Honour Investments Limited
Shacom Assets Investments Limited
Shacom Futures Limited
Shacom Insurance Brokers Limited
Shacom Investment Limited
Shacom Property (CA) Inc.
Shacom Property (NY) Inc.
Shacom Property Holdings (BVI) Limited
Shacom Securities Limited
Shanghai Commercial Bank (Nominees) Limited
Silver Wisdom Investments Limited

Subsidiary Companies

Infinite Financial Solutions Limited
Shanghai Commercial Bank Trustee Limited
Paofoong Insurance Company (Hong Kong) Limited