SHANGHAI COMMERCIAL BANK

2019
ANNUAL REPORT



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CORPORATE PROFILE

Established in November 1950, Shanghai Commercial Bank (the '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, loans, remittances, foreign exchange, credit cards, securities trading, international banking, insurance services, gold services, RMB services, internet and mobile banking.

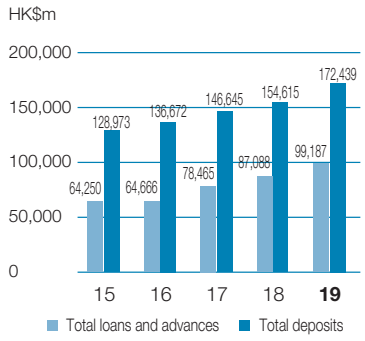
In addition to over 40 branches in Hong Kong, the Bank has a global network of overseas branches in San Francisco, Los Angeles, New York and London. In Mainland China, the Bank has established a branch presence in Shenzhen and Shanghai.

FIVE-YEAR FINANCIAL SUMMARY

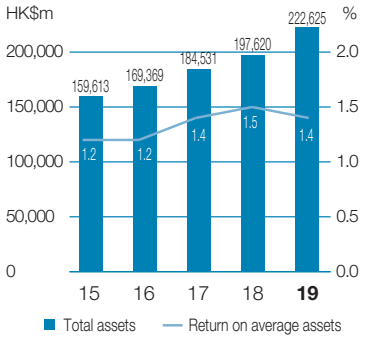
	2019	2018	2017	2016	2015
FOR THE YEAR (IN HK$ MILLION)					
Net interest income	**3,977**	3,608	3,100	2,637	2,481
Other operating income	**1,456**	1,348	1,504	1,222	1,147
Operating expenses	**1,649**	1,569	1,520	1,428	1,277
Operating profit	**3,723**	3,358	3,025	2,410	2,346
Profit before other comprehensive income attributable to equity holders	**3,016**	2,841	2,424	1,909	1,899
Dividend	**940**	940	940	940	940
AT YEAR END (IN HK$ MILLION)					
Shareholders' funds	**30,538**	27,821	25,468	24,308	22,572
Total assets	**222,625**	197,620	184,531	169,369	159,613
Total deposits*	**172,439**	154,615	146,645	136,672	128,973
Total loans and advances*	**99,187**	87,088	78,465	64,666	64,250
FINANCIAL RATIOS (IN PERCENTAGE %)					
Capital adequacy ratio	**19.5**	18.6	18.9	18.7	19.9
Average liquidity maintenance ratio	**53.3**	45.7	45.6	49.3	53.1
Loan to deposit ratio	**57.5**	56.3	53.5	47.3	49.8
Dividend payout ratio	**31.2**	33.1	38.8	49.2	49.5
Return on average assets	**1.4**	1.5	1.4	1.2	1.2

* The total deposit and total loan amounts are the principal amounts and do not include the relevant interest payable or receivable.

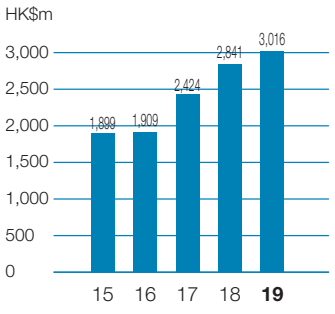
Total loans and advances and total deposits



Total assets and return on average assets



Profit before other comprehensive income attributable to equity holders



NOTICE OF ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that the Sixty-ninth Annual General Meeting of the Members of the Bank will be held at its Registered Office, Shanghai Commercial Bank Tower, 12 Queen's Road Central, Hong Kong on Wednesday, 22 April 2020 at 9:00 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 Auditor for the year ended 31 December 2019;
(2) To declare Dividend in respect of the year 2019;
(3) To re-elect Directors;
(4) To approve the payment of Directors' fees for the year ended 31 December 2019;
(5) To re-appoint Auditor and to authorise the Directors to fix their remuneration;
(6) To approve The Policy on the Acquisition and Disposal of Assets.

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 Wednesday, 15 April 2020 to Wednesday, 22 April 2020, both days inclusive.

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

Hong Kong, 17 January 2020

BOARD OF DIRECTORS



Front row from left to right

Ms. Maria Pui Man KIANG, Mr. Jafar Altaf AMIN, Mr. Stephen Ching Yen LEE, Mr. Hung-ching YUNG, Madam DAI Lanfang, Mr. JIN Yu

Back row from left to right

Mr. E. Michael FUNG, Mr. Johnson Mou Daid CHA, Dr. Richard LEE, Mr. David Sek-chi KWOK, Mr. Gordon Che Keung KWONG, Mr. CHEN Yih Pin, Mr. Charles Chi Man MA, Mr. John Con-sing YUNG

BOARD OF DIRECTORS (CONTINUED)

 # Stephen Ching Yen LEE
Chairman & Non-executive Director

^ David Sek-chi KWOK, *Fellow CB*
Managing Director & Chief Executive

 # Hung-ching YUNG, *JP*

*** Dr. Richard LEE**

*** Johnson Mou Daid CHA**

 # CHEN Yih Pin

*** Gordon Che Keung KWONG, *FCA***

 # DAI Lanfang

*** E. Michael FUNG**

 # JIN Yu

 # John Con-sing YUNG

 # Jafar Altaf AMIN

 # Maria Pui Man KIANG (appointed on 30 October 2019)

*** Charles Chi Man MA** (appointed on 30 October 2019)

^ Executive Director

* Independent Non-executive Directors

Non-executive Directors

MANAGEMENT

EXECUTIVES

Chief Executive	David Sek-chi KWOK
Deputy Chief Executives	Mong-ting CHONG Burton Chi-shan CHENG
Executive Vice Presidents	Wendy Li-chien WENG Ricky Chi-wai CHAN Edmund Kin-sang LAI Timothy Wai-tai LAW Clara Chor-hing FUNG Janet Hey CHONG Michael Yiu-wing FUNG Jenny Chui-yeung CHAU Christopher Lung-yuen YEONG Feng TIAN
Senior Vice Presidents	Stephen Wing-hing LAI Denis Man-heung WONG Steve Wai-fan TONG Tony Wai-man WAN Johnny Chung-pun CHOY Ka-shing YEUNG Wing-hung LAM

OVERSEAS BRANCHES

London Branch **Executive Vice President & Manager**	Jerome Chee-keong GOH
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

MAINLAND BRANCHES

Shenzhen Branch **Manager**	Vincent Chi-wing MAN
Shanghai Branch **Manager**	Lydia Li-ying CHEN

DIRECTORS

Mr. Stephen Ching Yen LEE

Aged 73. Chairman and Non-executive Director. Appointed a Director of the Bank in June 2004 and elected Chairman in April 2016. Deputy Chairman of The Shanghai Commercial & Savings Bank, Ltd., Taiwan, Managing Director of Great Malaysia Textile Investments Private Ltd., a Director of CapitaLand Ltd. and Temasek Holdings (Private) Ltd., and a member of the Council of Presidential Advisers of Singapore. Chairman of Singapore Airline Ltd. from 2006 to 2016.

Mr. David Sek-chi KWOK, Fellow CB

Aged 66. Managing Director and Chief Executive of the Bank since October 2007. Joined the Bank in October 1971. Appointed a Director in October 2001. Chairman of the Executive Committee of the Bank since November 2007. A Director of Bank of Shanghai Co., Ltd., Shanghai.

Mr. Hung-ching YUNG, JP

Aged 97. Appointed a Director of the Bank in March 1973. Managing Director of Nanyang Holdings Ltd. Chairman of The Shanghai Commercial & Savings Bank, Ltd., Taiwan, and Paofoong Insurance Company (Hong Kong) Ltd. A Director of The Wing On Enterprises, Ltd.

Dr. Richard LEE

Aged 82. Appointed a Director of the Bank in April 2001. Chairman of the Nomination Committee of the Bank since August 2017. Honorary Chairman of TAL Apparel Ltd.

Mr. Johnson Mou Daid CHA

Aged 68. Appointed a Director of the Bank in September 2001. Chairman of the Remuneration Committee of the Bank since August 2017. Director of Mingly Corporation, HKR International Ltd., Hanison Construction Holdings Ltd., China International Capital Corporation Ltd. and C.M. Capital Advisors (HK) Ltd. A board member of Qiu Shi Science & Technologies Foundation, a founding member of Moral Education Concern Group, a member of the Finance Committee and of the Council of The Hong Kong University of Science and Technology, and a member of the President's Global Advisory Council of Carnegie Mellon University.

Mr. CHEN Yih Pin

Aged 80. Alternate Director of the Bank since June 2004 and appointed a Director of the Bank in April 2006. Managing Director of The Shanghai Commercial & Savings Bank, Ltd., Taiwan.

Mr. Gordon Che Keung KWONG, FCA

Aged 70. 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 Chow Tai Fook Jewellery Group Ltd., NWS Holdings Ltd., Henderson Land Development Co. Ltd., China Power International Development Ltd. and Agile Group Holdings Ltd., as well as Lufax Holding Ltd., an associate of Ping An Insurance (Group) Company of China, Ltd.

Madam DAI Lanfang

Aged 65. Appointed a Director of the Bank in September 2015. Chairperson of Shanghai United International Investment Ltd. and Sino-US United MetLife Insurance Co., Ltd.

Mr. E. Michael FUNG

Aged 63. Appointed a Director of the Bank in December 2015. Chairman of the Risk Committee of the Bank since August 2017. Chairman and Principal of SouthBay Investment Advisors Ltd. An Independent Non-executive Director of Dickson Concepts (International) Ltd. A member of the Financial Services Development Council, Hong Kong from January 2013 to January 2017.

Mr. JIN Yu

Aged 55. Appointed a Director of the Bank in January 2016. Chairman of Bank of Shanghai Co., Ltd., Shanghai. A Director of Shanghai United International Investment Ltd.

Mr. John Con-sing YUNG

Aged 51. Alternate Director of the Bank since March 2013 and appointed a Director of the Bank in May 2016. Director, Executive Vice President and Chief Information Officer of The Shanghai Commercial & Savings Bank, Ltd., Taiwan. A Director of Nanyang Holdings Ltd. and AMK Microfinance Institutions Plc.

Mr. Jafar Altaf AMIN

Aged 47. Appointed a Director of the Bank in October 2018. Executive Vice President, Regional President and Head of Corporate & Investment Banking, Asia Pacific, Wells Fargo & Company. A Director of Wells Fargo International Banking Corporation, Wells Fargo Securities Asia Ltd. and Wells Fargo Securities (Japan) Co., Ltd.

Ms. Maria Pui Man KIANG

Aged 54. Appointed a Director of the Bank in October 2019. Assistant General Counsel, Asia Pacific, Legal Department of Wells Fargo Bank N.A. Solicitor of HKSAR and New South Wales, Australia.

Mr. Charles Chi Man MA

Aged 72. Appointed a Director of the Bank in October 2019. Consultant of mReferral Corporation (HK) Ltd. Former chief executive of China Construction Bank (Asia) Corporation Ltd., Macau Chinese Bank Ltd. and Bank of Shanghai (Hong Kong) Ltd.

SENIOR MANAGEMENT

Mr. David Sek-chi KWOK

(Biographical details are set out on page 8)

Mr. Mong-ting CHONG

Aged 57. Deputy Chief Executive, Chief Risk Officer. Joined the Bank in October 2015.

Mr. Burton Chi-shan CHENG

Aged 58. Deputy Chief Executive, Chief of Information Technology & Operations. Rejoined the Bank in August 1996.

Ms. Wendy Li-chien WENG

Aged 50. Executive Vice President, Chief Financial Controller. Joined the Bank in May 2012.

Mr. Ricky Chi-wai CHAN

Aged 48. Executive Vice President, Chief of Traditional Products. Joined the Bank in February 2014.

Mr. Edmund Kin-sang LAI

Aged 59. Executive Vice President, Chief of Treasury. Joined the Bank in December 2014.

Mr. Timothy Wai-tai LAW

Aged 43. Deputy Chief Risk Officer & Chief of Legal & Compliance. Joined the Bank in May 2016.

Ms. Clara Chor-hing FUNG

Aged 58. Executive Vice President, Chief of Human Resources. Joined the Bank in August 2016.

Ms. Janet Hey CHONG

Aged 50. Executive Vice President, Chief of Wealth Management. Joined the Bank in May 2017.

Mr. Michael Yiu-wing FUNG

Aged 62. Executive Vice President, Chief Auditor. Joined the Bank in September 1982.

Mr. Jerome Chee-keong GOH

Aged 47. Executive Vice President & Manager of London Branch. Joined the Bank in November 2013.

Mr. Christopher Lung-yuen YEONG

Aged 58. Deputy Chief Risk Officer & Head of Risks. Joined the Bank in December 2015.

Ms. Feng TIAN

Aged 45. Executive Vice President, Chief Lending Officer, U.S. Branches. Joined the Bank in August 2018.

The Bank continues to focus on advancing digital solutions for customer experiences and upgrade the branches for offering one-stop services to better meet customer expectations.

本行致力數字化發展以提升客戶體驗，亦繼續優化分行網絡，在一站式服務上更能達致客戶期望。











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We collaborate with The Hong Kong Mortgage Corporation Limited in the offerings of Reverse Mortgage Programme, Policy Reverse Mortgage Programme and SME Financing Guarantee Scheme; and HKMC Annuity Limited for the HKMC Annuity Plan.

我們與香港按揭證券有限公司合作無間，為推動安老按揭計劃、保單逆按計劃及中小企融資擔保計劃等而努力；同時亦與香港年金有限公司一起推動香港年金計劃。











2019 marked the twentieth anniversary of the Tri-bank Strategic Alliance, recollecting many accomplishments and recognitions built upon the founding motto "三地上銀，一心為您" while mapping the roadmap and setting initiatives for the future.

2019年為三地上海銀行策略聯盟二十周年，憑藉「三地上銀，一心為您」宗旨，聚力開拓，邁向國際，攜手並進，創造可能。







2000 - 2019
Conference Themes 歷屆主題

2019	繼往開來	順勢而為	創造可能
2018	聚力開拓	行穩致遠	攜手共贏
2017	匯聚優勢	智慧創新	價值共享
2016	融和開通	多元網絡	傳承創新
2015	創智未來	創新協同	創優共進
2014	創新領航	精進聯盟	集富共榮
2013	融智立新	創建品牌	跨境共贏
2012	創新驅動	共謀發展	攜手並進
2011	合作創新	通路造富	全球發展
2010	互動參與	長遠發展	邁向國際
2009	融匯才智	互惠共榮	創贏未來
2008	同心協力	創新價值	拓展商機
2007	合作無間	迸發創意	共建佳績
2006	開拓創新	融通智慧	合作共贏
2005	務實創新	優勢互補	掌握契機
2004	緊密合作	突顯聯盟	再創商機
2003	乘勢而上	加強合作	共謀發展
2002	加強交流	促進合作	共創三贏
2001	總結經驗	展望未來	再創商機
2000	迎接入世	加強合作	共同發展

QR codes for 2019 conference highlights
重溫二十屆研討會片段

We are an understanding partner aiming at providing customised solutions to our valued customers with personalised service.

我們團隊憑「聆聽、了解、支持」為尊貴客戶提供適切的理財及業務發展方案。





Daniel & Co.
瑞華行





Taste of Asia Group Limited
亞洲國際餐飲集團有限公司





Alpha Appliances Limited
第一電業有限公司





Zhongsheng Group Holdings Limited
中升集團控股有限公司





Wei Yit Vacuum Flask Manufactory Limited (CAMEL) & Camlux Hotel
唯一冷熱水壺廠有限公司（駱駝牌）及君立酒店





Dr. Kong Footcare Limited

As a responsible corporate citizen, the Bank together with the staff continue to partner with charitable organisations and participate in their volunteering activities, including:

作為負責任的企業，我們一直與慈善團體合作，參與各種義工活動，包括：

- Shanghai Commercial Pok Oi Cycle for Millions 2019 and Pok Oi Old Master Q Hong Kong Charity Run
- Po Leung Kuk Charity Run and Mooncake Workshop with Elderly
- The Community Chest's Walk for Millions
- Shanghai Commercial Silver Lining Charity Walk
- AVS Run & Walk for Volunteering 2019
- Heep Hong Society Challenge Day

- 上海商業博愛單車百萬行2019 及博愛老夫子香港慈善跑
- 保良局慈善跑 及 愛心月餅賀中秋
- 公益金百萬行
- 上海商業雲彩行動慈善步行
- 義務工作發展局義跑義行2019
- 協康會共融歷奇挑戰營







We take care of our staff, foster a corporate culture with seven core values, support work-life balance and encourage participation in different sports and recreational activities.

我們關愛員工，培植企業文化及七大核心價值，支持工作與生活平衡，鼓勵員工參與各種體育及康樂活動。











With some notable themes such as US-China trade tensions and Brexit carrying over from the previous year, certain events and conditions that arose in 2019 had also materially impacted our business environment. Hong Kong entered an unprecedented and protracted period of socio-political unrest, leading to downgrades for the territory by credit-rating agencies. Interest rate cuts by the US Federal Reserve had effectively reversed the increases in 2018, and the appearance of inverted US yield curves in the middle of 2019 highlighted recessionary concerns. Meanwhile, the Bank continued to execute its Five-year Plan for sustained steady growth into the future, maintained the credit ratings, and reasonably performed well amid the challenging operating circumstances.

Review of Operations

We are pleased to announce that the Bank delivered yet another year of record performance, with consolidated profit after tax for 2019 increased by HK$176 million from 2018, or 6.2%, to reach a new high of HK$3,022 million. The Bank recorded strong growth in net interest income, as well as in corporate fee and foreign exchange income. However, fee contribution from our securities, investment products and life insurance businesses declined year-on-year largely due to unfavourable investment sentiment.

Total comprehensive income attributable to equity holders for the year ended 31 December 2019 increased by 10.9% to HK$3,663 million, benefitted from the mark-to-market valuation of our debt securities portfolio and equity investments. On a year-on-year basis, total loans and advances increased by 13.9%, total customer deposits grew by 11.5%, and loan-to-deposit ratio thus rose 2%-points to 58% at the end of 2019 from that of 2018, while the impaired loan ratio improved to 0.57%. Net interest income increased by 10.2%, mainly due to loan and asset growth; yet net interest margin had slightly narrowed by two basis points to 2.01% for 2019. Impacted by the reduced contribution from our securities, investment products and life insurance businesses, overall fee and commission income stayed flat year-on-year.

The average yearly cost-to-income ratio improved to 30%, from 32% for 2018, mainly due to strong growth in operating income, and the relatively mild increase of 5.1% in operating expenses largely resulting from our continued investment in manpower resources to increase efficiency.

Total assets at the end of 2019 amounted to HK$223 billion, representing an increase of 12.7% or HK$25 billion, compared to that at the end of 2018. Returns on average total assets and average equity for the year were 1.4% and 10.3% respectively. Capital adequacy ratio was 19.5% at the end of 2019 and liquidity maintenance ratio averaged at 53.3% for the year, both at comfortable levels. In January 2019, we successfully launched the second issuance of our Tier-2 subordinated notes for US$300 million to support the planned growth of the Bank's operations and strengthen the capital base. The Bank continuously and consistently maintains a prudent and robust asset and liability management approach to enable our capital and liquidity levels meeting both regulatory requirements and business growth objectives.

Business Strategies

Entering into our 70th year of operation, we carry on with our organically-driven strategy and business expansion journey, focusing on our mainstay positions in corporate and Small-and-Medium sized Enterprises ("SMEs"), equipped with a comprehensive range of products and services covering corporate, commercial, retail and investments, and benefited from our network with international and cross-border presence, through branches in London, San Francisco, Los Angeles and New York, as well as Shenzhen and Shanghai, in addition to and complementing a well-entrenched footprint throughout Hong Kong.

We emphasize on serving the local community, particularly in maintaining long-standing customer relationships with personalized service, providing customized solutions to support the SMEs in Hong Kong, leveraging on overseas and cross-regional capabilities to help customers expand business interests and invest internationally while also offering products like the Reverse Mortgage Programme and Policy Reverse Mortgage Programme to the community.

Ongoing is our investment in resources to strengthen both business as well as compliance and risk functions in terms of systems and manpower, together with investment in digital banking and IT initiatives to support the growing business and enhance customer experience and operational efficiency. Following the launch of our new Corporate Internet Banking (CIB) platform, we rolled out biometric authentication for our Shacom Pay mobile application, and more offerings are in the pipeline to keep in pace with market developments in fintech and enhance customer convenience.

Our tri-bank strategic alliance with The Shanghai Commercial & Savings Bank, Ltd. in Taiwan and Bank of Shanghai in Mainland China marked its 20th anniversary. The three banks will continue reinforcing the ties and to forge new business collaboration for 2020 in servicing the customers and helping them to expand.

Sustainability and Social Responsibility

As a responsible corporate citizen, we continued to give back through our corporate social responsibility initiatives and programmes. Throughout the year, we reached out to the wider community by supporting activities organized by charitable organizations through fundraising, sponsorships and donations. Our staff actively volunteered in various activities for the children, the elderly and the underprivileged. Growing young talents is a key focus area of our community investment. In addition to scholarships for local universities and tertiary institutions, the Bank offered internship opportunities to students for gaining practical work experience, developing their skills, and acquiring better insights into the banking sector. The Bank will continue to work in close partnership with different organizations to generate positive community impact.

Bank Culture

The Bank's Culture Reform, in the third year of the transformation journey, remains a top agenda in our business strategy. From 2017 onwards, the Bank initiated a series of programmes on building the attitudes and goals for our staff in line with the Bank's mottos, vision and mission. In 2019, we had embedded our values and beliefs in our recruiting, interviewing, on-boarding and promotion processes as well as development activities. We focused on engaging employees throughout the Bank with what these values mean in practice. We encouraged positive behaviour via recognition programmes, incorporation of values and beliefs in policies, procedures and processes. Team building activities across the Bank aim to encourage teamwork, collaboration, and respect, reinforcing the need for alignment and change, identifying opportunities to drive business performance, providing support to leaders on managing the change journey and creating new insights and self-awareness in leadership and collaboration.

Looking Ahead

Though most stock markets ended 2019 on the upside, and despite positive developments such as the Phase 1 trade deal signed between the US and China and the US removal of the currency manipulator designation of China in early 2020, uncertainties persist going forward, including continued US-China trade negotiations, the social situation in Hong Kong and the coronavirus outbreak. We predict ongoing impact to be seen not only on the retail and catering sectors, tourism, and hotels, but also on property development, construction contractors, import and export businesses to varying degrees. Given the uncertainty associated with the evolving nature of the situation, it would be premature to fully evaluate the impact and estimate the timing of the recovery at this moment. However, the Bank has always been prudent and focused on protecting the asset quality, maintaining stability and safeguarding our tradition and strength. As a responsible member of the community and being a mainstay commercial bank in providing devoted personalized banking services to corporate and SME customers, we deeply understand the financial difficulties and cash flow pressures faced by them. We have accordingly introduced temporary relief measures to help our customers in overcoming this challenging period.

On behalf of the Board, we would like to welcome the new members who both joined on 30 October 2019: Ms. Maria Pui Man KIANG, Assistant General Counsel, Asia Pacific, Legal Department of Wells Fargo Bank N.A., as Non-executive Director and shareholder's representative, and Mr. Charles Chi Man MA, a veteran banker, as our new Independent Non-executive Director. We look forward to their wise counsel and advice.

We also wish to express our sincere appreciation to our Board of Directors for their guidance and strong leadership, to our loyal customers for their trust and continued support, and to all our staff for their hard work and dedication. There would be challenges ahead and we look forward to 2020 with guarded optimism.

Stephen Ching Yen LEE
Chairman

David Sek-chi KWOK
Managing Director & Chief Executive

Hong Kong, 18 March 2020

The Directors have pleasure in presenting their report together with the audited consolidated financial statements for the year ended 31 December 2019.

Principal activities

Shanghai Commercial Bank Limited (the "Bank") and its subsidiaries (the "Group") are engaged in the provision of banking and related financial services. The principal activities of the Bank's subsidiaries are set out in Note 24 to the consolidated financial statements.

Business review

A fair review of the business and a discussion and analysis of the performance of the Group for the year ended 31 December 2019, particulars of important events affecting the Group that have occurred since the end of the year 2019 (if any) as well as an indication of likely future development in the business of the Group are provided in the Message to Shareholders of this Annual Report.

Description of the principal risks and uncertainties facing the Group can be found in the Message to Shareholders and in Note 3 to the consolidated financial statements for the year ended 31 December 2019.

For the Group's environmental policy, the Bank has generally adopted the theme of "Reduce, Reuse and Recycle" as its principle of environmental protection. Involvement with our stakeholders is believed to be a key to success of implementation. For business operations, measures such as e-statement instead of paper-statement, use of energy efficient equipment, promotion of energy saving practices in office have been advocated for years so as to reduce paper and power consumption. For giving back to the community, we have encouraged our staff to participate in various environmental friendly activities in order to promote their awareness in this regard. The Bank, as a responsible corporate citizen, has striven to take different initiatives in making contributions to the environmental protection for the community and in addressing the growing concerns over the environmental issues and climate change affecting the rest of the world.

Compliance with relevant laws and regulations which have a significant impact on the Group can be found throughout this Annual Report, particularly in the Corporate Governance Report.

In addition, relationships with the key stakeholders that have a significant impact on the Group can be found in the Message to Shareholders and the Corporate Governance Report.

Results and appropriations

The profits of the Group for the year ended 31 December 2019 are set out in the consolidated statement of profit or loss on page 47 of this Annual Report.

The Directors recommend the payment of a final dividend of HK$47 (2018: HK$47) per ordinary share totalling HK$940 million (2018: HK$940 million).

Company status

By an ordinary resolution passed on 1 November 2017, the Bank has been converted from a private company to a public company.

Share capital

The Bank did not issue any new share during the year. Details of the share capital of the Bank during the year are set out in Note 33 to the consolidated financial statements.

Debentures issued

So far up to the year ended 31 December 2019, the Bank had issued two tranches of Tier 2 subordinated notes of which the first issuance of US$250 million maturing in 2027 and the second issuance of US$300 million maturing in 2029, both being traded on The Stock Exchange of Hong Kong Limited. The funds raised are used to strengthen the capital base and support the business growth of the Bank.

Equity-linked agreements

During the year ended 31 December 2019, the Bank did not enter into any equity-linked agreement.

Donations

Charitable and other donations made by the Group during the year amounted to HK$10,641,000 (2018: HK$9,875,000).

Directors

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

 # Hung-ching YUNG

*** Dr. Richard LEE**

*** Johnson Mou Daid CHA**

^ David Sek-chi KWOK

+ Stephen Ching Yen LEE

 # CHEN Yih Pin

*** Gordon Che Keung KWONG**

 # DAI Lanfang

*** E. Michael FUNG**

 # JIN Yu

 # John Con-sing YUNG

 # Jafar Altaf AMIN

 # Maria Pui Man KIANG (appointed on 30 October 2019)

*** Charles Chi Man MA** (appointed on 30 October 2019)

^ Executive Director

\+ Non-executive Chairman

\# Non-executive Director

* Independent Non-executive Director

In accordance with Article 104(A) of the Bank's Articles of Association, Messrs. Hung-ching YUNG, Stephen Ching Yen LEE, CHEN Yih Pin and John Con-sing YUNG shall retire by rotation at the forthcoming Annual General Meeting and, being eligible, offer themselves for re-election.

Furthermore, in accordance with Article 95 of the Bank's Articles of Association, Ms. Maria Pui Man KIANG and Mr. Charles Chi Man MA shall retire at the forthcoming Annual General Meeting and, being eligible, offer themselves for re-election.

Directors of subsidiaries

The names of all directors who have served on the boards of the subsidiaries of the Bank during the year and up to the date of this report are set out below:

Natural Person

Hung-ching YUNG, John Con-sing YUNG, David Sek-chi KWOK, Ricky Chi-wai CHAN, Timothy Kam-tim CHAN, Burton Chi-shan CHENG, CHENG Ming Ho, Janet Hey CHONG, Jerome Chee-keong GOH, Zachary Wing-kwong KWAN, Eric Wing-hong KO, Philip She-hoi LEE, LI Yiu Ki, Brenda Fen LEE, Riggs Kwok-ching TAM, Wendy Li-chien WENG, Philip Wing-cheong WONG, Sammy Tak-keung WONG, Sharon Kam-wing WONG, William Wai-leung WONG

Body Corporation

Right Honour Investments Limited, Shanghai Commercial Bank Limited

Directors' interests and short positions in shares, underlying shares and debentures

At no time during the year was the Bank, or any of its holding companies, subsidiaries or fellow subsidiaries a party to any arrangement to enable the Directors and the Chief Executive of the Bank (including their spouses and children under 18 years of age) to acquire benefits by means of the acquisition of any interests or short positions in the shares or underlying shares in, or debentures of, the Bank or any other body corporate.

Directors' interests in transactions, arrangements or contracts

No transaction, arrangement or contract of significance in relation to the Group's business to which the Bank, or any of its holding companies, subsidiaries or fellow subsidiaries was a party and in which a Director of the Bank or an entity connected with a Director had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year, except for a two-year contract between the Bank and Hanison Contractors Limited ("Hanison") for a sum of HK$452,880,000 commencing on 22 August 2019 relating to the redevelopment of the West Point Branch where Mr. Johnson M. D. Cha is a common director of the Bank and Hanison Construction Holdings Ltd., the holding company of Hanison.

Permitted indemnity provision

Pursuant to the Bank's Articles of Association, every Director or other officer of the Bank shall be entitled to be indemnified out of the assets of the Bank against all losses and liabilities (to the extent permitted by the Companies Ordinance) incurred by such Director or other officer in the execution of his/her duties or otherwise in relation thereto. Insurance cover has been arranged to indemnify the Directors and other officers of the Group.

Management contracts

Save for employment contracts, no contracts relating to the management and administration of the whole or any substantial part of the business of the Bank were entered into or subsisted during the year.

Compliance with the Banking (Disclosure) Rules

The Bank has complied with the disclosure requirements set out in the "Banking (Disclosure) Rules" and the "Guideline on the Application of the Banking (Disclosure) Rules" contained in the Supervisory Policy Manual issued by the Hong Kong Monetary Authority.

Compliance with the Corporate Governance Code

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

Auditor

The consolidated financial statements have been audited by PricewaterhouseCoopers who will retire at the forthcoming Annual General Meeting of the Bank and, being eligible, offer themselves for re-appointment.

On behalf of the Board
Stephen Ching Yen LEE
Chairman

Hong Kong, 18 March 2020

Shanghai Commercial Bank Limited (the "Bank") and its subsidiaries (the "Group") are committed to maintaining good corporate governance to safeguard the interests of the shareholders, depositors and other relevant stakeholders. The Bank is an authorized institution supervised by the Hong Kong Monetary Authority ("HKMA") under the Banking Ordinance. Throughout the year ended 31 December 2019, the Bank followed the module on "Corporate Governance of Locally Incorporated Authorized Institutions" of the Supervisory Policy Manual ("SPM CG-1") issued by the HKMA.

The Bank, after taking into consideration its particular circumstances as a non-listed public company, has also adopted the code provisions in the Corporate Governance Code (the "CG Code") as stated in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") that are relevant to the Bank. This Corporate Governance Report is prepared with reference to the CG Code.

Board of Directors

The Board has collective responsibility for promoting the long-term sustainability and success of the Bank by directing and supervising its affairs within a framework of prudent and effective controls. The Board takes into account the legitimate interests of shareholders, customers, employees and other relevant stakeholders.

The Board is responsible for providing strategic direction and overseeing the implementation of strategic objectives and goals by the Management. The Board has established Board-level specialized committees with clear delegation and formal terms of reference setting out the authorities, responsibilities and membership for the oversight of certain major functional areas. Each Board-level specialized committee, including the Executive Committee, Audit Committee, Nomination Committee, Remuneration Committee and Risk Committee, is provided with sufficient resources to perform its duties.

Chairman and Chief Executive

The roles of Chairman of the Board and Chief Executive are separate and are taken up by different persons.

The Chairman, Mr. Stephen Ching Yen LEE who is a Non-executive Director, is responsible for leading the Board and monitoring the overall effective functioning of the Board, as well as ensuring all key and appropriate issues are discussed by the Board in a timely manner.

The Chief Executive, Mr. David Sek-chi KWOK who is an Executive Director, is responsible for implementing the decisions, strategies and policies as established by the Board. The Chief Executive is also responsible for leading the Senior Management in running the day-to-day business and operations of the Bank as well as chairing the Executive Committee.

Board Composition

The Board comprises Directors with a variety of backgrounds and a diverse range of business, banking and professional expertise. The Board also has a well-balanced composition of Executive Director, Non-executive Directors and Independent Non-executive Directors ("INEDs") to ensure independence and objectivity of the decisions as well as robustness and impartiality of the Board's oversight of the Management.

The Board currently comprises fourteen Directors, including eight Non-executive Directors, one Executive Director and five INEDs whose biographical details are individually set out in the "Biographical Details of Directors and Senior Management" section of this Annual Report.

The Bank has received from each of the INEDs an annual confirmation of his independence which has also been assessed in accordance with the guidelines set out in Rule 3.13 of the Listing Rules as well as the factors outlined in HKMA's circular on "Empowerment of Independent Non-Executive Directors (INEDs) in the Banking Industry in Hong Kong" issued on 14 December 2016. The Board considers that all INEDs continue to be independent of the Management and free of any relationship that could materially interfere with the exercise of their independent judgment.

Among the eight Non-executive Directors of the Bank, Mr. Hung-ching YUNG is the grandfather of Mr. John Con-sing YUNG. Save as aforesaid, there is no relationship (including financial, business, family or other material/relevant relationship(s)) among Board members.

The Bank has maintained on its website (www.shacombank.com.hk) an updated List of Directors showing their roles and functions and whether they are INEDs.

Appointment and Re-election of Directors

The Board is empowered under the Articles to appoint any person as a Director either to fill a casual vacancy or as an addition to the Board. The Nomination Committee is responsible for reviewing any proposed appointment, mainly based on merits but also having due regard to the benefits of Board diversity, and making recommendation to the Board for consideration and approval. Pursuant to relevant requirements in the Banking Ordinance, consent from the HKMA for any new appointment is required and will also be sought.

All new Directors appointed by the Board are subject to re-election by shareholders of the Bank at the next annual general meeting after their appointments have become effective. There is no specified term of appointment for Non-executive Directors as provided under code provision A.4.1 of the CG Code. However, the Articles stipulate that at each annual general meeting one-third of the Directors (excluding the Executive Director holding the office as Chief Executive) who have been longest in office since their last election shall retire and be eligible for re-election.

Board Process

The Board meets regularly to formulate objectives, strategies, business plans and annual budgets and to assess the Bank's performance, position and prospects throughout the year. All Directors have unfettered access to board papers and related materials which are provided in a timely manner. The Corporate Secretary keeps the minutes of Board meetings.

Schedule for regular Board and Committee meetings in each year is made available to all Directors before the end of the preceding year to facilitate their attendance. Directors have demonstrated strong commitment in attending meetings over the years. All Directors are also given opportunities to propose matters in the meeting agenda. During the year, the Board held five physical meetings and the important matters discussed at Board meetings for the year included, among other things:

- half-yearly review of the 5-year plan for 2017-2021 and the outlook of the Bank for the years 2020-2025
- annual budget
- interim and annual financial statements, and the quarterly and half-year Consolidated Reporting Package of the Group for submission to the parent company, The Shanghai Commercial & Savings Bank, Ltd.
- appointment of Directors
- review of the report on board performance evaluation
- review of the directors' fees for Non-executive Directors and Independent Non-executive Directors
- appointment and oversight of senior management, and ensuring competent management being in place
- review of corporate grade structure and titles of the Bank
- Risk Appetite Statement
- half-yearly summary report on stress tests
- revised Terms of Reference of the Board, Executive Committee, Audit Committee, Risk Committee, Nomination Committee, Remuneration Committee and other management-level key specialized committees
- various significant policies and plans including but not limited to, Corporate Governance Policy, Business Continuity Plan and its Policy, Policy on Management Succession, Policy on Credit Risk Management for Treasury Operations, Capital Policy, Policy on Financial Statements Presentation and Disclosures, Policy on Liquidity Risk Management, Products and Services Governance Policy, Remuneration Policy, Recovery Plan, Strategic Risk Management Policy and subsidiary policies to the Credit Risk Policy, and etc.
- Internal Capital Adequacy Assessment Process
- setting up of portfolio limits on lending and matters relating to loan portfolio of the Bank
- Slavery and Human Trafficking Statement relating to the UK Modern Slavery Act 2015

To enable Board members to have a fair understanding and hence assessment of the Bank's performance, review of the main economic developments in Hong Kong is provided to Board members at each regular Board meeting in addition to regular financial and business reports.

The Bank has arranged directors and officers liability insurance cover to indemnify the Directors and other officers against any potential liability arising from the Bank's business activities to which such Directors and officers may be held liable.

Directors' Attendance Records

The attendance records of Board meetings and the Annual General Meeting ("AGM") during the year ended 31 December 2019 are set out in the following table:

	No. of meetings attended/No. of meetings held	
Non-executive Directors	Board	AGM
Mr. Stephen Ching Yen LEE – Chairman of the Board	5/5	1/1
Mr. Hung-ching YUNG	5/5	1/1
Mr. CHEN Yih Pin	5/5	1/1
Madam DAI Lanfang	5/5	1/1
Mr. JIN Yu	3/5	1/1
Mr. John Con-sing YUNG	5/5	1/1
Mr. Jafar Altaf AMIN	5/5	1/1
Ms. Maria Pui Man KIANG, appointed on 30 October 2019	2/2	N/A
Executive Director		
Mr. David Sek-chi KWOK – Managing Director & Chief Executive	5/5	1/1
Independent Non-executive Directors		
Dr. Richard LEE	5/5	1/1
Mr. Johnson Mou Daid CHA	5/5	1/1
Mr. Gordon Che Keung KWONG	5/5	1/1
Mr. E. Michael FUNG	5/5	1/1
Mr. Charles Chi Man MA, appointed effective from the close of the Board Meeting on 30 October 2019	1/1	N/A

Board Effectiveness

During the year ended 31 December 2019, the Board conducted an annual review of its effectiveness by way of a board performance evaluation questionnaire (the "Questionnaire") which was categorized into nine sections, consisting of (1) Board composition and skills; (2) Strategic orientation and risk management; (3) Board Committees; (4) Corporate culture, management development and succession; (5) Board meetings; (6) Performance management; (7) Communication with management; (8) Communication with shareholders, and (9) Director's self-evaluation. The overall feedback was positive. The performance of individual board members was satisfactory, and each of the Directors was willing and able to commit sufficient time, attention and efforts to fulfil their responsibilities. The results of the Questionnaire revealed that the Board and all the Board Committees continue to perform well.

Induction and training for Directors

Each newly appointed Director receives an information package on the scope of duties and obligations to be observed by a Director. Further, to enable the Directors to have a proper understanding of the Bank's operations and business, their responsibilities under applicable laws and regulations as well as the development trends in the industry, the Bank arranges and provides trainings and timely information to Directors on corporate structure and profile, board composition, senior management profile, Anti-money Laundering, legal, regulatory and compliance updates, changes in accounting standards, and etc. Directors are also informed of and encouraged to attend outside talks, trainings and seminars organized by professional bodies at the Bank's expenses to enrich their knowledge in discharging their duties as a director. The training attendance records of the Directors for each year are maintained by the Corporate Secretary.

The key areas of training received by current Directors of the Bank to update and develop their skills and knowledge during the year 2019 are summarized as follows:

	Training areas	
Directors	**Regulatory updates**	**Events/ Seminars/ Conferences relevant to the Bank's business and corporate governance**
Non-executive Directors		
Mr. Stephen Ching Yen LEE	✓	✓
Mr. Hung-ching YUNG	✓	✓
Mr. CHEN Yih Pin	✓	✓
Madam DAI Lanfang	✓	✓
Mr. JIN Yu	✓	✓
Mr. John Con-sing YUNG	✓	✓
Mr. Jafar Altaf AMIN	✓	✓
Ms. Maria Pui Man KIANG	✓	✓
Executive Director		
Mr. David Sek-chi KWOK	✓	✓
Independent Non-executive Directors		
Dr. Richard LEE	✓	✓
Mr. Johnson Mou Daid CHA	✓	✓
Mr. Gordon Che Keung KWONG	✓	✓
Mr. E. Michael FUNG	✓	✓
Mr. Charles Chi Man MA	✓	✓

Guiding principles on Board Diversity

The Bank recognizes and embraces the benefits of having a diverse Board to enhance the quality of its performance. With a view to achieving a sustainable and balanced business, the Bank sees increasing diversity at the Board level as an essential element in supporting the attainment of its strategic objectives and its sustainable development. In designing the Board's composition, board diversity is being considered from a number of aspects, including but not limited to gender, age, cultural and educational background, ethnicity, professional experience, skills, knowledge and length of service. All Board appointments will be based on meritocracy, and candidates will be considered against objective criteria, having due regard to the benefits of the Board diversity.

These guiding principles are not intended to, and do not, either enlarge or diminish the responsibilities of the Directors under the Articles of Association and such other relevant laws, rules, regulations, codes, guidelines, practice notes and circulars, but to serve for Directors to take appropriate actions to achieve the aims of Board diversity as outlined above. The Board will review and, where appropriate, revise from time to time the principles in light of experience, evolving standards of corporate governance and any other changing circumstances.

Board-level Specialized Committees

The Board has established five Committees, namely, the Executive Committee, Audit Committee, Remuneration Committee, Nomination Committee and Risk Committee, to assist it in carrying out its responsibilities. Each of these Committees has specific written terms of reference, which set out in detail their authorities and responsibilities.

Executive Committee

The Executive Committee operates as a general management committee under the delegated authority of the Board to oversee the management and day-to-day running of the Bank in accordance with its terms of reference and such other policies and directives as the Board may determine from time to time.

The Executive Committee provides regular updates to the Board on the business performance of the Bank by way of presenting monthly reports on financial performance, quarterly progress reports on budgets, and half-yearly progress reports on strategic and business plans. Minutes of monthly meetings of the Executive Committee are sent to all Directors for review.

The Executive Committee currently consists of four members including one Executive Director and three Non-executive Directors who are representatives from each of the three substantial shareholders, with the Executive Director being appointed as Chairman of the Committee.

A total of twelve monthly meetings of the Executive Committee were held in 2019 and attendance records thereof are set out below:

	No. of meetings attended/No. of meetings held
Mr. David Sek-chi KWOK – Chairman	12/12
Mr. Hung-ching YUNG	12/12
Madam DAI Lanfang	12/12
Mr. Jafar Altaf AMIN	12/12

Audit Committee

The Audit Committee considers the nature and scope of audit reviews and reviews the Bank's financial statements, the findings of both internal and external auditors and the effectiveness of the internal control systems of the Bank. During the year, the Board has delegated its corporate governance functions as set out in code provision D.3.1 of the CG Code to the Audit Committee. The Bank has made available on its website the latest Terms of Reference of the Audit Committee.

The Audit Committee currently consists of three members, including one Non-executive Director and two INEDs, one of whom is the Chairman of the Committee who possesses appropriate accounting qualifications and related financial management expertise.

The Audit Committee held four meetings in 2019 with the Bank's executives including the Chief Executive, Chief Risk Officer, Chief Financial Controller, Chief Auditor and representatives from the Bank's external auditor in attendance. The Audit Committee also met with the representatives of the Bank's external auditor in the absence of the Senior Management in accordance with its Terms of Reference.

Attendance records of the Audit Committee are set out below:

	No. of meetings attended/No. of meetings held
Mr. Gordon Che Keung KWONG – Chairman	4/4
Mr. John Con-sing YUNG	4/4
Mr. E. Michael FUNG	4/4

The following is a summary of the major items covered by the Audit Committee for the year:

- Review and making recommendations to the Board for approval of the Terms of Reference of the Audit Committee
- Review and making recommendations to the Board for approval of (i) the 2018 audited financial statements of the Group and the 2019 interim financial disclosure statement, and (ii) the quarterly and half-year Consolidated Reporting Package of the Group for submission to the parent company, The Shanghai Commercial & Savings Bank, Ltd.
- Review of the remuneration and terms of engagement of the external auditor and making recommendations to the Board for approval of their re-appointment
- Review of the adequacy of resources, staff qualifications, experience and training programmes of the financial reporting function
- Review of the adequacy of resources, effectiveness and the annual budget of the Internal Audit function and the performance of the Chief Auditor
- Review and approval of the Policy on Non-audit Services, review of the non-audit services provided by the external auditor and other professional firms on a semi-annual basis
- Review of the independence, objectivity and effectiveness of the audit process of the external auditor and discussion of their audit work
- Review of the independent review of the Internal Audit Function of the Bank conducted by external professional firm
- Review and approval of the Internal Audit Charter and Internal Audit Policy and Procedures, and the internal audit plan
- Review of the internal audit report, including findings and recommendations
- Review and approval of the compliance plan for the year 2019
- Review of compliance report on a regular basis
- Review of the annual report of whistleblowing cases, if any
- Review of the summary report from the Legal and Compliance Division of the Group on the HKMA examinations and regulatory concerns as well as management's actions in implementing the HKMA's recommendations
- Review of the Group's financial and accounting policies and practices and making recommendations to the Board for approval of, including but not limited to, Corporate Governance Policy and Policy on Financial Statements Presentation and Disclosures
- Review of the highlights of major new accounting and financial reporting standards and guidance issued by the Hong Kong Institute of Certified Public Accountants as well as impact to the Group on their adoption

Remuneration Committee

The Remuneration Committee oversees the implementation of a sound remuneration policy including recommending to the Board on the remuneration of the Directors and Senior Management of the Bank, with the assistance of independent professional consultants where appropriate. No Director or any of their associates is involved in deciding his/her own remuneration. The Bank has made available on its website the latest Terms of Reference of the Remuneration Committee.

The remuneration policy of the Group is reviewed by the Remuneration Committee and approved by the Board. Details of remuneration for Senior Management and key personnel of the Group during the year are disclosed in Note 14 of "Regulatory Disclosures" of this Annual Report in accordance with Banking (Disclosure) Rules with the exception of details of remuneration by band for the Senior Management. The Board currently considers such disclosure inappropriate for the time being but subject to review whenever necessary.

The Remuneration Committee currently consists of three members including one Non-executive Director and two INEDs with one being appointed as Chairman of the Committee.

The Remuneration Committee held two meetings in 2019 with the Bank's Chief Executive and Chief of Human Resources in attendance and attendance records thereof are set out below:

	No. of meetings attended/No. of meetings held
Mr. Johnson Mou Daid CHA – Chairman	2/2
Mr. Hung-ching YUNG	2/2
Dr. Richard LEE	2/2

The following is a summary of the major items covered by the Remuneration Committee for the year:

- Review and making recommendations to the Board for approval of the Terms of Reference of Remuneration Committee and Remuneration Policy
- Review and making recommendations to the Board for approval of directors' fees for Non-executive Directors and Independent Non-executive Directors, the remuneration packages of Senior Management and key personnel of the Bank
- Review of culture-related matters of the Bank

Nomination Committee

The Nomination Committee considers the structure, size and composition of the Board and is responsible for recommending to the Board on matters relevant to appointments, re-appointments, removal and succession planning of Directors and Senior Management in accordance with the Bank's relevant policies, guidelines and business strategies. The Bank has made available on its website the latest Terms of Reference of the Nomination Committee.

The Nomination Committee currently consists of three members including one Non-executive Director and two INEDs with one being appointed as Chairman of the Committee.

The Nomination Committee held three meetings in 2019 with the Bank's Chief Executive and Chief of Human Resources in attendance. Attendance records of the Nomination Committee are set out below:

	No. of meetings attended/No. of meetings held
Dr. Richard LEE – Chairman	3/3
Mr. Stephen Ching Yen LEE	3/3
Mr. Johnson Mou Daid CHA	3/3

The following is a summary of the major items covered by the Nomination Committee for the year:

- Review and making recommendations to the Board for approval of the Terms of Reference of the Nomination Committee
- Review of the structure, size and composition of the Board and its Board-level specialized committees
- Review and making recommendations to the Board for approval of nomination and re-appointment of Directors
- Review the report on board performance evaluation
- Review and making recommendations to the Board for approval of the corporate grade structure and titles of the Bank, the senior management organization structure, appointment of and promotion to senior management, Policy on Management Succession and the succession plan of the Bank

Risk Committee

The Risk Committee oversees and reviews the Bank's high-level risk related matters and makes recommendations to the Board on risk management strategies as well as the risk tolerance and risk appetite of the Bank. The Bank has made available on its website the latest Terms of Reference of the Risk Committee.

The Risk Committee currently consists of three members who are all INEDs, with one being appointed as Chairman of the Committee.

The Risk Committee held four meetings in 2019 with the Bank's executives in attendance, including the Chief Executive, Chief Risk Officer and Chief Financial Controller. The Risk Committee also met with the Chief Risk Officer in the absence of the Executive Director and Senior Management in accordance with its Terms of Reference.

The attendance records of the Risk Committee are set out below:

	No. of meetings attended/No. of meetings held
Mr. E. Michael FUNG – Chairman	4/4
Mr. Johnson Mou Daid CHA	3/4
Mr. Gordon Che Keung KWONG	4/4

The following is a summary of the major items covered by the Risk Committee for the year:

- Review and making recommendations to the Board for approval of the Terms of Reference of the Risk Committee, Asset and Liability Committee, Credit Committee and Operational Risk Management Committee
- Review of the quarterly report on risk exposures and risk management activities of the Bank
- Review of the Bank's 2019/2020 Supervisor-driven Stress Test
- Review and making recommendations to the Board for approval of the Risk Appetite Statement, Internal Capital Adequacy Assessment Process, Group Recovery Plan and Slavery and Human Trafficking Statement relating to the UK Modern Slavery Act 2015
- Review and making recommendations to the Board for approval of the high-level risk-related policies of the Bank including but not limited to, Capital Policy, Policy on Liquidity Risk Management, Products and Services Governance Policy, Strategic Risk Management Policy
- Review and approval of the Customer Acceptance and Anti-money Laundering and Counter-terrorist Financing Policy, Sanctions Policy, Complaint Handling Guideline, Information Technology Policy, Information Security Policy, Operational Risk Management Policy, Internal Capital Adequacy Assessment Process (ICAAP) – Stress-testing Methodology, Fair Valuation Policy for Financial Instruments, Stress-testing Policy and Whistleblowing Policy, and etc.
- Review and approval of the internal capital targets and internal leverage ratio targets of the Group for 2020 and onwards
- Review of reports on anti-money laundering related matters
- Review of material regulatory requirements and examination reports from HKMA and the follow-up actions taken by the Management
- Review of reports on the independent assessment of the Bank's information and technology system related to its emerging and existing e-banking services

Delegation by the Board

In addition to the Executive Committee, Audit Committee, Remuneration Committee, Nomination Committee and Risk Committee, the Board has also established the following management-level key specialized committees, each of which has specific written Terms of Reference in order to ensure that they discharge their functions properly and that their meeting minutes are sent to all Directors for review.

Information on these committees is set out below:

Asset and Liability Committee

The Asset and Liability Committee meets at least monthly to deal with issues related to the market, interest rate and liquidity risks of the Bank and reports directly to the Executive Committee and Risk Committee.

The members of the Asset and Liability Committee are the Chief Executive (Chairman), Deputy Chief Executive(s), Chief Risk Officer and Division Chiefs/Heads responsible for compliance, risk management, financial control, treasury, corporate banking, mainland and overseas branches, branch operations, regulated and traditional products and human resources of the Bank.

Credit Committee

The Credit Committee meets at least monthly to deal with all credit risk-related issues of the Group such as establishing credit policies, monitoring loan portfolio quality, ensuring compliance with statutory and internal lending limits, evaluating credit applications, making credit decisions, and etc. The Credit Committee reports directly to the Executive Committee and Risk Committee.

The members of the Credit Committee are the Chief Executive (Chairman), Deputy Chief Executive(s), Chief Risk Officer, Head of Credit, Head of Credit Appraisal, Head of Credit Control and the Division Chiefs/Heads responsible for treasury, corporate banking, mainland and overseas branches, branch operations, regulated and traditional products of the Bank.

Operational Risk Management Committee

The Operational Risk Management Committee meets at least once every two months to deal with major aspects of the Bank's operational risk as a distinct category of risk and to define the operational risk strategy within the Bank's overall business objectives. The Operational Risk Management Committee reports directly to the Executive Committee and Risk Committee.

The members of the Operational Risk Management Committee are the Chief Executive (Chairman), Deputy Chief Executive(s), Chief Risk Officer and Division Chiefs/Heads responsible for legal, compliance, risk management, treasury, corporate banking, mainland and overseas branches, branch operations, information technology, operations centres, regulated and traditional products, human resources and property/bank premises of the Bank.

Directors' Securities Transactions

The Board has not adopted code provision A.6.4 of the CG Code in relation to the setting up of written guidelines for Directors and relevant employees in respect of their dealings in the Bank's securities as the Bank's shares are not publicly listed.

Accountability and Audit

Directors' Responsibility in relation to Financial Reporting

The Directors are responsible for presenting a balanced, clear and comprehensive assessment of the Bank's performance, position and prospects. As such, the Management assists the Directors to discharge their duties through the submission of monthly financial and business updates of the Bank. Representatives of the Senior Management of core business lines and control functions are invited to attend Board/Board Committee meetings as appropriate to provide sufficient explanation and information, critical insights and analyses of the Bank's affairs relating to their areas of expertise to the Directors.

The Directors acknowledge their responsibility for preparing the financial statements of the Group in accordance with statutory requirements and applicable accounting standards. The Group's annual and interim results are reviewed by the Audit Committee and announced in a timely manner. As at 31 December 2019, the Directors of the Bank were not aware of any material uncertainties relating to events which may cast significant doubt upon the Group's ability to continue as a going concern. Accordingly, the Group's financial statements have been prepared on a going concern basis.

The statement of the Bank's external auditor concerning its reporting responsibilities on the Bank's consolidated financial statements and the key audit matters identified during the course of the audit are set out in the Independent Auditor's Report attached to the Bank's 2019 Consolidated Financial Statements.

Risk Management and Internal Controls

The Board is responsible for overseeing risk management and internal control systems including financial, operational and compliance controls and reviewing their effectiveness to achieve business objectives and safeguard shareholders' interests and the Group's assets. Management has to provide a confirmation to the Board on the effectiveness of these systems.

Well-established organizational structure and comprehensive policies and procedures are in place for ensuring effective checks and balances; managing possible gaps in achieving business objectives; safeguarding assets against unauthorized use or disposition; maintaining proper accounting records and ensuring the reliability of financial information used within the business or for publication. The procedures, providing reasonable but not absolute assurance against material errors, losses or fraud, are designed to ensure compliance with applicable laws, rules and regulations.

The Group has set up specialized committees and related departments responsible for identifying, assessing and managing key risks facing the Bank including credit risk, market risk, liquidity risk, operational risk, interest rate risk, strategic risk, legal, regulatory and compliance risk, technology risk and reputational risk through implementing appropriate policies and procedures. Periodic reports on risk exposure and risk management activities are submitted to the Executive Committee and Risk Committee through the Asset and Liability Committee, Credit Committee and Operational Risk Management Committee and ultimately to the Board for monitoring the risk management and internal control systems. The Group's risk management strategies, risk tolerance and risk appetite are reviewed by the Risk Committee and approved by the Board.

The Audit Committee reviews the external auditor's reports in connection with the annual audit and the recommendations on internal control arising therefrom, as well as their report on review of interim financial information.

Risk Management and Internal Controls (Continued)

In view of the fact that banking is one of the highly regulated industries in Hong Kong and is subject to various laws and regulations including but not limited to the Banking Ordinance, Anti-Money Laundering and Counter-Terrorist Financing Ordinance, Personal Data (Privacy) Ordinance, Foreign Account Tax Compliance Act, UK Modern Slavery Act 2015 and Common Reporting Standard on Automatic Exchange of Financial Account Information in Tax Matters, the Group has put in place a robust control framework to ensure compliance with applicable laws, rules, regulations and supervisory standards. Latest regulatory requirements are promptly brought to the attention of responsible units with revised guidelines and advices delivered for their implementation and strict adherence. Key compliance alerts and information are regularly reported to the Senior Management and the Board. Sufficient resources are also made available to ensure proper legal and regulatory compliance.

Whistleblowing Policy is established for employees to raise their genuine concerns in good faith about malpractice, impropriety, misconduct or unethical activity that they are aware of and which could compromise the interests of the customers, staff, shareholders, the public and/or the Group's image and reputation. All information received is treated confidentially and the identity and interests of all whistle-blowers are protected.

Internal Audit

The Internal Audit function plays an important role in reinforcing the 'Three Lines of Defence' risk management structure of the Bank. As the third line of defence, the Internal Audit function provides independent assurance to the Audit Committee and the Board as to whether the internal control system of the Group is adequate and effective. It has unfettered access to Senior Management for seeking information and explanation on audit matters. The Chief Auditor of the Bank who leads a team with professional expertise reports directly to the Audit Committee.

The Internal Audit function adopts a risk-based approach in its auditing activities. It sets its internal audit plan annually for approval of the Audit Committee based on risk assessment methodology which assists in prioritizing audit resources and focusing on higher risk areas. The review results are reported regularly to the Audit Committee. The Internal Audit function also verifies the implementation effectiveness of the recommendations on internal controls made by external auditors and regulatory bodies.

External Auditor

The Group's external auditor is PricewaterhouseCoopers. The Audit Committee is primarily responsible for making recommendations to the Board on the appointment, re-appointment and removal of the external auditor, including their remuneration and terms of engagement. The Audit Committee also regularly reviews and monitors the independence and objectivity as well as the effectiveness of the audit process of the external auditor.

To safeguard the independence of the external auditor, the Bank has established the Policy on Non-audit Services, setting out the criteria for appointing the external auditor to provide non-audit services. For the year ended 31 December 2019, fees payable to the external auditor of the Group amounted to HK$15,403,000 (2018: HK$23,817,000), of which HK$9,927,000 (2018: HK$10,017,000) was for audit and HK$5,476,000 (2018: HK$13,800,000) was for non-audit along with other compliance services such as tax and independent assessments on ad hoc projects for regulatory purposes.

The Board, on recommendation by the Audit Committee, will propose that PricewaterhouseCoopers be re-appointed as auditor of the Group at the Annual General Meeting of the Bank to be held on 22 April 2020.

Company Secretary

The company secretary is an employee of the Bank who provides support to the Board by ensuring timely information is provided; Board procedures are followed; and the Bank's Articles of Association, relevant rules and regulations including SPM CG-1 and the CG Code are complied with. The company secretary also advises the Board on corporate governance matters and facilitates the induction programme of new Directors and the continuous professional development of existing Directors.

During the year, the company secretary undertook over 15 hours of relevant professional training.

Employees

As of 31 December 2019, the total headcount of the Group was 1,858.

Staff members are regarded by the Bank as the most important and valuable asset, and the key to its success. As a caring employer, the Bank strives to build an engaged workforce through maintaining the well-being of individuals as well as their families. In addition to offering competitive remuneration package, recognition and career advancement, the Bank has introduced various family-friendly and staff engagement initiatives including organizing/sponsoring leisure and sports activities and corporate social responsibility events to promote employee wellness and work-life balance.

We endeavor to encourage and promote desirable staff behavior for adherence to the 7 core values of the Bank:

Proactive	Encourage empowerment and can-do attitude to provide excellent service to staff and customers
Integrity	Adhere to the highest ethical standards and righteous behavior
Respect	Establish mutual trust and respect with staff and customers
Professionalism	Provide high quality service by competent staff
Teamwork	Work across unit lines to achieve success
Accountability	Take ownership in work to drive extraordinary performance
Leadership	Direct, inspire, engage and motivate staff to nurture future leaders

On the training and development side, induction and orientation programmes are provided to staff to help them acquaint with the Bank's history, vision, mission, values, related regulatory requirements and procedural guidelines. The Bank also offers comprehensive training curriculum in both classroom and e-learning formats covering specialized business and operations training to ensure updated technical knowledge be applied in service and operations delivery; personal competencies and skills training to enhance personal effectiveness as well as various regulatory, risk and compliance related training. Professional qualification subsidy and scholarships are available to support the staff in their acquisition of relevant professional/academic qualifications.

Shareholders' Rights

Each shareholder currently has director representation on the Board through which effective communication with shareholders regarding the business and affairs of the Bank is maintained. Shareholders are well informed of their rights to call an extraordinary general meeting of the Bank, the procedures by which enquiries may be presented to the Board and proposals may be put forward at shareholders' meetings as stipulated under Sections 566 to 568 and 615 of the Companies Ordinance. The Corporate Secretary acts as the contact to enable these enquiries or proposals to be properly directed.

The Chairman of the Board is committed to maintaining constant communication with the shareholders to ensure that they have fair and timely access to the Bank's information. All announcements, regulatory disclosures, annual/interim reports and press releases of the Bank are available on the corporate website (www.shacombank.com.hk). Press releases relating to half-yearly and annual financial results of the Bank are also disseminated to major media corporations for public disclosure. As the Bank is a non-listed public company and the four shareholders meet and communicate regularly, the Board considers it unnecessary for the time being to set up a shareholders' communication policy as stipulated in code provision E.1.4 of the CG Code but the matter would be evaluated whenever necessary.

Hong Kong, 18 March 2020

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

(Incorporated in Hong Kong with limited liability)

Opinion

What we have audited

The consolidated financial statements of Shanghai Commercial Bank Limited (the "Bank") and its subsidiaries (the "Group") set out on pages 47 to 129, which comprise:

- the consolidated statement of financial position as at 31 December 2019;
- the consolidated statement of profit or loss for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

Our opinion

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2019, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") and have been properly prepared in compliance with the Hong Kong Companies Ordinance.

Basis for Opinion

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

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

Independence

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

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. The key audit matter identified in our audit is related to the measurement of expected credit losses of loans and advances to customers.

Measurement of expected credit losses ("ECL") of loans and advances to customers

This is the second year that ECL has been reported under HKFRS 9. The ECL model of the Group categorizes the financial assets into three stages. As at 31 December 2019, the Group recorded loan impairment allowances of HK$413 million, with HK$302 million as stage 1 impairment allowances, HK$73 million as stage 2 impairment allowances and HK$38 million as stage 3 impairment allowances in respect of the total gross loan balance of HK$99,187 million. Refer to Note 18 to the consolidated financial statements.

Key Audit Matters (Continued)

Measurement of expected credit losses ("ECL") of loans and advances to customers (Continued)

For the calculation of ECL, management judgement is required in determining impairment methodology, various model inputs and post model adjustments. Management is required to establish a methodology to determine the stage for its financial assets based on changes in credit quality since initial recognition by identifying Significant Increase in Credit Risk ("SICR") and default events. The ECL is measured from the calculation model depending on the stage of the financial assets. Management is also required to incorporate in the ECL models the forward-looking information, where it identifies the key macroeconomic variables impacting credit risk and expected credit loss for each portfolio. Management also concluded that post model adjustments, i.e., the management overlay, are required to address certain limitation in its ECL model methodology. The Group established governance processes and controls for the measurement of ECL.

Our audit focused on the measurement of ECL of loans and advances to customers due to significant judgements applied by management. Specifically we focused on the following:

(1) Criteria for determining whether or not there was a significant increase in credit risk, or a default or impairment loss was incurred;

(2) Economic indicators for forward-looking measurement, and the application of economic scenarios and weightings;

(3) Management overlay adjustments due to model constraints or data limitation not covered in the models; and

(4) The discounted cash flows for corporate loans and advances in stage 3.

How our audit addressed the Key Audit Matter

We obtained an understanding, evaluated and tested the controls that management has established to support their measurement of ECL, including,

– governance over ECL models approval and ongoing monitoring;

– Credit Committee's oversight and regular monitoring of the overall credit quality;

– regular post draw-down monitoring of the grading of credit quality by monitoring units which are independent from the loan initiation units;

– key controls over management's assessment of criteria for determining significant increase in credit risk; and

– regular review and approval of key management judgements including forward-looking and management overlay adjustments.

We assessed major ECL model methodologies and assumptions used for stage 1 and 2 ECL calculation, including reasonableness of the portfolio segmentation and key parameters estimation, with the support of our modelling specialists.

We tested, on a sample basis, management's post draw-down credit reviews and assessed the appropriateness of management's identification of significant increase in credit risk, defaults and credit-impaired loans by considering financial information and non-financial information of the borrowers, relevant external evidence and other factors. We examined the results of a thematic portfolio analysis performed by management in response to changes in external market environments over the credit quality of certain loan portfolios.

For forward-looking measurement, we reviewed management's analysis of their selection of economic indicators; economic scenarios and weightings employed, assessed the reasonableness of the prediction of economic indicators and performed sensitivity analysis of probability weightings.

Key Audit Matters (Continued)

How our audit addressed the Key Audit Matter (Continued)

We assessed the reasonableness of management's selection of uncertain factors and analysis of data limitations and model constraints, as well as their application and measurement in the management overlay adjustments, and examined the accuracy of the relevant mathematical calculations.

We tested, on a sample basis, the ECL calculation of stage 3 loans by challenging management's assumptions in deriving the future cashflows based on borrowers' circumstances, objective evidence of inputs for impairment calculation (including valuation of collateral and macroeconomic variable estimates) and our industry knowledge.

Based on the results of the above testing, management's measurement of ECL for loans and advances to customers are supported with the evidence we obtained.

Other Information

The Directors of the Bank are responsible for the other information. The other information comprises all of the information included in the annual report other than the consolidated financial statements and our auditor's report thereon.

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

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

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

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

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

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

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

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

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. We report our opinion solely to you, as a body, in accordance with Section 405 of the Hong Kong Companies Ordinance and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements (Continued)

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

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Directors.

- Conclude on the appropriateness of the Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

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

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

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

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 18 March 2020

CONSOLIDATED STATEMENT OF PROFIT OR LOSS

(All amounts in HK dollar thousands unless otherwise stated)

	Note	Year ended 31 December 2019	2018
Interest income	6	6,746,101	5,456,164
Interest expense	6	(2,768,808)	(1,847,683)
Net interest income		3,977,293	3,608,481
Fee and commission income	7	870,836	870,394
Fee and commission expense	7	(55,159)	(54,907)
Net fee and commission income		815,677	815,487
Net trading income	8	225,226	185,347
Net gains from disposal of investment securities at fair value through other comprehensive income		60,685	31,297
Dividend income from investment securities at fair value through other comprehensive income		176,872	148,308
Other operating income	9	164,937	145,826
Net earned insurance premium	10	50,388	45,175
Net insurance claims incurred and movement in policyholders' liabilities	10	(38,152)	(23,696)
Operating expenses	11	(1,649,253)	(1,569,265)
Credit impairment losses	12	(60,504)	(28,589)
Operating profit		3,723,169	3,358,371
Share of net profits of associates and joint venture	25	36,519	23,753
Other non-operating income	25	–	118,333
Profit before income tax		3,759,688	3,500,457
Income tax expense	14	(737,705)	(654,784)
Profit for the year		3,021,983	2,845,673
Attributable to:			
Equity holders of the Bank		3,016,086	2,841,357
Non-controlling interests		5,897	4,316
		3,021,983	2,845,673

The notes on pages 53 to 129 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 31 December 2019	2018
Profit for the year		**3,021,983**	2,845,673
Other comprehensive income			
Items that may be reclassified to profit or loss			
Exchange differences on translation of overseas operations		**(53,855)**	(93,775)
Investment securities at fair value through other comprehensive income			
– Changes in fair value		**431,430**	(35,395)
– Credit impairment losses recognised in profit or loss		**(1,083)**	3,065
– Fair value changes transferred to profit or loss on disposal		**(60,685)**	(31,297)
– Deferred income tax	32	**(61,173)**	11,004
Share of reserves of associates and joint venture	34	**18,245**	(22,121)
Items that will not be reclassified to profit or loss			
Equity investments at fair value through other comprehensive income			
– Changes in fair value		**379,998**	225,861
– Deferred income tax	32	**(6,168)**	404,137
Share of reserves of associates and joint venture	34	**(13)**	(29)
Other comprehensive income for the year, net of tax		**646,696**	461,450
Total comprehensive income for the year		**3,668,679**	3,307,123
Attributable to:			
Equity holders of the Bank		**3,662,761**	3,302,852
Non-controlling interests		**5,918**	4,271
Total comprehensive income for the year		**3,668,679**	3,307,123

The notes on pages 53 to 129 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 31 December 2019	2018
ASSETS			
Cash and balances with banks	16	**34,128,614**	28,608,498
Placements with banks	17	**7,090,556**	8,643,722
Loans and advances to customers	18	**98,773,691**	86,725,546
Financial assets at fair value through profit or loss	19	**1,881,025**	1,858,984
Derivative financial instruments	20	**285,089**	313,320
Investment securities at fair value through other comprehensive income	21	**71,558,546**	63,399,110
Investment securities at amortised cost	22	**2,480,924**	2,413,650
Properties for sale	23	**449,462**	416,346
Investments in associates and joint venture	25	**417,663**	388,447
Properties and equipment	26	**2,700,014**	2,332,709
Investment properties	27	**1,017,148**	1,025,892
Deferred income tax assets	32	**28,115**	72,193
Other assets	28	**1,814,267**	1,421,495
TOTAL ASSETS		**222,625,114**	197,619,912
LIABILITIES			
Deposits and balances from banks		**11,677,610**	10,344,988
Deposits from customers	29	**172,438,516**	154,614,718
Derivative financial instruments	20	**292,599**	305,731
Subordinated debts	30	**4,257,647**	1,945,079
Other liabilities	31	**2,813,883**	2,416,189
Current income tax liabilities		**501,694**	91,316
Deferred income tax liabilities	32	**18,901**	27
TOTAL LIABILITIES		**192,000,850**	169,718,048
EQUITY			
CAPITAL AND RESERVES ATTRIBUTABLE TO EQUITY HOLDERS			
Share capital	33	**2,000,000**	2,000,000
Retained earnings		**17,158,968**	15,317,380
Reserves	34	**11,378,917**	10,503,623
		30,537,885	27,821,003
Non-controlling interests in equity		**86,379**	80,861
TOTAL EQUITY		**30,624,264**	27,901,864
TOTAL EQUITY AND LIABILITIES		**222,625,114**	197,619,912

Approved and authorised for issue by the Board of Directors on 18 March 2020.

Stephen Ching Yen LEE
Chairman

Hung-ching YUNG
Director

Gordon Che Keung KWONG
Director

David Sek-chi KWOK
Managing Director & Chief Executive

The notes on pages 53 to 129 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 equity holders			Non-controlling interests	Total equity
		Share capital	Reserves	Retained earnings (including proposed dividends)		
As at 1 January 2018		2,000,000	10,028,070	13,430,081	76,990	25,535,141
Profit for the year		–	–	2,841,357	4,316	2,845,673
Other comprehensive income (net of tax)		–	475,553	(14,058)	(45)	461,450
Investment securities at fair value through other comprehensive income	34	–	577,420	–	(45)	577,375
Currency translation difference arising from overseas operations	34	–	(79,717)	(14,058)	–	(93,775)
Share of reserves of associates and joint venture	34	–	(22,150)	–	–	(22,150)
Total comprehensive income		–	475,553	2,827,299	4,271	3,307,123
Payment of dividend relating to 2017		–	–	(940,000)	(400)	(940,400)
As at 31 December 2018		2,000,000	10,503,623	15,317,380	80,861	27,901,864
As at 31 December 2018 as originally presented		**2,000,000**	**10,503,623**	**15,317,380**	**80,861**	**27,901,864**
Changes in accounting policy	2.1(c)	**–**	**–**	**(5,879)**	**–**	**(5,879)**
Restated as at 1 January 2019		**2,000,000**	**10,503,623**	**15,311,501**	**80,861**	**27,895,985**
Profit for the year		**–**	**–**	**3,016,086**	**5,897**	**3,021,983**
Other comprehensive income (net of tax)		**–**	**675,294**	**(28,619)**	**21**	**646,696**
Investment securities at fair value through other comprehensive income	34	**–**	**682,298**	**–**	**21**	**682,319**
Currency translation difference arising from overseas operations	34	**–**	**(25,236)**	**(28,619)**	**–**	**(53,855)**
Share of reserves of associates and joint venture	34	**–**	**18,232**	**–**	**–**	**18,232**
Total comprehensive income		**–**	**675,294**	**2,987,467**	**5,918**	**3,668,679**
Transfer from retained earnings	34	**–**	**200,000**	**(200,000)**	**–**	**–**
Payment of dividend relating to 2018		**–**	**–**	**(940,000)**	**(400)**	**(940,400)**
As at 31 December 2019		**2,000,000**	**11,378,917**	**17,158,968**	**86,379**	**30,624,264**

	Year ended 31 December	
	2019	2018
Proposed dividend included in retained earnings	**940,000**	940,000

The notes on pages 53 to 129 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(All amounts in HK dollar thousands unless otherwise stated)

	Note	Year ended 31 December 2019	2018
Cash flows from operating activities			
Profit before income tax		**3,759,688**	3,500,457
Share of net profits of associates and joint venture	25	**(36,519)**	(23,753)
Credit impairment losses	12	**60,504**	28,589
Depreciation expenses	11	**231,307**	105,487
Net (gains)/losses from disposal of equipment	9	**(50)**	2,897
Net gains from disposal of investment securities at fair value through other comprehensive income		**(60,685)**	(31,297)
Interest income on investment securities at amortised cost	6	**(44,250)**	(29,681)
Interest income on investment securities at fair value through other comprehensive income	6	**(1,784,182)**	(1,378,843)
Interest expense on subordinated debts	6	**189,413**	75,241
Interest expense on lease liabilities	6	**11,759**	–
Other non-operating income from termination of sale of an associate	25	**–**	(118,333)
Dividend income		**(176,872)**	(148,308)
Hong Kong profits tax paid		**(1,611)**	(757,207)
Overseas tax paid		**(336,411)**	(230,718)
Effect of exchange rate changes		**448,103**	813,296
Cash flows from operating activities before changes in operating assets and liabilities		**2,260,194**	1,807,827
Changes in operating assets and liabilities:			
– Net decrease in balances with banks with original maturity beyond 3 months		**2,129,736**	648,072
– Net decrease in placements with banks with original maturity beyond 3 months		**1,992,874**	7,170,221
– Net (increase)/decrease in financial assets at fair value through profit or loss		**(22,041)**	115,269
– Net decrease/(increase) in derivative financial instruments		**15,099**	(12,779)
– Net increase in loans and advances to customers		**(12,107,771)**	(8,625,771)
– Net increase in right-of-use assets		**(136,717)**	–
– Net (increase)/decrease in other assets		**(361,312)**	375,338
– Net increase in deposits and balances from banks		**1,332,622**	3,591,075
– Net increase in deposits from customers		**17,823,798**	7,970,024
– Net increase in lease liabilities		**135,201**	–
– Net decrease in other liabilities		**(28,192)**	(292,087)
Net cash flows from operating activities		**13,033,491**	12,747,189

CONSOLIDATED STATEMENT OF CASH FLOWS (CONTINUED)

(All amounts in HK dollar thousands unless otherwise stated)

	Note	Year ended 31 December 2019	2018
Cash flows from investing activities			
Interest received on investment securities at amortised cost and investment securities at fair value through other comprehensive income		1,638,832	1,383,205
Dividends received on investment securities at fair value through other comprehensive income		176,872	148,308
Dividends received from associates and joint venture	25	25,535	27,070
Purchases of properties and equipment	26	(104,654)	(68,774)
Additions of investment properties	27	(150)	(14,282)
Additions of properties for sale		(33,116)	(18,024)
Proceeds from sale of equipment		157	118
Purchases of investment securities at fair value through other comprehensive income		(59,218,760)	(31,798,851)
Purchases of investment securities at amortised cost		(8,254,942)	(4,414,442)
Other non-operating income from termination of sale of an associate	25	–	118,333
Additional investment in an associate	25	–	(75,000)
Proceeds from sale and redemption of investment securities at fair value through other comprehensive income		48,058,270	25,541,568
Proceeds from redemption of investment securities at amortised cost		8,850,041	4,708,553
Net cash flows from investing activities		(8,861,915)	(4,462,218)
Cash flows from financing activities			
Issue of subordinated debts	35(a)	2,338,326	–
Interest paid on subordinated debts		(132,088)	(73,763)
Payment of lease liabilities		(115,406)	–
Dividend paid to equity holders		(940,000)	(940,000)
Dividend paid to non-controlling interests		(400)	(400)
Net cash flows from financing activities		1,150,432	(1,014,163)
Net increase in cash and cash equivalents		5,322,008	7,270,808
Cash and cash equivalents at beginning of the year		34,702,607	27,720,636
Effect of exchange rate changes on cash and cash equivalents		(212,002)	(288,837)
Cash and cash equivalents at end of the year	35(b)	39,812,613	34,702,607
Cash flows from operating, investing and financing activities included:			
Interest received		6,757,234	5,391,685
Interest paid		(2,502,045)	(1,754,847)

The notes on pages 53 to 129 are an integral part of these consolidated financial statements.

1 GENERAL INFORMATION

Shanghai Commercial Bank Limited (the "Bank") and its subsidiaries (together, the "Group") are engaged in the provision of banking and related financial services in Hong Kong, the United States, the United Kingdom and the People's Republic of China.

The Bank is a financial institution incorporated in Hong Kong. The address of its registered office is Shanghai Commercial Bank Tower, 12 Queen's Road Central, Hong Kong.

The ultimate holding company is The Shanghai Commercial & Savings Bank, Ltd., which is incorporated in the Republic of China (Taiwan).

These consolidated financial statements are presented in thousands of units of Hong Kong Dollars (HK$'000), unless otherwise stated and were approved for issue by the Board of Directors on 18 March 2020.

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 have been prepared in accordance with all applicable Hong Kong Financial Reporting Standards ("HKFRSs") and the requirements of the Hong Kong Companies Ordinance Cap. 622. The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of investment securities at fair value through other comprehensive income, financial assets at fair value through profit or loss and derivative financial instruments, which are carried 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 judgements in the process of applying the Group's accounting policies. The areas involving a higher degree of judgements or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

(a) New and amended standards adopted by the Group for the year ended 31 December 2019

The Group applies, for the first time, HKFRS 16 "Leases" ("HKFRS 16"), and elected to adopt the new rules retrospectively but recognised the cumulative effect of initially applying the new standard on 1 January 2019. The impact of the adoption is disclosed in Note 2.1(c).

The other standards and amendments which became effective for the accounting period beginning on 1 January 2019 did not have material impact on the Group's financial statements.

(b) Amendments, new standards and interpretations issued but not yet effective for the year ended 31 December 2019

The HKICPA has issued a few amendments, new standards and interpretations which are not yet effective for the year ended 31 December 2019 and which have not been adopted in these consolidated financial statements. These include the following which may be relevant to the Group:

	Effective for accounting periods beginning on or after
HKFRS 17 "Insurance contracts"	1 January 2021
Definition of Material – Amendments to HKAS 1 and HKAS 8	1 January 2020
Definition of a Business – Amendments to HKFRS 3	1 January 2020
Revised Conceptual Framework for Financial Reporting	1 January 2020

The Group is assessing the financial impact of the amendments, new standards and interpretations and preparing for their implementation on effective dates.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.1 Basis of preparation (Continued)

(b) Amendments, new standards and interpretations issued but not yet effective for the year ended 31 December 2019 (Continued)

HKFRS 17 "Insurance contracts"
HKFRS 17 "Insurance contracts" is effective for the accounting period beginning on or after 1 January 2021. It establishes the principles for the recognition, measurement, presentation and disclosure of insurance contracts within the scope of the standard and to replace the HKFRS 4 "Insurance contracts". The objective of HKFRS 17 is to ensure that an entity provides relevant information that faithfully represents those contracts. HKFRS 17 defines clear and consistent rules that will significantly increase the comparability of financial statements. The general model under HKFRS 17 requires an entity to measure an insurance contract at initial recognition at the total of the fulfilment cash flows and the contractual service margin. Aside from this general model, the standard provides, as a simplification, the premium allocation approach. The Group is in the process of assessing the financial and disclosure impact on the adoption of the standard.

(c) Changes in accounting policies

This note explains the impact of the adoption of HKFRS 16 on the Group's financial statements and also discloses the new accounting policies that have been applied from 1 January 2019, where they are different to those applied in prior periods. The new accounting policies are disclosed in Note 2.14.

The Group has adopted HKFRS 16 retrospectively from 1 January 2019, but has not restated comparatives for the 2018 reporting period, as permitted under the specific transitional provisions in the standard. The classifications and the adjustments arising from the new leasing rules are therefore recognised in the opening statement of financial position on 1 January 2019.

On adoption of HKFRS 16, the Group recognised lease liabilities in relation to leases which had previously been classified as "operating leases" under the principles of HKAS 17 "Leases". These liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate as of 1 January 2019.

Set out below are disclosures relating to the impact of the adoption of HKFRS 16 on the Group.

(i) Practical expedients applied

In applying HKFRS 16 for the first time, the Group has used the following practical expedients permitted by the standard:

- the use of a single discount rate to a portfolio of leases with reasonably similar characteristics;
- reliance on previous assessments on whether leases are onerous;
- the accounting for operating leases with a remaining lease term of less than 12 months as at 1 January 2019 as short-term leases;
- the exclusion of initial direct costs for the measurement of the right-of-use asset at the date of initial application; and
- the use of hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.1 Basis of preparation (Continued)

(c) Changes in accounting policies (Continued)

(ii) Measurement of lease liabilities

Operating lease commitments disclosed as at 31 December 2018	260,670
Discounted using the Group's incremental borrowing rate	(12,885)
Add: finance lease liabilities recognised as at 31 December 2018	113
(Less): short-term leases recognised on a straight-line basis as expense	(61)
(Less): low-value leases recognised on a straight-line basis as expense	(3,787)
Add: contracts reassessed as lease agreements	12,701
Add: adjustments as a result of a different treatment of extension and termination options	100,522
Lease liabilities recognised as at 1 January 2019	357,273
Of which are:	
Current lease liabilities	108,920
Non-current lease liabilities	248,353
	357,273

(iii) Measurement of right-of-use assets

The associated right-of-use assets for property leases were measured on a retrospective basis as if the new rules had always been applied. Other right-of-use assets were measured at the amount equal to the lease liabilities, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the statement of financial position as at 31 December 2018. There were no onerous lease contracts that would have required an adjustment to the right-of-use assets at the date of initial application.

(iv) Adjustments recognised in the consolidated statement of financial position on 1 January 2019

The change in accounting policy affected the following items in the consolidated statement of financial position as at 1 January 2019:

Right-of-use assets	
– Buildings	334,714
– Equipment	14,756
– Motor vehicles	219
	349,689
Deferred income tax assets	1,497
Effect on total assets	351,186
Retained earnings	(5,879)
Lease liabilities	357,273
Other liabilities	(208)
Effect on total equity and liabilities	351,186

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.2 Consolidation

The consolidated financial statements include the financial statements of the Bank and all its subsidiaries made up to 31 December 2019.

(a) Subsidiaries

Subsidiaries are all entities (including structured entities) over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the 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.

(c) Associates

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

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

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.2 Consolidation (Continued)

(c) Associates (Continued)

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

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

(d) Joint ventures

A joint venture is an arrangement whereby the Group and other parties contractually agree to share control of the arrangement and have right to the net assets of the arrangement. Joint ventures are accounted for using the equity method.

Under the equity method of accounting, interests in joint ventures are initially recognised at cost and adjusted thereafter to recognise the Group's share of the post-acquisition profits or losses and movements in other comprehensive income. When the Group's share of losses in a joint venture equals or exceeds its interests in the joint venture (which includes any long-term interests that, in substance, form part of the Group's net investment in the joint venture), the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the joint venture.

Unrealised gains on transactions between the Group and its joint ventures are eliminated to the extent of the Group's interest in the joint ventures. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

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 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. 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 rate at the date when the fair value was determined.

Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at exchange rates at the reporting date of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of profit or loss.

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.3 Foreign currency translation (Continued)

(b) Transactions and balances (Continued)

In the case of changes in the fair value of monetary assets denominated in foreign currency classified as fair value through other comprehensive income ("FVOCI"), 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 ("FVTPL"), are reported as part of the fair value gain or loss. Translation differences on non-monetary financial instruments, such as equities classified as FVOCI investments, are included in other comprehensive income.

(c) Group companies and overseas branches

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

- Assets and liabilities for each statement of financial position presented are translated at the closing rate at the reporting date;

- Income and expenses for each statement of profit or loss 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, 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 statement of profit or loss 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 Fee and commission income and expense

Fees and commissions income are recognised on an accrual basis when the service has been provided to customers. Loan fees for servicing a loan are recognised as fee income. 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 over the tenor of the contract. Any resulting increases or decreases in estimated revenues related to contract liabilities is reflected in statement of profit or loss in the period in which the circumstances that give rise to the revision become known by management.

2.5 Rental income

Rental income from investment properties is recognised in the consolidated statement of profit or loss on a straight-line basis over the terms of the leases.

2.6 Dividend income

Dividends are recognised in the statement of profit or loss when the entity's right to receive payment is established.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.7 Financial assets, financial liabilities, interest income and expense

Measurement methods

Initial recognition and measurement

Financial assets and financial liabilities are recognised when the Group becomes a party to the contractual provisions of the instrument. Regular way purchases and sales of financial assets are recognised on trade-date, the date on which the Group commits to purchase or sell the asset.

At initial recognition, the Group measures a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are incremental and directly attributable to the acquisition or issue of the financial asset or financial liability, such as fees and commissions. Transaction costs of financial assets and financial liabilities carried at fair value through profit or loss are expensed in profit or loss. Immediately after initial recognition, expected credit loss ("ECL") is recognised for financial assets measured at amortised cost or measured at FVOCI, which results in an accounting loss being recognised in profit or loss when an asset is newly originated.

When the fair value of financial assets and liabilities differs from the transaction price on initial recognition, the Group recognises the difference as follows:

(a) When the fair value is evidenced by a quoted price in an active market for an identical asset or liability (i.e. a Level 1 input) or based on a valuation technique that uses only data from observable markets, the difference is recognised as a gain or loss.

(b) In all other cases, the difference is deferred and the timing of recognition of deferred day one profit or loss is determined individually. It is either amortised over the life of the instrument, deferred until the instrument's fair value can be determined using market observable inputs, or realised through settlement.

Classification and subsequent measurement

The Group classifies its financial assets into the following measurement categories:

– Amortised cost;

– FVOCI; or

– FVTPL.

Debt instruments

Classification and subsequent measurement of debt instruments depend on:

(i) the Group's business model for managing the asset; and

(ii) the cash flow characteristics of the asset.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.7 Financial assets, financial liabilities, interest income and expense (Continued)

Classification and subsequent measurement (Continued)

Debt instruments (Continued)

There are three measurement categories into which the Group classifies its debt instruments:

(a) Amortised cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest ("SPPI"), and that are not designated at FVTPL, are measured at amortised cost. The carrying amount of these assets is adjusted by ECL recognised. Interest income from these financial assets is included in "Net interest income" using the effective interest rate method.

(b) FVOCI: Assets that are held for collection of contractual cash flows and for selling the assets, where the assets' cash flows represent solely payments of principal and interest, and that are not designated at FVTPL, are measured at FVOCI. Movements in the carrying amount are taken through other comprehensive income, except for the recognition of impairment gains or losses, interest income and foreign exchange gains and losses on the instrument's amortised cost which are recognised in profit or loss. When the financial asset is derecognised, the cumulative gain or loss previously recognised in other comprehensive income is reclassified from equity to profit or loss. Interest income from these financial assets is included in "Net interest income" using the effective interest rate method.

(c) FVTPL: Assets that do not meet the criteria for amortised cost or FVOCI are measured at FVTPL. A gain or loss on a debt instrument that is subsequently measured at FVTPL is recognised in profit or loss and presented net in the statement of profit or loss within "Net trading income" in the period in which it arises.

Business model: the business model reflects how the Group manages the assets in order to generate cash flows. That is, whether the Group's objective is solely to collect the contractual cash flows from the assets or is to collect both the contractual cash flows and cash flows arising from the sale of assets. If neither of these is applicable (e.g. financial assets are held for trading purposes), then the financial assets are classified as part of "other" business model and measured at FVTPL. Factors considered by the Group in determining the business model for a group of assets include past experience on how the cash flows for these assets were collected, how the asset's performance is evaluated and reported to key management personnel, how risks are assessed and managed and how managers are compensated.

SPPI: Where the business model is to hold assets to collect contractual cash flows or to collect contractual cash flows and sell, the Group assesses whether the financial instruments' cash flows represent solely payments of principal and interest (the "SPPI test"). In making this assessment, the Group considers whether the contractual cash flows are consistent with a basic lending arrangement i.e. interest includes only consideration for the time value of money, credit risk, other basic lending risks and a profit margin that is consistent with a basic lending arrangement. Where the contractual terms introduce exposure to risk or volatility that are inconsistent with a basic lending, the related financial asset is classified and measured at fair value through profit or loss.

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.7 Financial assets, financial liabilities, interest income and expense (Continued)

Classification and subsequent measurement (Continued)

Equity instruments

The Group subsequently measures equity instruments at FVTPL, except where the Group's management has elected, at initial recognition, to irrevocably designate an equity security at FVOCI. Where the Group's management has elected to present fair value gains and losses on equity instruments in other comprehensive income, there is no subsequent reclassification of fair value gains and losses to profit or loss following the derecognition of the instruments. Dividends from such instruments continue to be recognised in profit or loss as dividend income when the Group's right to receive payments is established.

Gains and losses on equity instruments at FVTPL are included in the "Net trading income" in the statement of profit or loss.

Modification of financial assets

If the borrower is in financial difficulty, where the terms of the financial assets are modified and being substantially different to the original terms, the Group derecognises the original financial asset and recognises a "new" asset at fair value and recalculates a new effective interest rate for the asset. The date of renegotiation is consequently considered to be the date of initial recognition for impairment calculation purpose, including for the purpose of determining whether a significant increase in credit risk has occurred. However, the Group also assesses whether the new financial asset recognised is deemed to be credit-impaired at initial recognition, especially in circumstances where the renegotiation was driven by the debtor being unable to make the originally agreed payments. Difference in the carrying amount is also recognised in profit or loss as a gain or loss on derecognition.

If the terms are not substantially different, the renegotiation or modification does not result in derecognition, the financial asset continues to be subject to the same assessments for significant increase in credit risk relative to initial recognition and credit-impairment, as described above.

Derecognition other than on a modification

Financial assets, or a portion thereof, are derecognised when the contractual rights to receive the cash flows from the assets have expired, or when they have been transferred and either (i) the Group transfers substantially all the risks and rewards of ownership, or (ii) the Group neither transfers nor retains substantially all the risks and rewards of ownership and the Group has not retained control.

The Group enters into transactions where it retains the contractual rights to receive cash flows from assets but assumes a contractual obligation to pay those cash flows to other entities and transfers substantially all of the risks and rewards. These transactions are accounted for as "pass through" transfers that result in derecognition if the Group:

(i) does not have obligation to make payments unless it collects equivalent amounts from the assets;

(ii) is prohibited from selling or pledging the assets; and

(iii) has an obligation to remit any cash it collects from the assets without material delay.

Collateral furnished by the Group under standard repurchase agreements and securities lending and borrowing transactions are not derecognised because the Group retains substantially all the risks and rewards on the basis of the predetermined repurchase price, and the criteria for derecognition are therefore not met.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.7 Financial assets, financial liabilities, interest income and expense (Continued)

Impairment of financial assets

The Group assesses on a forward-looking basis ECL associated with its financial assets carried at amortised cost and debt instruments measured at FVOCI and with the exposure arising from loan commitments and financial guarantee contracts. The Group recognises a loss allowance for such losses at each reporting date. The measurement of ECL reflects:

- An unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;
- The time value of money; and
- Reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

Note 3.1.1 provides more detail of how the ECL is measured.

Financial liabilities

Classification and subsequent measurement

The Group classifies its financial liabilities at amortised cost, except for:

(a) financial liabilities at fair value through profit or loss: this classification is applied to derivatives, financial liabilities held for trading and other financial liabilities designated as such at initial recognition. Gains or losses on financial liabilities designated at fair value through profit or loss are presented partially in other comprehensive income (the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability, which is determined as the amount that is not attributable to changes in market conditions that give rise to market risk) and partially profit or loss (the remaining amount of change in the fair value of the liability). Should such a presentation create, or enlarge, an accounting mismatch, in which case the gains and losses attributable to changes in the credit risk of the liability are also presented in profit or loss; and

(b) financial liabilities arising from the transfer of financial assets which did not qualify for derecognition: when the transfer of financial asset did not qualify for derecognition, a financial liability is recognised for the consideration received for the transfer. In subsequent periods, the Group recognises any expense incurred on the financial liability.

Derecognition

Financial liabilities are derecognised when they are extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires).

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.7 Financial assets, financial liabilities, interest income and expense (Continued)

Interest income and expense

Interest income and expense for all interest-bearing financial instruments, except for those classified as financial assets or financial liabilities at fair value through profit or loss, are recognised within "interest income" and "interest expense" in the statement of profit or loss using the effective interest method.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset (i.e. its amortised cost before any impairment allowance) or to the amortised cost of a financial liability. The calculation does not consider ECL and includes the transaction costs, premiums or discounts and fees and points paid or received that are integral to the effective interest rate, such as origination fees. For purchased or originated credit-impaired ("POCI") financial assets – assets that are credit-impaired at initial recognition – the Group calculates the credit-adjusted effective interest rate, which is calculated based on the amortised cost of the financial asset instead of its gross carrying amount and incorporates the impact of ECL in estimated future cash flows.

Interest income is calculated by applying the effective interest rate to the gross carrying amount of financial assets, except for:

(a) POCI financial assets, for which the original credit-adjusted effective interest rate is applied to the amortised cost of the financial asset.

(b) Financial assets that have subsequently become credit-impaired (or "Stage 3"), for which interest income is calculated by applying the effective interest rate to their amortised cost (i.e. net of the ECL provision).

2.8 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 are embedded in hybrid contracts, such as the equity option in an equity linked instrument. If the hybrid contract contains a host that is a financial asset, then the Group assesses the entire contract as described in the financial assets section above for classification and measurement purposes.

2.9 Financial guarantee contracts and loan commitments

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 guarantee contracts are initially measured at fair value and subsequently measured at the higher of:

- The amount of the impairment allowance; and
- The premium received on initial recognition less income recognised in accordance with the principles of HKFRS15.

Loan commitments provided by the Group are measured as the amount of the impairment allowance.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.10 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 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 end of each reporting period.

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 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 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.

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.11 Properties 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. The land is depreciated over the lease term. The depreciation of the buildings is based on management's appraisal of their conditions, which includes estimations of the remaining useful lives, which are not expected to exceed 40 years.

Interest in freehold land is stated at cost.

(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 are calculated to write off the costs of the assets over their estimated useful lives on a straight line basis over 4 to 10 years.

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 statement of profit or loss during the financial period in which they are incurred.

(c) Property under development

Leasehold land for property 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 leasehold land for properties under development, please refer to Note 2.11(a) above.

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 2.15). The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

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

2.12 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. 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 unexpired period of the lease term for land and the shorter of the leases or 40 years for buildings.

2.13 Properties for sale

Properties for sale are carried at the lower of cost and net realisable value. Net realisable value takes into account the price ultimately expected to be realised and the anticipated costs to completion.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.14 Leases

The Group's leasing activities and how these are accounted for

The Group leases various properties, equipment and motor vehicles. Rental contracts are typically made for fixed periods of 2 to 5 years but may have extension options. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. The lease agreements do not impose any covenants, but leased assets may not be used as security for borrowing purposes.

Until the 2018 financial year, leases of property and equipment were classified as either finance or operating leases. Payments made under operating leases (net of any incentives received from the lessor) were charged to profit or loss on a straight-line basis over the period of the lease.

From 1 January 2019, leases are recognised as a right-of-use asset and a corresponding liability on the date when the leased asset is available for use by the Group. Each lease payment is allocated between the liability and finance cost (i.e. interest on lease liabilities). The finance cost is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The right-of-use asset is depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis.

Assets and liabilities arising from a lease are initially measured on a present value basis. Lease liabilities include the net present value of the following lease payments:

– fixed payments (including in-substance fixed payments), less any lease incentives receivable;

– amounts expected to be payable by the lessee under residual value guarantees;

– the exercise price of a purchase option if the lessee is reasonably certain to exercise that option; and

– payments of penalties for terminating the lease, if the lease term reflects the lessee exercising that option.

The lease payments are discounted using the Group's incremental borrowing rate, being the rate that the lessee would have to pay to borrow the funds necessary to obtain an asset of similar value in a similar economic environment with similar terms and conditions.

Right-of-use assets are measured at cost comprising the following:

– the amount of the initial measurement of lease liabilities;

– any lease payments made at or before the commencement date less any lease incentives received;

– any initial direct costs; and

– restoration costs.

Payments associated with short-term leases and leases of low-value assets are recognised on a straight-line basis as an expense in profit or loss. Short-term leases are leases with a lease term of 12 months or less. Low-value assets comprise IT equipment and small items of office furniture.

The accounting for leasehold land previously classified as finance lease remains the same. Amortisation for leasehold land commences from the time when the land interest becomes available for its intended use. Interest in leasehold land is amortised on a straight-line basis over the unexpired period of the lease term.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.14 Leases (Continued)

Extension and termination options

Extension and termination options are included in a number of property and equipment leases across the Group. These terms are used to maximise operational flexibility in terms of managing contracts. The majority of extension and termination options held are exercisable only by the Group and not by the respective lessor.

Where the Group is a lessor

Lease income from operating leases where the Group is a lessor is recognised in income on a straight-line basis over the lease term. The respective leased assets are included in the consolidated statement of financial position based on their nature.

2.15 Impairment of investment in subsidiaries, associates, joint venture 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.

2.16 Current and deferred income tax

The tax expense for the period comprises current and deferred tax. Tax is recognised in the statement of profit or loss, 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 reporting date in the countries where the Group's 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 financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted at the reporting date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

The principal temporary differences arise from depreciation of properties 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. 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, associates and joint venture, 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.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.16 Current and deferred income tax (Continued)

Deferred income tax related to fair value re-measurement of FVOCI debt investments, which is charged or credited to other comprehensive income, is also credited or charged to other comprehensive income and is subsequently recognised in the statement of profit or loss together with the deferred gain or loss upon disposal.

Deferred income tax related to fair value re-measurement of FVOCI equity investments, which is charged or credited to other comprehensive income, will remain in reserves and will not be subsequently recognised in the statement of profit or loss upon disposal.

2.17 Employee benefits

(a) Retirement benefit costs

The Group operates 2 retirement benefit schemes comprising of a Mandatory Provident Fund Scheme and a defined benefit scheme that are available to the Group's employees. However, the principal scheme that the Group contributes to is the Mandatory Provident Fund Scheme. The assets of the Group's Mandatory Provident Fund Scheme and the defined benefit scheme are held separately from those of the Group in independently administered funds.

The Group's contributions to the Mandatory Provident Fund Scheme are charged to the statement of profit or loss.

The defined benefit scheme is funded by payments from the Group's Hong Kong Office 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 statement of profit or loss 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 3 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 or when the entity recognises costs for a restructuring that is within the scope of HKAS 37 and involves payment of termination benefits. 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 reporting date are discounted to present value.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.18 Provisions

Provisions 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.

2.19 Related parties

For the purposes of these financial statements, a party is considered to be related to the Group if that party controls, jointly controls or has significant influence over the Group; is a member of the same financial reporting group, such as parents, subsidiaries and fellow subsidiaries; is an associate or a joint venture of the Group or parent reporting group; is a key management personnel of the Group or parents, or where the Group and the party are subject to common control. Related parties may be individuals or entities.

2.20 Repossessed assets

Repossessed assets are recorded as "Repossessed assets" and reported in "Other assets" and the relevant loans are derecognised when the Group has taken the legal title and control of the repossessed assets. The repossessed assets are measured at the lower of carrying amount of loan and fair value less cost to sell.

2.21 Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise balances with less than 3 months' maturity from the date of acquisition including cash, balances with banks, placements with banks, treasury bills and certificates of deposit that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

2.22 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.

2.23 Segment reporting

Operating segments, and the amounts of each segment item reported in the consolidated financial statements, are identified from the financial information provided regularly to the Group's most senior executive management for the purposes of allocating resources to, and assessing the performance of, the Group's various lines of business and geographical locations.

Individually material operating segments are not aggregated for financial reporting purposes unless the segments have similar economic characteristics and are similar in respect of the nature of products and services, the nature of production processes, the type or class of customers, the methods used to distribute the products or provide the services, and the nature of the regulatory environment. Operating segments which are not individually material may be aggregated if they share a majority of these criteria.

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. 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 Risk Committee, the Executive Committee, the Asset and Liability Committee, the Credit Committee and the Operational Risk Management Committee for the supervision of major functional areas. 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 Division is responsible for monitoring the overall risk management of the Group's operations. 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 Committee before submission to the management for approval. All of the above arrangements ensure that the risk management processes are operating effectively.

The Internal 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 reporting date.

The Group has in place effective credit review, monitoring and control systems including an effective loan classification system that identify, monitor, and determine impairment allowance in a timely manner. Management therefore carefully manages the 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 principal 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.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.1 Expected credit loss measurement

The Group adopts a "three-stage" model in accordance with HKFRS 9 for impairment based on changes in credit quality since initial recognition as summarised below:

- A financial instrument that is not credit-impaired at initial recognition is classified as "Stage 1" and has its credit risk continuously monitored by the Group;
- If a significant increase in credit risk ("SICR") since initial recognition is identified, the financial instrument is moved to "Stage 2" though it has not yet deemed to be credit-impaired;
- If the financial instrument is credit-impaired, it will be allocated to "Stage 3";
- Financial instruments in Stage 1 have their ECL measured at an amount equal to the portion of lifetime ECL that result from default events possible within the next 12 months. Instruments at Stages 2 or 3 have their ECL measured on lifetime basis;
- ECL of financial instruments are measured by taking into consideration forward-looking information; and
- POCI financial assets are those financial assets that are credit-impaired at initial recognition. Their ECL are always measured on lifetime basis (Stage 3).

The Group adopts the approach that utilises the Probability of Default ("PD"), Exposure at Default ("EAD") and Loss Given Default ("LGD") to estimate ECL of financial instruments. Simplified alternatives are applied to portfolios that have difficulties in adopting this approach.

To estimate PD, EAD and LGD, exposures are first segmented according to their product types and customer types so that each group contains exposures with similar risk characteristics and product specifications. The factors used for segmentation are outlined below:

(i) Customers' characteristics
(ii) Product types
(iii) Facilities' utilization
(iv) Loan to collateral ratios

The modelling approaches used for different segments vary and with the consideration of the following factors:

(i) Portfolio size
(ii) Historical behavioural data
(iii) Data sufficiency

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.1 Expected credit loss measurement (Continued)

Management overlay and judgements

For HKFRS 9 ECL calculation, the Group has implemented and applied management overlay above the modeled ECL. The management overlay methodologies and amounts are subject to regular robust review and governance processes to assess the adequacy and relevancy of such overlay. The management overlay includes items that are inevitably not precisely quantifiable and necessitate involvement of expert judgements, so as to account for model constraints, data limitation, exceptional events, etc. The management overlay methodologies constitute of allowing for reasonably sufficient impairment to the portfolios of the overseas branches and marginal Stage 1 loans, and accounting for other uncertainty factors on data, models, and events that might impact the ECL computation.

The key judgements and assumptions adopted by the Group in addressing the requirements of the standard are discussed below:

3.1.1.1 SICR

The Group considers a financial instrument to have experienced a significant increase in credit risk when one or more of the following criteria have been met:

- The borrower is more than 30 days past due on its contractual payments;
- The financial instrument is downgraded in the internal rating categories and there is an increase in PD more than predetermined thresholds since initial recognition; and
- Significant increase in credit risk since initial recognition with reference to external rating downgrade after initial recognition.

3.1.1.2 Definition of default and credit-impaired assets

The Group defines a financial instrument as in default, which is fully aligned with the definition of credit-impaired, when it meets one or more of the following criteria:

Quantitative criteria

- The borrower is more than 90 days past due on its contractual payments.

Qualitative criteria

The borrower meets unlikeliness-to-pay criteria, which indicates the borrower is in significant financial difficulty. These could be instances where:

- The financial instrument is restructured due to financial stress;
- The financial instrument is partially written off;
- The borrower is bankrupt;
- The borrower is unlikely to honour its credit obligation; and
- The instrument is tagged with Substandard, Doubtful or Loss in the Loan Classification, except for credit card.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.1 Expected credit loss measurement (Continued)

3.1.1.3 Measuring ECL – Explanation of inputs, assumptions and estimation techniques

The ECL is measured on either a 12-month or Lifetime basis depending on whether a significant increase in credit risk has occurred since initial recognition or whether an asset is considered to be credit-impaired. ECL is calculated as the discounted product of the PD, EAD and LGD, defined as follows:

- PD represents the likelihood of a borrower defaulting on its financial obligation.
- EAD is based on the amounts the Group expects to be owed at the time of default.
- LGD represents the Group's expectation of the extent of loss on a defaulted exposure. LGD varies by type of counterparty, type and seniority of claim and availability of collateral or other credit support. LGD is expressed as a percentage loss per unit of exposure at the time of default.

There have been no significant changes in estimation technique or significant assumptions made during the reporting period.

3.1.1.4 Forward-looking information incorporated in the ECL models

The calculation of ECL incorporates forward-looking information by considering key economic variables identified by the Group that have impact on credit risk and ECL for the Group's portfolios.

These economic variables and their associated impact on the PD, EAD and LGD vary by the type of financial instruments. Expert judgement has also been applied in this process. Forecasts of these economic variables (the "base economic scenario") are provided by the Group's Treasury Research team on a monthly basis as a projection of how the global economy will evolve over the next four years. Beyond these four years, the average portfolio default rate is adopted as the PD of the facilities and the last forecasted LGD is adopted for the remaining lifetime of the instrument.

In addition to the base economic scenario, the Group's Treasury Research team also provides two other plausible scenarios along with the assigned weightings as probability of occurrence under the current economic environment. The scenarios and their corresponding weightings are determined by a combination of model-based analysis and expert judgement, taking into account the range of possible outcomes each chosen scenario is representative of. The probability weighted ECL is determined by applying each scenario on the financial instruments through running the relevant ECL models and multiplying the resulted ECLs by the appropriate scenario weighting.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.1 Expected credit loss measurement (Continued)

3.1.1.4 Forward-looking information incorporated in the ECL models (Continued)

Economic variable assumptions

The most significant period-end assumptions used for the ECL estimate as at 31 December 2019 are set out below. The scenarios "base", "upside" and "downside" were used for all portfolios.

		2019	2020	2021	2022	2023
Hong Kong Gross Domestic Product ("GDP")	Base	1.5% to 1.5%	–0.5% to 2.0%	2.9% to 3.3%	2.9% to 3.3%	3.4% to 3.4%
	Upside	2.2% to 2.2%	0.6% to 2.2%	3.3% to 3.7%	3.3% to 3.7%	3.8% to 3.8%
	Downside	–1.0% to –1.0%	–4.7% to 0.6%	3.0% to 3.5%	3.1% to 3.5%	3.0% to 3.0%
United States GDP	Base	2.1% to 2.1%	0.4% to 1.4%	1.6% to 1.6%	1.5% to 1.5%	1.5% to 1.5%
	Upside	3.0% to 3.0%	2.2% to 2.2%	2.0% to 2.0%	1.8% to 1.8%	1.8% to 1.8%
	Downside	–0.2% to –0.2%	–1.9% to –0.9%	1.1% to 1.1%	1.0% to 1.0%	1.0% to 1.0%
Hong Kong unemployment rate	Base	3.0% to 3.0%	3.3% to 3.7%	3.5% to 3.9%	3.7% to 4.1%	3.9% to 4.3%
	Upside	3.0% to 3.0%	3.0% to 3.5%	3.3% to 3.7%	3.5% to 4.0%	3.8% to 3.9%
	Downside	3.5% to 3.5%	3.7% to 4.3%	4.3% to 4.8%	4.8% to 5.3%	5.3% to 5.7%
United States unemployment rate	Base	3.9% to 3.9%	4.1% to 4.5%	4.5% to 4.8%	4.9% to 5.2%	5.3% to 5.5%
	Upside	3.8% to 3.8%	3.8% to 3.8%	3.9% to 4.0%	4.0% to 4.1%	4.1% to 4.1%
	Downside	4.4% to 4.4%	4.8% to 5.7%	5.8% to 6.1%	6.2% to 6.5%	6.6% to 6.8%
Hong Kong property price index	Base	0.9% to 0.9%	–7.4% to 4.8%	3.0% to 7.4%	0.0% to 0.0%	3.0% to 3.0%
	Upside	10.3% to 10.3%	1.9% to 6.0%	2.0% to 2.0%	2.0% to 2.0%	5.0% to 5.0%
	Downside	–3.6% to –3.6%	–19.3% to –4.3%	–0.3% to 4.1%	0.0% to 0.0%	0.0% to 0.0%
United States house price index	Base	2.0% to 2.0%	–1.3% to 1.2%	1.2% to 3.0%	2.0% to 2.0%	2.0% to 2.0%
	Upside	3.2% to 3.2%	0.2% to 1.8%	1.5% to 3.3%	2.3% to 2.4%	2.4% to 2.4%
	Downside	–2.4% to –2.4%	–8.5% to –4.3%	–5.4% to –2.1%	–3.2% to –0.8%	–0.8% to –0.8%
United Kingdom house price index	Base	3.7% to 3.7%	–0.8% to 3.2%	–3.9% to –1.6%	–0.4% to 0.8%	0.9% to 1.0%
	Upside	5.5% to 5.5%	1.7% to 4.6%	0.2% to 1.2%	0.8% to 0.8%	1.0% to 1.1%
	Downside	–1.5% to –1.5%	–2.3% to 0.9%	–7.8% to –3.7%	–5.9% to 0.0%	0.0% to 0.0%
People's Republic of China house price index	Base	4.0% to 4.0%	–2.6% to 0.5%	1.0% to 2.0%	2.0% to 2.0%	2.0% to 2.0%
	Upside	6.0% to 6.0%	3.0% to 3.0%	3.0% to 3.0%	3.0% to 3.0%	3.0% to 3.0%
	Downside	–5.0% to –5.0%	–5.0% to –2.0%	2.0% to 2.0%	2.0% to 2.0%	2.0% to 2.0%
Hong Kong commercial building price index	Base	0.9% to 0.9%	–7.4% to 4.8%	3.0% to 7.4%	0.0% to 0.0%	3.0% to 3.0%
	Upside	10.3% to 10.3%	1.9% to 6.0%	2.0% to 2.0%	2.0% to 2.0%	5.0% to 5.0%
	Downside	–3.6% to –3.6%	–19.3% to –4.3%	–0.3% to 4.1%	0.0% to 0.0%	0.0% to 0.0%

The weightings assigned to each economic scenario as at 31 December 2019 were as follows:

	Base	Upside	Downside
All portfolios	60%	20%	20%

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.1 Expected credit loss measurement (Continued)

3.1.1.4 Forward-looking information incorporated in the ECL models (Continued)

Economic variable assumptions (Continued)

The most significant period-end assumptions used for the ECL estimate as at 1 January 2019 are set out below. The scenarios "base", "upside" and "downside" were used for all portfolios.

		2018	2019	2020	2021	2022
Hong Kong GDP	Base	2.6% to 2.6%	1.6% to 2.5%	1.9% to 3.0%	2.7% to 3.1%	2.9% to 3.0%
	Upside	2.9% to 2.9%	2.0% to 3.4%	2.0% to 3.2%	3.2% to 3.5%	3.3% to 3.3%
	Downside	0.8% to 0.8%	–1.9% to 0.6%	0.8% to 2.1%	2.4% to 2.8%	2.9% to 3.0%
United States GDP	Base	2.8% to 2.8%	2.3% to 3.5%	1.1% to 1.8%	1.6% to 1.6%	1.5% to 1.5%
	Upside	3.4% to 3.4%	2.4% to 4.2%	2.2% to 2.2%	2.0% to 2.0%	1.5% to 1.5%
	Downside	–0.7% to –0.7%	–1.8% to 0.5%	0.3% to 0.8%	–0.4% to 0.1%	–0.5% to –0.4%
Hong Kong unemployment rate	Base	2.9% to 2.9%	2.8% to 3.1%	2.9% to 3.3%	3.1% to 3.5%	3.4% to 3.7%
	Upside	2.8% to 2.8%	2.8% to 3.2%	3.0% to 3.3%	3.1% to 3.4%	3.2% to 3.4%
	Downside	3.0% to 3.0%	3.4% to 3.6%	3.9% to 4.0%	4.3% to 4.5%	3.0% to 4.8%
United States unemployment rate	Base	3.9% to 3.9%	3.8% to 4.0%	4.2% to 4.6%	4.8% to 5.1%	5.2% to 5.3%
	Upside	3.9% to 3.9%	3.8% to 4.0%	4.2% to 4.4%	4.5% to 4.6%	4.8% to 4.9%
	Downside	4.5% to 4.5%	4.8% to 5.2%	5.4% to 6.0%	6.2% to 7.0%	7.3% to 7.5%
Hong Kong property price index	Base	9.0% to 9.0%	–6.4% to 2.3%	–1.9% to 1.7%	2.8% to 3.9%	0.0% to 0.0%
	Upside	11.0% to 11.0%	–2.2% to 4.5%	2.0% to 7.2%	2.0% to 2.0%	2.0% to 2.0%
	Downside	5.8% to 5.8%	–14.9% to –3.2%	–8.6% to 2.0%	–0.6% to 0.6%	0.0% to 0.0%
United States house price index	Base	3.7% to 3.7%	1.8% to 3.3%	1.2% to 1.8%	1.2% to 3.7%	2.0% to 2.0%
	Upside	4.5% to 4.5%	4.1% to 4.7%	2.2% to 3.1%	1.5% to 4.0%	2.3% to 2.4%
	Downside	1.8% to 1.8%	–1.7% to –0.1%	–3.6% to –2.4%	–5.4% to –1.3%	–3.2% to –2.4%
United Kingdom house price index	Base	4.4% to 4.4%	4.1% to 5.8%	–0.9% to 4.4%	–5.9% to –2.6%	–0.9% to 0.8%
	Upside	4.8% to 4.8%	4.5% to 6.2%	1.7% to 4.4%	0.0% to 0.9%	0.8% to 0.8%
	Downside	3.0% to 3.0%	1.9% to 4.2%	–1.9% to 4.5%	–9.6% to –5.3%	–7.3% to –4.9%
People's Republic of China house price index	Base	9.9% to 9.9%	3.5% to 8.3%	–2.6% to 0.5%	1.0% to 2.0%	2.0% to 2.0%
	Upside	9.9% to 9.9%	3.5% to 8.3%	3.0% to 3.0%	3.0% to 3.0%	3.0% to 3.0%
	Downside	6.4% to 6.4%	–5.0% to –5.0%	–5.0% to –5.0%	2.0% to 2.0%	2.0% to 2.0%
Hong Kong commercial building price index	Base	9.0% to 9.0%	–6.4% to 2.3%	–1.9% to 1.7%	2.8% to 3.9%	0.0% to 0.0%
	Upside	11.0% to 11.0%	–2.2% to 4.5%	2.0% to 7.2%	2.0% to 2.0%	2.0% to 2.0%
	Downside	5.8% to 5.8%	–14.9% to –3.2%	–8.6% to 2.0%	–0.6% to 0.6%	0.0% to 0.0%

The weightings assigned to each economic scenario as at 1 January 2019 were as follows:

	Base	Upside	Downside
All portfolios	60%	20%	20%

3.1.1.5 Sensitivity analysis

The output of the Group's ECL model takes into consideration forward-looking information and scenarios based on the market analysis prepared by the Group's Treasury Research team. The Group has applied appropriate weightings to the base case, upside and downside scenarios which are sources of sensitivity. Two additional sensitivity scenarios (scenarios 1 and 2 below) have been drawn up. Should the weightings applied by the Group be changed to those of the sensitivity scenarios as follows, the impact to ECL amount would be immaterial.

	Base	Upside	Downside
Weightings applied by the Group	60%	20%	20%
Sensitivity scenario 1	40%	30%	30%
Sensitivity scenario 2	80%	10%	10%

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.2 Loss allowance

The loss allowance recognised in the period is impacted by a variety of factors, as described below:

- Transfers between Stage 1, Stage 2 and Stage 3 due to financial instruments experiencing significant increases (or decreases) of credit risk or becoming credit-impaired in the period, and the consequent "step up" (or "step down") between 12-month and Lifetime ECL;
- Additional allowances for new financial instruments recognised during the period, as well as releases for financial instruments de-recognised in the period;
- Impact on the measurement of ECL due to changes in PDs, EADs and LGDs in the period, arising from regular refreshing of inputs to models;
- Impact on the measurement of ECL due to changes made to models and assumptions;
- Discount unwind within ECL due to the passage of time, as ECL is measured on a present value basis;
- Foreign exchange retranslations for assets denominated in foreign currencies and other movements; and
- Write-offs of allowances related to assets that were written off during the period.

Reconciliation of gross carrying amount and allowances for loans and advances to customers are as follows:

	Stage 1		Stage 2		Stage 3		Originated credit-impaired		Total	
	Gross carrying amount	Allowance for ECL	Gross carrying amount	Allowance for ECL	Gross carrying amount	Allowance for ECL	Gross carrying amount	Allowance for ECL	Gross carrying amount	Allowance for ECL
As at 1 January 2018	74,703,040	260,150	3,160,477	51,263	572,090	23,770	28,961	12,258	78,464,568	347,441
Transfer to lifetime ECL	(1,374,194)	(6,995)	1,374,194	15,195	–	–	–	–	–	8,200
Transfer to credit impaired loans and advances	(50,647)	(97)	(34,621)	(595)	85,268	4,847	–	–	–	4,155
Transfer to 12-month ECL	569,820	4,635	(563,036)	(13,878)	(6,784)	(24)	–	–	–	(9,267)
Loans derecognised or repayments	(25,127,881)	(62,876)	(1,280,397)	(8,368)	(96,859)	(4,498)	(7,569)	(239)	(26,512,706)	(75,981)
New loans originated and further lending	34,353,652	125,563	877,439	8,462	33,727	13	5,168	–	35,269,986	134,038
Change in PDs/LGDs/EADs	–	(11,257)	–	(3,084)	–	676	–	(293)	–	(13,958)
Write-offs	–	–	–	–	(4,318)	(4,318)	–	–	(4,318)	(4,318)
Foreign exchange and other movements	(126,746)	(29,624)	(5,549)	2,623	3,025	(600)	–	5	(129,270)	(27,596)
As at 31 December 2018	82,947,044	279,499	3,528,507	51,618	586,149	19,866	26,560	11,731	87,088,260	362,714
As at 1 January 2019	82,947,044	279,499	3,528,507	51,618	586,149	19,866	26,560	11,731	87,088,260	362,714
Transfer to lifetime ECL	(2,129,587)	(11,410)	2,139,724	25,804	(10,137)	(6)	–	–	–	14,388
Transfer to credit impaired loans and advances	(38,723)	(32)	(22,454)	(979)	61,177	7,737	–	–	–	6,726
Transfer to 12-month ECL	437,354	3,285	(409,621)	(7,892)	(27,733)	(75)	–	–	–	(4,682)
Loans derecognised or repayments	(27,110,595)	(57,757)	(1,406,643)	(6,685)	(97,285)	(1,018)	(10,814)	(126)	(28,625,337)	(65,586)
New loans originated and further lending	39,702,404	103,570	1,178,463	9,552	33,815	2,840	15,374	2,726	40,930,056	118,688
Change in PDs/LGDs/EADs	–	(27,940)	–	(2,926)	–	5,870	–	(472)	–	(25,468)
Write-offs	–	–	–	–	(10,808)	(10,808)	–	–	(10,808)	(10,808)
Foreign exchange and other movements	(97,661)	12,970	(99,513)	4,788	2,153	(262)	(59)	(68)	(195,080)	17,428
As at 31 December 2019	93,710,236	302,185	4,908,463	73,280	537,331	24,144	31,061	13,791	99,187,091	413,400

Note: The loans and advances which previously included within "Foreign exchange and other movements" now re-presented to "New loans originated and further lending" and "Loans derecognised or repayments" by distribution, with total carrying amount of HK$3,644,632,000 and HK$5,279,073,000, respectively, to align with current year's presentation. Their allowances for ECL have also been re-presented to align with the presentation.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.3 Write-off policy

The Group writes off financial assets in whole when it has exhausted all practical recovery efforts and has concluded there is no reasonable expectation of recovery. Indicators that there is no reasonable expectation of recovery include (i) ceasing enforcement activity and (ii) the shortfall amount after realization of collateral.

The Group seeks to recover amounts that are legally owed in full, but it writes off financial assets in part when the recovery method is realization of collateral and the value of the collateral is such that there is no reasonable expectation of recovering amounts that are legally owed in full.

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

3.1.5 Maximum exposure to credit risk

	Maximum exposure	
	2019	2018
Financial instruments subject to impairment		
Credit risk exposures relating to on-balance sheet assets are as follows:		
Loans and advances	98,773,691	86,725,546
Balances with banks and placements with banks	40,456,429	36,894,609
Investment securities	69,320,531	61,463,994
Credit risk exposures relating to off-balance sheet items are as follows:		
– Financial guarantees	2,409,657	2,437,941
– Off-balance sheet commitments and other credit related contingent liabilities	50,605,678	48,460,194
Financial instruments not subject to impairment		
Financial assets at fair value through profit or loss	1,881,025	1,858,984
Equity securities at fair value through other comprehensive income	4,718,939	4,348,766
Derivative financial instruments	285,089	313,320

The following table contains an analysis of the credit risk exposure of financial instruments for which an ECL allowance is recognised. The gross carrying amount of financial assets below also represents the Group's maximum exposure to credit risk on these assets, without taking account of any collateral held or other credit enhancements attached.

2019					
	Loans and advances				
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Originated credit-impaired	Total
Credit grade					
Pass	93,121,397	3,160,278	210	1,686	96,283,571
Special Mention	588,810	1,747,997	6	988	2,337,801
Substandard	29	188	102,923	17,350	120,490
Doubtful	–	–	430,655	10,675	441,330
Loss	–	–	3,537	362	3,899
Gross carrying amount	93,710,236	4,908,463	537,331	31,061	99,187,091
ECL	(302,185)	(73,280)	(24,144)	(13,791)	(413,400)
Net carrying amount	93,408,051	4,835,183	513,187	17,270	98,773,691

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.5 Maximum exposure to credit risk (Continued)

2018

	Loans and advances				
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Originated credit-impaired	Total
Credit grade					
Pass	81,756,510	2,145,241	254	533	83,902,538
Special Mention	1,190,486	1,383,206	67	6,487	2,580,246
Substandard	48	60	129,739	7,966	137,813
Doubtful	–	–	452,339	11,574	463,913
Loss	–	–	3,750	–	3,750
Gross carrying amount	82,947,044	3,528,507	586,149	26,560	87,088,260
ECL	(279,499)	(51,618)	(19,866)	(11,731)	(362,714)
Net carrying amount	82,667,545	3,476,889	566,283	14,829	86,725,546

As at 31 December 2019, 98% (2018: 97%) of the off-balance sheet items are "Pass" and 2% (2018: 3%) are "Special Mention". The amount classified as "Substandard", "Doubtful" or "Loss" are immaterial. Majority of the ECL are provided on stage 1 (2018: stage 1).

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

"Special Mention" represents loans with deficiencies and potential weakness such that if adverse conditions persist, loss of principal or interest for the Bank may occur.

"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 losses of principal or interest are possible.

"Doubtful" represents loans which the Group expects to sustain a loss of interest and/or principal.

"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.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.5 Maximum exposure to credit risk (Continued)

The table below presents an analysis of debt securities by rating agency designation for the respective issues as at 31 December, based on Standard & Poor's ratings or their equivalent. In the absence of such issue ratings, the ratings designated for the issuers are reported.

	Investment securities					
	2019			2018		
	Investment securities at fair value through other comprehensive income	Investment securities at amortised cost	Total	Investment securities at fair value through other comprehensive income	Investment securities at amortised cost	Total
Credit grade						
AAA	1,497,657	–	1,497,657	1,332,403	–	1,332,403
AA – to AA+	14,928,202	2,442,022	17,370,224	15,707,663	2,374,517	18,082,180
A – to A+	36,867,032	–	36,867,032	31,468,502	–	31,468,502
BBB – to BBB+	8,630,279	38,922	8,669,201	6,920,661	39,153	6,959,814
Unrated	4,916,437	–	4,916,437	3,621,115	–	3,621,115
Gross carrying amount	66,839,607	2,480,944	69,320,551	59,050,344	2,413,670	61,464,014
Stage 1 ECL	7,959	20	7,979	9,042	20	9,062

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.6 Concentration of credit risk of financial assets

International claims

The following table shows the Group's international claims by major country or geographical segment, each representing 10% or more of the Group's total international claims. International claims refer to exposures to counterparties on which the ultimate risk lies, and are derived according to the location of the counterparties after taking into account any recognised risk transfer. In general, transfer of risk from one country to another is recognised if the claims against a counterparty are guaranteed by another party in a different country or if the claims are on an overseas branch of a bank whose head office is located in a different country.

As at 31 December 2019

			Non-bank private sector		
	Banks	Official sector	Non-bank financial institutions	Non-financial private sector	Total
Developed countries	21,027,000	315,000	1,987,000	718,000	24,047,000
Offshore centres	5,969,000	63,000	3,967,000	27,560,000	37,559,000
– of which Hong Kong	4,009,000	63,000	1,953,000	22,778,000	28,803,000
Developing Asia-Pacific	45,486,000	194,000	252,000	8,203,000	54,135,000
– of which China	33,672,000	194,000	252,000	6,689,000	40,807,000

As at 31 December 2018

			Non-bank private sector		
	Banks	Official sector	Non-bank financial institutions	Non-financial private sector	Total
Developed countries	20,649,000	381,000	1,794,000	871,000	23,695,000
Offshore centres	4,749,000	7,000	3,305,000	17,892,000	25,953,000
– of which Hong Kong	3,719,000	7,000	1,864,000	13,819,000	19,409,000
Developing Asia-Pacific	46,056,000	69,000	256,000	6,001,000	52,382,000
– of which China	37,016,000	69,000	256,000	4,832,000	42,173,000

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.7 Loans and advances (excluding trade bills and other eligible bills)

(a) Loans and advances by industry sector

The following table shows the breakdown of the Group's loans and advances (excluding trade bills and other eligible bills) by industry sector according to the usage of loans based on the categories and definitions set by the Hong Kong Monetary Authority ("HKMA").

	2019		2018	
	Balance	% covered by collateral	Balance	% covered by collateral
Loans for use in Hong Kong				
Industrial, commercial and financial				
– Property development	4,870,738	53%	5,354,479	54%
– Property investment	6,878,804	93%	7,302,076	93%
– Financial concerns	2,176,346	8%	312,458	79%
– Stockbrokers	460,367	20%	520,812	75%
– Wholesale and retail trade	2,199,875	47%	3,201,529	30%
– Manufacturing	1,253,394	71%	1,494,476	66%
– Transport and transport equipment	415,212	96%	279,852	89%
– Recreational activities	526,287	85%	255,442	72%
– Information technology – telecommunication	85,777	70%	89,264	70%
– Hotels, boarding houses and catering	1,912,016	90%	2,250,871	88%
– Others	14,030,765	58%	9,185,296	75%
Individuals				
– Loans for the purchase of flats in the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme or their respective successor schemes	82,168	100%	90,423	100%
– Loans for the purchase of other residential properties	4,066,948	100%	4,118,120	100%
– Credit card advances	195,944	0%	203,890	0%
– Others	7,205,968	93%	6,534,583	96%
Trade financing	7,894,868	68%	7,494,542	62%
Loans for use outside Hong Kong	44,558,560	86%	37,946,027	86%
	98,814,037	77%	86,634,140	80%

As at 31 December 2019 and 2018, the Bank did not have exposures to individual industry sector constituting 10% or more of the Group's total amount of loans and advances.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.7 Loans and advances (excluding trade bills and other eligible bills) (Continued)

(b) Loans and advances by geographical area

The information concerning the breakdown of the gross amount of loans and advances to customers (excluding trade bills and other eligible bills) by country or geographical area is derived according to the location of the customers after taking into account any transfer of risk. In general, such transfer of risk takes place if the loans and advances are guaranteed by a party in a country which is different from that of the customers.

As at 31 December 2019

	Balance	Stage 3 balance	Balance overdue for over 3 months	Total Stage 3 impairment allowances	Total Stage 1 and Stage 2 impairment allowances
Hong Kong	62,849,908	496,248	427,878	20,500	311,987
Mainland China	7,383,429	60,507	44,913	17,435	11,155
United States	24,185,044	6,675	6,675	–	38,650
Others	4,395,656	3,348	–	–	13,264
	98,814,037	566,778	479,466	37,935	375,056
% of total loans and advances to customers		0.57			
Fair value of collateral		1,389,110			

As at 31 December 2018

	Balance	Stage 3 balance	Balance overdue for over 3 months	Total Stage 3 impairment allowances	Total Stage 1 and Stage 2 impairment allowances
Hong Kong	53,952,274	548,582	421,848	20,374	275,850
Mainland China	6,676,279	35,902	35,902	11,107	10,526
United States	21,152,386	14	14	9	31,900
Others	4,853,201	22,526	18,435	107	12,399
	86,634,140	607,024	476,199	31,597	330,675
% of total loans and advances to customers		0.70			
Fair value of collateral		1,487,205			

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Credit risk (Continued)

3.1.7 Loans and advances (excluding trade bills and other eligible bills) (Continued)

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

	2019		2018	
		% of gross loans and advances to customers		% of gross loans and advances to customers
Balances which have been overdue for:				
– 6 months or less but over 3 months	46,975	0.05	29,087	0.03
– 1 year or less but over 6 months	2,049	–	9,601	0.01
– over 1 year	430,442	0.44	437,511	0.51
	479,466	0.49	476,199	0.55
Current market value of collateral	1,184,434		1,157,462	
Covered portion by collateral	459,602		466,168	
Uncovered portion by collateral	19,864		10,031	
Impairment allowances	34,674		18,853	

Collateral held against such loans and advances mainly include mortgages over properties.

(d) Rescheduled loans and advances (net of amounts included in loans and advances overdue for more than 3 months)

	2019		2018	
		% of gross loans and advances to customers		% of gross loans and advances to customers
Rescheduled loans and advances	17,768	0.02	25,810	0.03

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

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 foreign exchange and equity contracts, that comprise transactions initiated for the Group's own account and customer needs. The Group's positions are managed by the Treasury Division under the limits and guidelines laid down in the foreign exchange risk management policy and the policy on allocating transactions of financial instruments to the trading, non-trading or investment book, which are approved by the Executive Committee and the Risk Committee. The Risk Management Division is responsible for monitoring the transactions to ensure the activities are within the relevant limits and guidelines.

3.2.1 Market risk measurement techniques

The measuring procedures and limit system used for market risk management have been approved by the Executive Committee (and also Risk Committee for the measuring procedures). Limits on notional, stop loss and sensitivity are set for trading positions which are marked-to-market daily.

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, the Asset and Liability Committee, the Executive Committee, the Risk Committee and the Board of Directors.

3.2.2 Market risk sensitivity summary

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 foreign exchange rate and interest rate contracts which are typically made over-the-counter and are managed within limits approved by the Executive Committee and the Risk Committee. The policy on the use of derivatives is reviewed by the Risk Committee and recommended changes and amendments are approved by the Executive Committee or the Risk Committee.

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 Division and monitored by the Risk Management Division, management and the Asset and Liability Committee within position limits set in the foreign exchange risk management policy approved by the Executive Committee and the Risk Committee. The Board sets limits on the level of exposure by currency and in aggregate for both overnight and intra-day positions, which are monitored on a daily basis. The table below summarises the Group's exposure to foreign currency exchange rate risk as at 31 December. Included in the table are the Group's financial instruments at carrying amounts, categorised by currency.

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

As at 31 December 2019	HKD	USD	RMB	Other	Total
Assets					
Cash and balances with banks	5,372,535	18,571,074	5,941,493	4,243,512	34,128,614
Placements with banks	3,949,894	2,191,401	814,665	134,596	7,090,556
Loans and advances to customers	55,201,124	31,461,424	6,060,172	6,050,971	98,773,691
Financial assets at fair value through profit or loss	27,585	1,853,440	–	–	1,881,025
Derivative financial instruments	55,859	74,020	60,006	95,204	285,089
Investment securities at fair value through other comprehensive income	34,944,515	24,219,873	10,056,078	2,338,080	71,558,546
Investment securities at amortised cost	2,045,006	435,918	–	–	2,480,924
Other assets	1,181,785	469,719	120,397	42,366	1,814,267
Total	102,778,303	79,276,869	23,052,811	12,904,729	218,012,712
Liabilities					
Deposits and balances from banks	955,759	5,685,808	3,392,585	1,643,458	11,677,610
Deposits from customers	86,958,501	63,309,583	14,034,177	8,136,255	172,438,516
Derivative financial instruments	17	133,020	70,470	89,092	292,599
Subordinated debts	–	4,257,647	–	–	4,257,647
Other liabilities	1,917,813	704,704	147,552	43,814	2,813,883
Total	89,832,090	74,090,762	17,644,784	9,912,619	191,480,255
Net on-balance sheet position	12,946,213	5,186,107	5,408,027	2,992,110	26,532,457
Credit commitments	31,000,027	19,953,814	1,538,350	535,247	53,027,438

As at 31 December 2018	HKD	USD	RMB	Other	Total
Assets					
Cash and balances with banks	10,020,094	13,096,914	2,595,027	2,896,463	28,608,498
Placements with banks	3,799,836	2,629,639	1,206,320	1,007,927	8,643,722
Loans and advances to customers	48,156,300	29,188,721	4,937,375	4,443,150	86,725,546
Financial assets at fair value through profit or loss	26,111	1,832,439	–	434	1,858,984
Derivative financial instruments	55,250	16,695	216,999	24,376	313,320
Investment securities at fair value through other comprehensive income	29,670,914	19,191,330	11,865,770	2,671,096	63,399,110
Investment securities at amortised cost	2,024,790	388,860	–	–	2,413,650
Other assets	798,200	375,531	184,301	63,463	1,421,495
Total	94,551,495	66,720,129	21,005,792	11,106,909	193,384,325
Liabilities					
Deposits and balances from banks	1,075,600	5,234,025	2,278,199	1,757,164	10,344,988
Deposits from customers	80,112,105	52,605,281	13,283,465	8,613,867	154,614,718
Derivative financial instruments	46	72,717	214,479	18,489	305,731
Subordinated debts	–	1,945,079	–	–	1,945,079
Other liabilities	1,764,753	463,225	158,967	29,244	2,416,189
Total	82,952,504	60,320,327	15,935,110	10,418,764	169,626,705
Net on-balance sheet position	11,598,991	6,399,802	5,070,682	688,145	23,757,620
Credit commitments	30,367,602	18,617,285	1,244,960	681,046	50,910,893

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.2 Market risk (Continued)

3.2.4 Interest rate risk in the banking book ("IRRBB")

General information about IRRBB

The primary forms of IRRBB faced by the Group can be divided into three broad categories:

– Gap risk is the risk arising from changes in the interest rates on instruments of different maturities. The extent of gap risk depends on whether changes to the term structure of interest rates occur consistently across the yield curve (parallel risk) or differentially by period (non-parallel risk). Parallel risk is fundamental to banking business and this risk is taken on the balance sheet as part of the strategy to improve earnings. It can, however, affect the income and economic value of the Group as interest rates fluctuate. Non-parallel risk materialises when unanticipated changes in the shape of the yield curve have adverse effects on the Group's income or economic value.

– Basis risk arises from imperfect correlation between changes in the rates earned and paid on different instruments with otherwise similar repricing characteristics. As a result of these differences, the cash flows and earnings spread between assets, liabilities and off-balance sheet instruments of similar maturities or repricing frequencies will change.

– Option risk arises from interest rate option derivatives or from optional elements embedded in the Group's assets, liabilities and/or off-balance sheet instruments, where the customers can alter the level and timing of their cash flows. Option risk can be further characterised into automatic option risk and behavioural option risk. Automatic option risk arises from standalone instruments, such as exchange-traded and over-the-counter option contracts, or options explicitly embedded within an otherwise standard financial instrument, where the option will almost certainly be exercised if it is in the holder's financial interest to do so. Behavioural option risk arises from the flexibility embedded implicitly or within the terms of financial contracts, such that changes in interest rates may affect the behaviour of the customer.

Apart from the three sources of risks listed above, which are directly linked to IRRBB, credit spread risk in the banking book ("CSRBB") is a related risk that is monitored and assessed within interest rate risk management framework. CSRBB refers to any kind of asset/liability spread risk of credit-risky instruments that is not explained by IRRBB or by the expected credit risk or jump to default risk.

Governance of IRRBB risk management

The Group's IRRBB risk management framework follows a hierarchy structure:

The Executive Committee and Risk Committee are delegated by the Board to be responsible for ensuring that an appropriate interest rate risk management structure, which identifies the lines of authorities and responsibilities for different levels of management is established, maintaining continued awareness of the Group's performance and overall interest rate risk, and ensuring the interest rate risk is adequately managed and controlled within the established risk management framework.

The Asset and Liability Committee is responsible for managing the overall interest rate risk of the Group, reviewing the report on interest rate risk position and reporting regularly on interest rate risk management to the Executive Committee and Risk Committee.

The Treasury Division is responsible for the day-to-day management of interest rate risk for the Group including branches of the Bank outside Hong Kong under the guidelines and limits approved by the Executive Committee and Risk Committee.

The Risk Management Division is responsible for monitoring the day-to-day management of the interest rate risk for the Group including branches of the Bank outside Hong Kong, reporting identified irregularities and taking appropriate remedial actions. It is also responsible to conduct regular stress test on interest rate risk and review the IRRBB behavioural assumption on a periodic basis.

The Internal Audit Department is responsible for conducting periodic review on the internal control and risk management process for interest rate risk to ensure its integrity, accuracy and reasonableness.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.2 Market risk (Continued)

3.2.4 Interest rate risk in the banking book ("IRRBB") (Continued)

IRRBB risk measure

The IRRBB is assessed daily with risk indicators, such as the repricing gap and the sensitivity of the net interest income ("NII") and economic value of equity ("EVE") under interest rate shock and stress scenarios.

Six interest rate shock scenarios prescribed by the HKMA under the completion instruction for the "Return of Interest Rate Risk in the Banking Book" are applied to the Group's banking book. They include parallel shifts up and down of the interest rate curve, and non-parallel shifts such as a steepening or flattening of the interest rate curve, as well as shifting the short rate up and down relative to the long rate. The sensitivity of the EVE is specified as the maximum decrease of the banking book economic value under the six interest rate shock scenarios. Likewise, the sensitivity of the NII is specified as the maximum reduction in NII under the parallel shifts up and down scenarios, compared to the base scenario, over a period of 12 months. Additional scenarios are also applied for Internal Capital Adequacy Assessment Process purposes, which make reference to historical scenarios such as the Asian Financial Crisis in 1997 and the Global Financial Crisis in 2008, to estimate the IRRBB capital charge under those stressed scenarios.

IRRBB related hedging decisions are made by the Asset and Liability Committee and executed in the market by the Treasury Division. The Group has not designated any derivatives in any hedge relationship for the application of hedge accounting.

Key modelling and parametric assumptions

For EVE change/impact, commercial margins and other spread components have been included in the cash flow profiling, while the discount curves used are risk-free yield curves without spread components.

For Non-maturity deposits ("NMDs"), these are segmented into several sub-portfolios according to entity (such as head office and overseas branches), customer type and transaction type (such as retail and non-retail accounts, and transactional and non-transactional accounts), currency, and product type (such as current and savings accounts). It is assumed that customer behaviours within the same sub-portfolio are homogeneous. For each sub-portfolio, the average repricing maturity is determined after:

– Stable NMDs over a 10-year historical horizon are identified;

– The Core Deposit Ratio is estimated based on historical interest rate changes; and

– Slotting rates for NMDs repricing, which are subject to average repricing maturity caps in accordance with the customer types, are constructed.

The average and longest repricing maturity of the NMDs of major currencies as at 31 December 2019 were 1.68 years and 8.33 years respectively.

For fixed rate loan prepayment, a statistical behavioural model is developed using the historical data for retail fixed rate loans, which are segmented into sub-portfolios by product type and branches and further by homogeneous groups with similar prepayment behaviour categorized by currency, customer type, tenor, etc. This allows the conditional prepayment rates ("CPR") to be estimated. The parameters are then applied in cash flow slotting for reporting.

For early withdrawal of time deposits, a statistical behavioural model is developed using the historical data for retail term deposits to estimate early withdrawal rates. The term deposit portfolio is segmented into sub-portfolios by currency and tenor group with homogeneous early redemption behaviour for modelling.

Quantitative disclosure

The new standard on IRRBB as set out by the HKMA per Supervisory Policy Manual IR-1 became effective on 1 July 2019 to replace the non-statutory guideline "Interest Rate Risk Management" issued by the HKMA in 2002. The IRRBB introduces six interest rate shock scenarios (namely interest yield curve parallel up, parallel down, steepener, flattener, short rate up and short rate down) for assessing the impact in economic value of equity ("EVE") and net interest income ("NII") in respect of the interest rate exposures arising from banking book positions.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.2 Market risk (Continued)

3.2.4 Interest rate risk in the banking book ("IRRBB") (Continued)

Quantitative disclosure (Continued)

The table below shows the negative impact in economic value of equity ("ΔEVE") and changes in net interest income ("ΔNII") over next 12 months under the six interest rate shock scenarios ("six scenarios") for Hong Kong dollar banking books based on the financial position as at 31 December 2019. The maximum losses among the six scenarios on EVE and NII would have been HK$100 million and HK$248 million respectively.

(Currency: HKD only)		(a) ΔEVE*	(b) ΔNII**
	Scenario	2019	
1	Parallel up	–	(248,000)
2	Parallel down	100,000	248,000
3	Steepener	2,000	
4	Flattener	62,000	
5	Short rate up	62,000	
6	Short rate down	63,000	
	Maximum loss	100,000	248,000
	Tier 1 capital	27,572,305	

* Positive value indicates negative impact in EVE

** Negative value indicates increase in NII, positive value indicates decrease in NII

The table below shows the negative impact in economic value of equity ("ΔEVE") and changes in net interest income ("ΔNII") over next 12 months under the six scenarios for banking books comprising major currencies including HKD based on the financial position as at 31 December 2019. The maximum losses among the six scenarios on EVE and NII would have been HK$299 million and HK$282 million respectively.

(All major currencies including HKD) Equivalent in Hong Kong dollars		(a) ΔEVE*	(b) ΔNII**
	Scenario	2019	
1	Parallel up	299,000	(279,000)
2	Parallel down	100,000	282,000
3	Steepener	25,000	
4	Flattener	84,000	
5	Short rate up	246,000	
6	Short rate down	70,000	
	Maximum loss	299,000	282,000
	Tier 1 capital	27,572,305	

* Positive value indicates negative impact in EVE

** Negative value indicates increase in NII, positive value indicates decrease in NII

As at 31 December 2018, the variations in earnings over the next 12 months for 200 basis points interest rate rise, broken down by currencies, were as follows. The effect of decline or increase in earnings with interest rate risk shock of 200 basis points downward were contra to that with interest rate risk shock of 200 basis points upward. The analysis is based on the methodology as set out by the HKMA in the completion instructions for the "Return of Interest Rate Risk Exposure" prior to 1 July 2019.

2018	Currency				
Equivalent in Hong Kong Dollars	HKD	USD	RMB	Others	Total
Increase/(decline) in earnings arising from interest rate risk shock of 200 basis points upward	351,984	32,726	(26,106)	(61,618)	296,986

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

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 is managed by the Treasury Division and monitored by management and the Asset and Liability Committee in accordance with the guidelines and procedures laid down in the liquidity risk management policy approved by the Board of Directors, which has regard to a variety of factors, including liquidity maintenance ratio, loan to deposit ratio, liquidity cushion, maturity mismatch profile, diversity and stability of the deposit base and ability to borrow in the interbank market to ensure that both the funding liquidity and market liquidity are properly handled. 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 under both normal business conditions and emergency situations.

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 liquidity maintenance 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 (Note 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.

The Group conducts stress testing regularly to analyse liquidity risk. The Group's stress tests are conducted with hypothetical as well as historical assumptions. Both funding and market liquidity risks are addressed. Three stress scenarios including the institution-specific crisis, the general market crisis and the combined crisis are adopted with minimum survival period defined according to Supervisory Policy Manual LM-2 "Sound Systems and Controls for Liquidity Risk Management" of the HKMA.

With reference to the stress-testing results, the Group identifies potential vulnerability within the Group, and formulates a Contingency Funding Plan, a component of the Group's Business Continuity Plan, to describe the Group's strategy for dealing with any liquidity problem and the procedures for making up cash flow deficits in emergency situations.

Annual drill test is conducted and the Contingency Funding Plan is subject to regular review in order to cope with the changes of business environment. Any significant changes to the Contingency Funding Plan are approved by the Board of Directors.

The Group also performs reverse stress-testing in accordance with the HKMA's Supervisory Policy Manual IC-5 "Stress-testing". It is a process of working backwards from the event causing business failures and involves a mix of qualitative and quantitative analyses. The Group uses results of stress-testing and reverse stress-testing to strengthen resilience to liquidity stress and serve as early-warning triggers for the formulation of management actions and contingency funding plan to mitigate potential stress and vulnerability which the Group might face.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.3 Liquidity risk (Continued)

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 reporting date to the contractual maturity date.

As at 31 December 2019	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	8,634,242	25,494,372	–	–	–	–	–	34,128,614
Placements with banks	–	–	3,138,599	3,951,957	–	–	–	7,090,556
Loans and advances to customers	5,493,495	5,566,299	10,536,189	22,349,213	36,015,386	18,201,327	611,782	98,773,691
Financial assets at fair value through profit or loss	–	2,277	–	7,898	18,179	1,825,087	27,584	1,881,025
Derivative financial instruments	–	48,398	53,318	127,613	55,760	–	–	285,089
Investment securities at fair value through other comprehensive income	–	4,259,517	10,597,303	22,351,737	25,707,988	3,920,188	4,721,813	71,558,546
Investment securities at amortised cost	–	31,104	1,009,042	1,417,323	23,455	–	–	2,480,924
Properties for sale	–	–	–	–	449,462	–	–	449,462
Investments in associates and joint venture	–	–	–	–	–	–	417,663	417,663
Properties and equipment	–	10,318	19,363	76,806	175,116	78,583	2,339,828	2,700,014
Investment properties	–	–	–	–	–	–	1,017,148	1,017,148
Deferred income tax assets	–	–	–	–	–	–	28,115	28,115
Other assets	197,993	789,679	118,179	279,506	348,809	75,787	4,314	1,814,267
Total assets	14,325,730	36,201,964	25,471,993	50,562,053	62,794,155	24,100,972	9,168,247	222,625,114
Liabilities								
Deposits and balances from banks	1,260,751	6,018,335	3,585,042	813,482	–	–	–	11,677,610
Deposits from customers	60,399,842	39,696,628	43,196,509	28,885,935	259,602	–	–	172,438,516
Derivative financial instruments	–	49,274	52,804	134,761	55,760	–	–	292,599
Subordinated debts	–	–	–	–	–	4,257,647	–	4,257,647
Other liabilities	311,291	1,135,109	374,909	685,440	226,262	80,262	610	2,813,883
Current income tax liabilities	–	407,914	93,780	–	–	–	–	501,694
Deferred income tax liabilities	–	–	–	–	–	–	18,901	18,901
Total liabilities	61,971,884	47,307,260	47,303,044	30,519,618	541,624	4,337,909	19,511	192,000,850
Net liquidity gap	(47,646,154)	(11,105,296)	(21,831,051)	20,042,435	62,252,531	19,763,063	9,148,736	30,624,264
Of which lease liabilities included in:								
Other liabilities	–	9,914	18,793	74,979	192,575	80,262	–	376,523

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.3 Liquidity risk (Continued)

3.3.2 Maturity analysis (Continued)

As at 31 December 2018

	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	10,001,422	18,607,076	–	–	–	–	–	28,608,498
Placements with banks	–	–	5,939,072	2,704,650	–	–	–	8,643,722
Loans and advances to customers	4,632,344	6,175,346	9,030,892	17,597,946	29,717,025	18,963,160	608,833	86,725,546
Financial assets at fair value through profit or loss	–	–	–	50,248	86,325	1,695,866	26,545	1,858,984
Derivative financial instruments	–	36,893	53,398	171,287	51,742	–	–	313,320
Investment securities at fair value through other comprehensive income	–	8,246,584	1,227,739	12,841,803	36,553,760	177,584	4,351,640	63,399,110
Investment securities at amortised cost	–	7,826	2,087,260	256,254	62,310	–	–	2,413,650
Properties for sale	–	–	–	–	–	–	416,346	416,346
Investments in associates and joint venture	–	–	–	–	–	–	388,447	388,447
Properties and equipment	–	–	–	–	–	–	2,332,709	2,332,709
Investment properties	–	–	–	–	–	–	1,025,892	1,025,892
Deferred income tax assets	–	–	–	–	–	–	72,193	72,193
Other assets	59,950	644,541	79,110	194,759	385,598	53,120	4,417	1,421,495
Total assets	14,693,716	33,718,266	18,417,471	33,816,947	66,856,760	20,889,730	9,227,022	197,619,912
Liabilities								
Deposits and balances from banks	1,218,308	5,414,546	2,601,190	1,110,944	–	–	–	10,344,988
Deposits from customers	62,975,284	34,938,324	35,444,777	21,140,974	115,359	–	–	154,614,718
Derivative financial instruments	–	41,868	46,356	165,765	51,742	–	–	305,731
Subordinated debts	–	–	–	–	–	1,945,079	–	1,945,079
Other liabilities	830,983	893,281	346,377	342,906	2,642	–	–	2,416,189
Current income tax liabilities	–	–	91,316	–	–	–	–	91,316
Deferred income tax liabilities	–	–	–	–	–	–	27	27
Total liabilities	65,024,575	41,288,019	38,530,016	22,760,589	169,743	1,945,079	27	169,718,048
Net liquidity gap	(50,330,859)	(7,569,753)	(20,112,545)	11,056,358	66,687,017	18,944,651	9,226,995	27,901,864
Of which lease liabilities included in:								
Other liabilities	–	–	–	–	–	–	–	–

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 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.3 Liquidity risk (Continued)

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 reporting date. The amounts disclosed in the table are the contractual undiscounted cash flow, whereas the Group manages the liquidity risk based on a different basis, but they do not result in a significantly different analysis.

As at 31 December 2019	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Liabilities						
Deposits and balances from banks	7,285,244	3,624,031	828,468	–	–	11,737,743
Deposits from customers	100,329,884	43,554,088	29,486,720	280,571	–	173,651,263
Subordinated debts	58,383	–	131,361	758,974	5,002,025	5,950,743
Other liabilities	1,207,537	84,889	538,862	234,355	81,022	2,146,665
Total	108,881,048	47,263,008	30,985,411	1,273,900	5,083,047	193,486,414
Assets held for managing liquidity risk	49,880,457	26,070,406	52,845,904	68,312,827	35,727,468	232,837,062

As at 31 December 2018	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Liabilities						
Deposits and balances from banks	6,639,777	2,632,537	1,147,316	–	–	10,419,630
Deposits from customers	98,094,052	35,679,125	21,588,909	123,280	–	155,485,366
Subordinated debts	–	–	73,410	293,640	2,238,719	2,605,769
Other liabilities	1,546,245	183,646	250,686	2,158	–	1,982,735
Total	106,280,074	38,495,308	23,060,321	419,078	2,238,719	170,493,500
Assets held for managing liquidity risk	48,017,215	18,969,131	36,002,026	72,180,818	31,651,119	206,820,309

Assets available to meet all of the liabilities and to cover outstanding loan commitments include cash and balances with banks, placements with banks, loans and advances to customers, investment securities at fair value through other comprehensive income, investment securities at amortised cost and financial assets at fair value through profit or loss. In addition, debt securities can be pledged to secure liabilities, if necessary. 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.

The Group's policy defines the size and composition of liquidity cushion. The Group's liquidity cushion includes but not limited to high quality government securities such as Exchange Fund papers and the United States Treasury securities.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.3 Liquidity risk (Continued)

3.3.5 Derivative liabilities

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 reporting date 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.

As at 31 December 2019	Up to 1 month	1-3 months	3-12 months	1-5 years	Total
Derivatives held for trading:					
Exchange rate contracts					
– Outflow	26,554,972	12,634,691	46,991,915	19,049,856	105,231,434
– Inflow	26,556,235	12,635,957	46,991,404	19,049,856	105,233,452

As at 31 December 2018	Up to 1 month	1-3 months	3-12 months	1-5 years	Total
Derivatives held for trading:					
Exchange rate contracts					
– Outflow	9,691,432	10,286,822	40,811,237	19,971,573	80,761,064
– Inflow	9,686,799	10,295,612	40,820,040	19,971,573	80,774,024

3.3.6 Off-balance sheet items

The contractual maturity profile of off-balance sheet items including contingent liabilities and commitments is included in Note 36.

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.4 Fair value of financial assets and liabilities

(a) Financial instruments not measured at fair value

(i) Balances with banks and placements with banks

Balances with banks and placements with banks include inter-bank placements and are stated net of impairment allowances. The maturities of these financial assets are within one year. The carrying amount at the reporting date approximates their fair value.

(ii) Loans and advances to customers

Loans and advances are stated net of impairment allowances. An insignificant portion of loans and advances to customers bears interest at fixed rate. The carrying amount at the reporting date approximates their fair value.

(iii) Investment securities at amortised cost

The fair value for investment securities at amortised cost 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. For the carrying value of investment securities at amortised cost, please refer to Note 22. The fair value of investment securities at amortised cost is classified under Level 1 (2019: HK$2,479,459,000, 2018: HK$2,412,583,000) in the fair value hierarchy. Please refer to Note 3.4(b) for the definition of fair value hierarchy.

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

Substantially all the deposits and balances from banks and deposits from customers will mature within 1 year from the reporting date. Hence, the carrying amount at the reporting date approximates their fair value.

(v) Subordinated debts

The fair value of subordinated debts of HK$4,430,988,000 (2018: HK$1,896,606,000) is classified under Level 2 in the fair value hierarchy.

(b) Fair value hierarchy

Valuation governance

The Group has in place fair valuation policy to ensure adequate governance and control processes for the designation and valuation of financial instruments to be measured at fair value for financial reporting, risk management and regulatory capital purposes. The valuation process is conducted by control units independent of risk taking units.

The Group is to recognise transfers into and transfers out of fair value hierarchy levels as of that date of the event or change in circumstances that caused the transfer.

HKFRS 13 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, funds and debt securities on exchanges and paper gold.

Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the assets or liabilities, either directly (that is, as prices) or indirectly (that is, derived from prices). This level includes instruments such as over-the-counter derivative contracts, unlisted equity securities and unlisted debt securities. Observable parameters that are used as input include market data such as HIBOR and LIBOR yield curves and exchange rate implied volatilities.

Level 3 – Inputs for the assets or liabilities that are not based on observable market data (unobservable inputs). This level includes unlisted equity securities and unlisted debt securities 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)

Recurring fair value measurement

As at 31 December 2019	Level 1	Level 2	Level 3	Total
Financial assets at fair value through profit or loss				
Debt securities	–	1,853,440	–	1,853,440
Equity securities	20,391	–	7,194	27,585
Derivative financial instruments				
Exchange rate contracts	–	285,089	–	285,089
Investment securities at fair value through other comprehensive income				
Debt securities	33,689,617	33,147,116	2,874	66,839,607
Equity securities	4,657,821	–	61,118	4,718,939
Total Assets	38,367,829	35,285,645	71,186	73,724,660
Derivative financial instruments				
Exchange rate contracts	–	292,599	–	292,599
Total Liabilities	–	292,599	–	292,599

As at 31 December 2018	Level 1	Level 2	Level 3	Total
Financial assets at fair value through profit or loss				
Debt securities	–	1,832,439	–	1,832,439
Equity securities	20,094	–	6,017	26,111
Others	434	–	–	434
Derivative financial instruments				
Exchange rate contracts	–	313,320	–	313,320
Investment securities at fair value through other comprehensive income				
Debt securities	28,707,157	30,340,313	2,874	59,050,344
Equity securities	4,288,351	–	60,415	4,348,766
Total Assets	33,016,036	32,486,072	69,306	65,571,414
Derivative financial instruments				
Exchange rate contracts	–	305,731	–	305,731
Total Liabilities	–	305,731	–	305,731

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

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

3.4 Fair value of financial assets and liabilities (Continued)

(b) Fair value hierarchy (Continued)

Level 2 fair values of unlisted debt securities are determined based on quotes from brokers. The most significant input is discount rate of the instruments.

Level 2 fair values of exchange rate contracts are determined using forward exchange rates and implied volatilities at the reporting date, with the resulting value discounted back to present value.

Level 3 fair values of unlisted equity securities and debentures are determined based on valuation techniques using significant unobservable inputs, which includes the market comparison approach and the dividend discount approach. The fair value is positively correlated to the price to book ratio of appropriate comparables or dividend growth rate.

If the significant unobservable inputs would be shifted by +/– 5%, the impact on other comprehensive income would be increased by HK$3,584,000 (2018: HK$5,219,000) or decreased by HK$3,289,000 (2018: HK$4,459,000) and profit or loss would be increased/decreased by HK$360,000 (2018: HK$301,000) respectively.

The following table presents the changes in level 3 instruments for the years ended 31 December 2018 and 2019 respectively.

	Financial assets at fair value through profit or loss		Investment securities at fair value through other comprehensive income		
	Equity securities	Total	Equity securities	Debt securities	Total
As at 1 January 2018	4,369	4,369	29,546	2,874	32,420
Total gains					
– Profit	1,648	1,648	–	–	–
– Other comprehensive income	–	–	19,722	–	19,722
Purchases	–	–	11,100	–	11,100
Exchange adjustments	–	–	47	–	47
As at 31 December 2018	6,017	6,017	60,415	2,874	63,289
As at 1 January 2019	**6,017**	**6,017**	**60,415**	**2,874**	**63,289**
Total gains					
– Profit	**1,177**	**1,177**	**–**	**–**	**–**
– Other comprehensive income	**–**	**–**	**926**	**–**	**926**
Exchange adjustments	**–**	**–**	**(223)**	**–**	**(223)**
As at 31 December 2019	**7,194**	**7,194**	**61,118**	**2,874**	**63,992**

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 ("BCR") 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 BCR. The required information is filed with the HKMA periodically.

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 statutory minimum ratio. 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 regulatory capital of the Group comprises the following:

- Common Equity Tier 1 ("CET1") capital and Tier 1 capital: share capital, general reserve, investment revaluation reserve and retained earnings; and
- Tier 2 capital: subordinated debts, Stage 1 and Stage 2 impairment allowances and regulatory reserve.

	2019	2018
CET1 capital ratio	**16.2%**	16.6%
Tier 1 capital ratio	**16.2%**	16.6%
Total capital ratio	**19.5%**	18.6%

3 FINANCIAL RISK MANAGEMENT (CONTINUED)

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 Risk Committee. The Operational Risk Management Department is responsible for the central operational risk management function. Policies and procedures have been established to control exposures and to identify operational risk factors. Insurance policies are taken to mitigate unforeseeable operational risk. 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 JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Group's financial statements and its financial results are influenced by accounting policies, assumptions, estimates, and management judgements 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.

Measurement of the ECL allowance

The measurement of the ECL allowance for financial assets measured at amortised cost and FVOCI is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behaviour (e.g. the likelihood of customers defaulting and the resulting losses). Explanation of the inputs, assumptions and estimation techniques used in measuring ECL is further detailed in Note 3.1.1, which also sets out key sensitivities of the ECL to changes in these elements.

A number of significant judgements are required in applying the accounting requirements for measuring ECL, such as:

- Determining criteria for significant increase in credit risk;
- Choosing appropriate models and assumptions for the measurement of ECL;
- Establishing the number and relative weightings of forward-looking scenarios for each type of product/market and the associated ECL;
- Establishing groups of similar financial assets for the purposes of measuring ECL; and
- Assessing data limitation and model uncertainty, and determining post model adjustments.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES (CONTINUED)

Determining the lease term of a right-of-use asset

In determining the lease term, management considers all facts and circumstances that create an economic incentive to exercise an extension option, or not to exercise a termination option. Extension options (or periods after termination options) are only included in the lease term if the lease is reasonably certain to be extended (or not terminated).

The assessment is reviewed if a significant event or a significant change in circumstances occurs which affects this assessment and that is within the control of the lessee. During the current financial period, no revisions were made to the lease terms to reflect the effect of exercising extension and termination options.

5 SEGMENT REPORTING

(a) By operating segment

Operating segments, and the amounts of each segment item reported in the consolidated financial statements, are identified from the financial information provided regularly to the Group's most senior executive management for the purposes of allocating resources to, and assessing the performance of, the Group's various lines of business and geographical locations.

For the purpose of assessing performance of business activity by class, 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.

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

Retail and corporate banking – incorporating banking services to individual and corporate customers such as current accounts, savings accounts, time deposits, safe deposit box, credit and debit cards, loans and other credit facilities.

Trade finance – incorporating import and export bills services, invoice financing and invoice discounting.

Treasury – conducting treasury operations for trading and investment purposes such as foreign exchange, money market and capital market activities and providing treasury products such as yield enhancement and hedging products to retail and corporate customers.

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

5 SEGMENT REPORTING (CONTINUED)

(a) By operating segment (Continued)

2019

	Retail and corporate banking	Trade finance	Treasury	Others	Total
Net interest income	2,903,070	82,024	798,390	193,809	3,977,293
Non-interest income	378,809	105,240	285,911	685,673	1,455,633
Operating income	3,281,879	187,264	1,084,301	879,482	5,432,926
Operating expenses	(871,681)	(85,222)	(119,197)	(573,153)	(1,649,253)
Operating profit before credit impairment losses	2,410,198	102,042	965,104	306,329	3,783,673
Credit impairment losses	(62,859)	1,450	1,167	(262)	(60,504)
Operating profit after credit impairment losses	2,347,339	103,492	966,271	306,067	3,723,169
Share of net profits of associates and joint venture	–	–	–	36,519	36,519
Profit before income tax (after taking into account internal fund transfers and cost allocation)	2,347,339	103,492	966,271	342,586	3,759,688
Income tax expense	553,060	13,379	157,507	13,759	737,705
Depreciation expenses	89,616	9,778	6,850	125,063	231,307
Total assets	99,737,363	3,618,689	113,258,316	6,010,746	222,625,114
Total liabilities	173,887,503	86,828	16,471,637	1,554,882	192,000,850

2018

	Retail and corporate banking	Trade finance	Treasury	Others	Total
Net interest income	2,432,290	122,933	957,584	95,674	3,608,481
Non-interest income	273,103	109,027	216,644	748,970	1,347,744
Operating income	2,705,393	231,960	1,174,228	844,644	4,956,225
Other non-operating income	–	–	–	118,333	118,333
Operating expenses	(859,703)	(85,801)	(114,928)	(508,833)	(1,569,265)
Operating profit before credit impairment losses	1,845,690	146,159	1,059,300	454,144	3,505,293
Credit impairment losses	(24,871)	(1,216)	(2,538)	36	(28,589)
Operating profit after credit impairment losses	1,820,819	144,943	1,056,762	454,180	3,476,704
Share of net profits of associates and joint venture	–	–	–	23,753	23,753
Profit before income tax (after taking into account internal fund transfers and cost allocation)	1,820,819	144,943	1,056,762	477,933	3,500,457
Income tax expense	415,791	20,277	168,806	49,910	654,784
Depreciation expenses	5,029	493	1,485	98,480	105,487
Total assets	86,673,470	3,931,065	101,677,652	5,337,725	197,619,912
Total liabilities	155,608,207	92,105	12,981,204	1,036,532	169,718,048

5 SEGMENT REPORTING (CONTINUED)

(b) By geographical area

The following tables provide information by geographical area, which was determined with reference to the location of the principal operations of the branches and subsidiaries of the Group.

2019	Total assets	Total liabilities	Contingent liabilities and commitments	Total operating income	Profit before income tax	Capital expenditure
Hong Kong and Mainland China	190,562,725	175,150,782	43,887,734	4,340,807	2,840,940	206,708
United States	27,056,085	13,895,206	8,992,640	1,005,527	859,306	33,744
United Kingdom	5,006,304	2,954,862	147,064	86,592	59,442	1,185
Total	222,625,114	192,000,850	53,027,438	5,432,926	3,759,688	241,637

2018	Total assets	Total liabilities	Contingent liabilities and commitments	Total operating income	Profit before income tax	Capital expenditure
Hong Kong and Mainland China	170,407,173	154,443,145	42,555,434	4,158,369	2,742,098	82,398
United States	23,719,537	12,836,448	8,229,634	851,752	716,085	530
United Kingdom	3,493,202	2,438,455	125,825	64,437	42,274	128
Total	197,619,912	169,718,048	50,910,893	5,074,558	3,500,457	83,056

6 NET INTEREST INCOME

Interest income	2019	2018
Cash and balances with banks	760,743	774,789
Investment securities at amortised cost	44,250	29,681
Investment securities at fair value through other comprehensive income	1,784,182	1,378,843
Loans and advances to customers	4,141,403	3,257,068
Others	15,523	15,783
Interest income on financial assets that are not measured at fair value through profit or loss	6,746,101	5,456,164

Interest expense		
Deposits and balances from banks	291,508	223,358
Deposits from customers	2,267,754	1,537,221
Subordinated debts	189,413	75,241
Lease liabilities	11,759	–
Others	8,374	11,863
Interest expense on financial liabilities that are not measured at fair value through profit or loss	2,768,808	1,847,683

7 NET FEE AND COMMISSION INCOME

Fee and commission income	2019	2018
Bills	87,511	93,379
Nominees, custodian and securities brokerage	174,058	229,709
Investment products	125,833	144,572
Remittance	63,387	63,839
Facility fees	260,953	157,630
Credit cards	49,363	49,348
Retail banking	47,439	52,094
Insurance	51,798	69,761
Loans and advances	6,965	6,640
Trust and other commissions	3,529	3,422
	870,836	870,394

Fee and commission expense		
Bills	11,218	8,702
Nominees, custodian and securities brokerage	13,074	15,819
Retail banking	30,762	30,173
Credit cards	63	66
Remittance	42	147
	55,159	54,907
Of which:		
Net fee and commission income, other than amounts included in determining the effective interest rate, arising from financial assets or financial liabilities that are not measured at fair value through profit or loss		
– fee and commission income	404,792	306,997
– fee and commission expense	11,281	8,768
Net fee and commission income on trust and other fiduciary activities		
– fee and commission income	24,310	24,206

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 NET TRADING INCOME

	2019	2018
Foreign exchange	168,599	188,535
Interest rate instruments	46,546	(4,347)
Equities	3,741	825
Other trading income	6,340	334
	225,226	185,347

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

9 OTHER OPERATING INCOME

	2019	2018
Gross rental income from investment properties	87,723	79,050
Net gains/(losses) from disposal of equipment	50	(2,897)
Others	77,164	69,673
	164,937	145,826

Direct operating expenses arising from investment properties of HK$131,000 (2018: nil) are included in building expenses (Note 11).

10 NET EARNED INSURANCE PREMIUM

	2019	2018
Insurance premium revenue	62,031	56,160
Insurance premium ceded to reinsurers	(11,643)	(10,985)
	50,388	45,175

The related net insurance claims incurred and movement in policyholders' liabilities of HK$38,152,000 (2018: HK$23,696,000) were shown after being netted off with the insurance claims and loss adjustment expenses recovered from reinsurers of HK$5,023,000 (2018: HK$6,713,000).

11 OPERATING EXPENSES

	2019	2018
Auditor's remuneration		
Audit services (Note a)	9,927	10,017
Non-audit and other services (Note b)	5,476	13,800
Advertising costs	17,731	21,813
Depreciation expenses	231,307	105,487
Employee benefit expenses		
Wages and salaries and other costs (Note c)	949,536	882,494
Pension costs – defined contribution schemes	67,027	64,978
Premises and equipment expenses, excluding depreciation		
Rental of premises	6,093	123,063
Expenses relating to short-term and low-value leases	2,628	–
Building expenses	37,543	34,848
Other operating expenses		
Computer rental and licence	26,510	27,415
Credit card business promotion	29,538	31,757
Credit card service fee	12,356	13,445
Insurance	12,669	11,991
Legal and consultancy	15,482	25,592
Postage	15,722	16,426
Printing and stationery	7,658	11,721
Repair and maintenance	30,448	28,220
Telephone and communications	30,158	32,539
Travelling and transportation	9,157	9,001
Water, heat and light	17,720	17,443
Others	114,567	87,215
	1,649,253	1,569,265

Note a: Auditor's remuneration for audit services represents the fee for the audit of the Group's financial information for the interim and annual period to comply with the statutory and regulatory requirements in Hong Kong and Taiwan.

Note b: Non-audit and other services include the fee for the review under Hong Kong Standard on Review Engagements 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" for the first and third quarter results of the Group in accordance with the regulatory requirements of the ultimate holding company in Taiwan.

Note c: Employee benefit expenses include directors' emoluments (Note 13(a)).

12 CREDIT IMPAIRMENT LOSSES

	2019	2018
Loans and advances to customers	61,776	19,884
Balances with banks and placements with banks	(90)	(895)
Investment securities	(1,083)	3,081
Other assets	556	(199)
Loan commitments and financial guarantee contracts	(655)	6,718
	60,504	28,589

13 BENEFITS AND INTERESTS OF DIRECTORS

(a) Directors' emoluments

The emoluments of the Directors of the Bank disclosed pursuant to section 383 of the Hong Kong Companies Ordinance (Cap. 622) and the Companies (Disclosure of Information about Benefits of Directors) Regulation (Cap. 622G) are set out below:

	2019	2018
Fees	7,725	6,483
Basic salaries, allowances and bonus	28,776	26,355
Contributions to retirement benefits schemes	1,297	1,282
	37,798	34,120

(b) Directors' material interests in transactions, arrangements or contracts

In 2019, the Bank had entered into a contract with Hanison Contractors Limited ("Hanison") as the main contractor for a sum of HK$452,880,000 relating to the redevelopment of West Point Branch where Mr. Johnson M. D. Cha is a common director of the Bank and Hanison Construction Holdings Ltd., the holding company of Hanison.

14 INCOME TAX EXPENSE

Hong Kong profits tax has been provided at the rate of 16.5% (2018: 16.5%) on the estimated assessable profits for the year. Taxation on overseas profits has been calculated on the estimated assessable profits for the year at the rates of taxation prevailing in the countries in which the Group operates.

The amount of taxation charged to the statement of profit or loss represents:

	2019	2018
Current income tax:		
– Hong Kong profits tax	422,813	413,785
– Overseas taxation	315,004	256,896
– Under/(over) provisions in respect of prior years	3,299	(11,758)
Total current income tax	741,116	658,923
Deferred income tax:		
– Hong Kong deferred tax	2,303	(774)
– Overseas deferred tax	(5,714)	(3,365)
Total deferred income tax	(3,411)	(4,139)
Income tax expense	737,705	654,784

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:

	2019	2018
Profit before tax	3,759,688	3,500,457
Tax calculated at domestic tax rates applicable to profits in the respective countries	760,458	692,540
Tax effects of:		
Income not subject to tax	(49,261)	(31,480)
Expenses not deductible for tax purposes	23,209	5,482
Under/(over) provisions in respect of prior years	3,299	(11,758)
Income tax expense	737,705	654,784

15 DIVIDEND

The dividends paid in 2019 and 2018 were HK$940,000,000 (HK$47 per share) for both years. A dividend in respect of the year ended 31 December 2019 of HK$47 per share, amounting to a total dividend of HK$940,000,000, is to be proposed at the Annual General Meeting on 22 April 2020. These financial statements do not reflect this dividend payable.

	2019	2018
Proposed final dividend of HK$47 (2018: HK$47) per ordinary share	940,000	940,000

16 CASH AND BALANCES WITH BANKS

	2019	2018
Cash in hand	762,741	357,611
Balances with central banks and HKMA	2,779,502	3,040,697
Balances with banks	30,586,874	25,210,725
	34,129,117	28,609,033
Less: Stage 1 impairment allowances	(503)	(535)
	34,128,614	28,608,498

Included in the above amounts, HK$247,051,000 (2018: HK$257,677,000) were deposited in central banks or designated banks as at 31 December 2019, to comply with the statutory requirements of respective jurisdiction in which the Group is operating the business.

17 PLACEMENTS WITH BANKS

	2019	2018
Placements with banks maturing between 1 and 12 months	7,090,662	8,643,886
Less: Stage 1 impairment allowances	(106)	(164)
	7,090,556	8,643,722

Included in the above amounts, HK$365,289,000 (2018: HK$370,697,000) were deposited with designated banks in the People's Republic of China as at 31 December 2019, to comply with the local statutory requirement.

18 LOANS AND ADVANCES TO CUSTOMERS

	2019	2018
Gross loans and advances to customers	99,187,091	87,088,260
Less: impairment allowances		
– Stage 1	(302,185)	(279,499)
– Stage 2	(73,280)	(51,618)
– Stage 3	(37,935)	(31,597)
	98,773,691	86,725,546
Gross trade bills and other eligible bills, included within gross loans and advances to customers	373,054	454,120
Less: impairment allowances on trade bills		
– Stage 1	(227)	(195)
– Stage 2	(182)	(247)
	372,645	453,678

The Group accepted listed securities at fair value of HK$3,968,969,000 (2018: HK$4,966,306,000) as collateral for shares financing facilities. These securities are permitted to be sold or re-pledged in the event of default by the borrowers.

19 FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

	2019	2018
Debt securities		
Unlisted	1,853,440	1,832,439
Total debt securities	1,853,440	1,832,439
Equity securities		
Listed in Hong Kong	20,391	20,094
Unlisted	7,194	6,017
Total equity securities	27,585	26,111
Others	–	434
Total	1,881,025	1,858,984
Type of issuer:		
Sovereigns	20,557	–
Banks	–	434
Corporates	1,860,468	1,858,550
	1,881,025	1,858,984

As at 31 December 2019, financial assets at fair value through profit or loss amounting to HK$1,853,440,000 (2018: HK$1,832,439,000) have been pledged to a shareholder of the Bank for its provision of the credit facilities to the Bank's branches in the United States.

20 DERIVATIVE FINANCIAL INSTRUMENTS

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.

As at 31 December 2019

	Contract amount	Fair values	
		Assets	Liabilities
Derivatives held for trading			
Exchange rate contracts	105,233,452	285,089	(292,599)
Total recognised derivative assets/(liabilities)		285,089	(292,599)

As at 31 December 2018

	Contract amount	Fair values	
		Assets	Liabilities
Derivatives held for trading			
Exchange rate contracts	80,774,024	313,320	(305,731)
Total recognised derivative assets/(liabilities)		313,320	(305,731)

	Credit risk weighted amount	
	2019	2018
Exchange rate contracts	1,217,716	1,261,899

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

The credit risk weighted amounts as at 31 December 2019 and 2018 are the amounts that have been calculated in accordance with the BCR.

The above credit risk weighted amounts and fair values have not taken into account the effect of bilateral netting arrangements 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 positions. Trading limits and price verification controls are key aspects of this activity.

21 INVESTMENT SECURITIES AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

	2019	2018
Debt securities		
Listed in Hong Kong	13,840,219	10,385,205
Listed outside Hong Kong	11,948,600	10,524,034
Unlisted	41,050,788	38,141,105
Total debt securities	66,839,607	59,050,344
Equity securities		
Listed outside Hong Kong	4,657,821	4,288,351
Unlisted	61,118	60,415
Total equity securities	4,718,939	4,348,766
	71,558,546	63,399,110
Type of issuer:		
Sovereigns	8,051,350	7,825,092
Public sector entities	45,469	–
Banks	39,495,147	41,544,916
Corporates	23,966,580	14,029,102
	71,558,546	63,399,110
Impairment allowances of debt securities		
Stage 1	7,959	9,042

Note:

As at 31 December 2019, equity securities designated at fair value through other comprehensive income amounting to HK$4,718,939,000 (2018: HK$4,348,766,000) were for long term investment purpose, of which HK$4,504,341,000 (2018: HK$4,171,383,000) were the fair value of the Bank's investment in Bank of Shanghai, China.

The movement in investment securities at fair value through other comprehensive income is summarised as follows:

	2019	2018
As at 1 January	63,399,110	49,787,255
Additions	63,409,364	40,029,044
Gains from changes in fair value	874,593	393,463
Disposals and redemptions	(55,856,189)	(25,973,843)
Amortisation	122,958	(16,071)
Exchange adjustments	(391,290)	(820,738)
As at 31 December	71,558,546	63,399,110

22 INVESTMENT SECURITIES AT AMORTISED COST

	2019	2018
Debt securities		
Listed in Hong Kong	38,922	109,195
Listed outside Hong Kong	397,016	349,727
Unlisted	2,045,006	1,954,748
	2,480,944	2,413,670
Less: Stage 1 impairment allowances	(20)	(20)
	2,480,924	2,413,650
Type of issuer:		
Sovereigns	2,442,018	2,374,513
Banks	38,906	39,137
	2,480,924	2,413,650

As at 31 December 2019, certain of the Bank's branches in the United States have pledged investment securities at amortised cost amounting to HK$397,016,000 (2018: HK$349,727,000) to the State of California and with the Office of the Comptroller of the Currency in compliance with local regulatory requirements. In addition, listed and unlisted Exchange Fund Bills and Notes at amortised cost of HK$2,045,006,000 (2018: HK$2,024,790,000) were pledged to the HKMA to facilitate settlement operations. There were no related liabilities at the year end.

The movement in investment securities at amortised cost is summarised as follows:

	2019	2018
As at 1 January	2,413,650	2,384,609
Additions	9,201,848	4,733,498
Redemptions	(9,169,097)	(4,708,553)
Amortisation	37,099	3,519
Exchange adjustments	(2,576)	593
Net movement of impairment allowances	–	(16)
As at 31 December	2,480,924	2,413,650

23 PROPERTIES FOR SALE

	2019	2018
Property development		
Leasehold land held for development for sale	382,598	382,598
Building development cost	66,864	33,748
	449,462	416,346

The Group has undertaken a project to redevelop the properties located in West Point. As at 31 December 2019, the net book amount of land and building incurred for this project were HK$561,609,000 (2018: HK$520,323,000), of which HK$449,462,000 (2018: HK$416,346,000) were classified as properties held for sale while the remaining HK$112,147,000 (2018: HK$103,977,000) as bank premises under development (Note 26) in accordance with the redevelopment plan.

24 SUBSIDIARIES

The following is a list of the subsidiaries as at 31 December 2019:

Name	Place of incorporation	Principal activities and place of operation	Particulars of issued share capital	Percentage of ordinary share capital held	2019 Total assets	2019 Total equity	2018 Total assets	2018 Total equity
Shanghai Commercial Bank (Nominees) Limited	Hong Kong	Nominee services Hong Kong	100 ordinary shares	100%[1]	10	10	10	10
Shanghai Commercial Bank Trustee Limited	Hong Kong	Trustee services Hong Kong	1,000 ordinary shares	60%[2]	15,798	15,476	15,138	14,948
Shacom Futures Limited	Hong Kong	Commodities trading Hong Kong	600,000 ordinary shares[3]	100%[1]	97,224	54,557	46,919	11,108
Shacom Investment Limited	Hong Kong	Investment in Exchange Fund Bills and Notes Hong Kong	10,000 ordinary shares	100%[1]	2,788,841	2,102	2,600,944	1,448
Shacom Property Holdings (BVI) Limited	British Virgin Islands	Property holding United Kingdom	2 ordinary shares of US$1 each	100%[1]	24,431	2,516	35,706	1,555
Shacom Property (NY), Inc.	United States of America	Property holding United States of America	10 ordinary shares of US$1 each	100%[1]	5,595	5,595	5,658	5,658
Shacom Property (CA), Inc.	United States of America	Property holding United States of America	10 ordinary shares of US$1 each	100%[1]	2,711	2,711	2,739	2,739
Shacom Assets Investments Limited	Hong Kong	Investment in notes and bonds Hong Kong	10,000 ordinary shares	100%[1]	1,081,974	37	1,048,500	77
Infinite Financial Solutions Limited	Hong Kong	I.T. application services provider Hong Kong	500,000 ordinary shares	100%[1]	27,008	20,001	27,273	19,558
Shacom Insurance Brokers Limited	Hong Kong	Insurance broker Hong Kong	1,000,000 ordinary shares	100%[1]	7,716	1,507	4,669	1,397
Shacom Securities Limited	Hong Kong	Securities brokerage services Hong Kong	1,000,000 ordinary shares	100%[1]	286,731	163,250	187,043	162,128
Hai Kwang Property Management Company Limited	Hong Kong	Property management Hong Kong	2 ordinary shares	100%[1]	845	527	792	517

24 SUBSIDIARIES (CONTINUED)

Name	Place of incorporation	Principal activities and place of operation	Particulars of issued share capital	Percentage of ordinary share capital held	2019 Total assets	2019 Total equity	2018 Total assets	2018 Total equity
Paofoong Insurance Company (Hong Kong) Limited	Hong Kong	Insurance Hong Kong	500,000 ordinary shares	60%[2]	312,876	200,478	298,633	186,795
Right Honour Investments Limited	British Virgin Islands	Property holding Hong Kong	1 ordinary share of US$1 each	100%[1]	5	(145)	6	(128)
Glory Step Westpoint Investments Limited	British Virgin Islands	Property holding Hong Kong	1 ordinary share of US$1 each	100%	191,187	(6,754)	192,411	(2,556)
Silver Wisdom Westpoint Investments Limited	British Virgin Islands	Property holding Hong Kong	1 ordinary share of US$1 each	100%	294,791	(19,487)	294,871	(2,798)
KCC 23F Limited	British Virgin Islands	Property holding Hong Kong	1 ordinary share of HK$1 each	100%[1]	344,314	152,951	341,244	150,040
KCC 25F Limited	British Virgin Islands	Property holding Hong Kong	1 ordinary share of HK$1 each	100%[1]	345,253	153,856	342,221	150,947
KCC 26F Limited	British Virgin Islands	Property holding Hong Kong	1 ordinary share of HK$1 each	100%[1]	347,258	155,970	344,233	153,068

1 Ordinary share capital is held directly by the Bank.

2 60% of ordinary share capital is held directly by the Bank and 40% of ordinary share capital is held by non-controlling interests in equity.

3 On 19 September 2019, the share capital of Shacom Futures Limited increased by HK$45,000,000 to HK$60,000,000 and the Bank subscribed its new capital to maintain 100% of equity interests and voting rights of Shacom Futures Limited.

The carrying amounts of loans to subsidiaries are HK$4,944,402,000 (2018: HK$4,735,977,000) which approximate their fair values, of which HK$4,353,080,000 (2018: HK$4,145,254,000) are secured, interest free and have no fixed term of repayment, while HK$591,322,000 (2018: HK$590,724,000) are secured, interest-bearing with fixed term of repayment.

25 INVESTMENTS IN ASSOCIATES AND JOINT VENTURE

Movement in investments in associates and joint venture

	2019			2018		
	Investment in associates	Investment in joint venture	Total	Investment in associates	Investment in joint venture	Total
As at 1 January	349,557	38,890	388,447	299,379	39,535	338,914
Additional investment cost	–	–	–	75,000	–	75,000
Share of profits, net of tax	36,490	29	36,519	23,698	55	23,753
Dividends paid	(25,500)	(35)	(25,535)	(26,370)	(700)	(27,070)
Other equity movement	18,232	–	18,232	(22,150)	–	(22,150)
As at 31 December	378,779	38,884	417,663	349,557	38,890	388,447

The Group's interests in its associates and joint venture for the years ended 2019 and 2018, which are unlisted, are as follows:

Name of entity	Principle activities	Place of incorporation and operation	Proportion of voting power	% of ownership interest	Nature of relationship
Bank Consortium Holding Limited	Investment holding and provision of trustee, administration and custodian services for retirement schemes	Hong Kong	14.29% of "A" shares	13.33%	Associate
BC Reinsurance Limited	Underwriting of general reinsurance business	Hong Kong	21%	21%	Associate
Hong Kong Life Insurance Limited	Underwriting of life insurance business	Hong Kong	16.67%	16.67%	Associate
Joint Electronic Teller Services Limited	Provision of ATM network services	Hong Kong	20% of "A" shares	2.67%	Joint venture

25 INVESTMENTS IN ASSOCIATES AND JOINT VENTURE (CONTINUED)

Summarised financial information for associates and joint venture which are accounted for using the equity method is set out below:

2019

Name	Assets	Liabilities	Revenue	Profit	Other comprehensive income	Total comprehensive income	Dividends received
Joint Electronic Teller Services Limited	456,702	83,543	134,516	1,010	–	1,010	35
Bank Consortium Holding Limited	1,018,151	140,946	761,667	220,975	(97)	220,878	23,400
BC Reinsurance Limited	885,474	402,243	149,512	32,621	640	33,261	2,100
Hong Kong Life Insurance Limited	18,645,989	17,543,555	1,601,644	1,059	108,665	109,724	–
	21,006,316	18,170,287	2,647,339	255,665	109,208	364,873	25,535

2018

Name	Assets	Liabilities	Revenue	Profit/(loss)	Other comprehensive income	Total comprehensive income	Dividends received
Joint Electronic Teller Services Limited	400,860	27,366	133,804	1,913	–	1,913	700
Bank Consortium Holding Limited	899,449	87,872	876,531	210,970	(214)	210,756	20,700
BC Reinsurance Limited	842,677	382,707	119,857	(27,983)	1,481	(26,502)	5,670
Hong Kong Life Insurance Limited	16,668,580	16,125,870	1,354,773	8,668	(134,594)	(125,926)	–
	18,811,566	16,623,815	2,484,965	193,568	(133,327)	60,241	27,070

Note a: The balances with the associates and joint venture arise from normal business transactions and are included in Note 39.

Note b: In 2019, the Group reclassified the investments in Hong Kong Life Insurance Limited ("Hong Kong Life"), Bank Consortium Holding Limited and BC Reinsurance Limited previously included in investments in joint ventures into investments in associates as management considered that such presentation would more appropriately reflect the way these investments are managed. Comparatives have been re-presented.

Note c: On 20 March 2017, the Bank along with the other four shareholders ("the sellers") of Hong Kong Life entered into an agreement with First Origin International Limited to sell their entire interest in Hong Kong Life at a consideration of HK$7.1 billion. On 1 October 2018, the sellers terminated the sale in accordance with the terms of the share sale agreement on the basis that the closing conditions had not been satisfied by the long stop date as defined in the agreement, being 30 September 2018. Accordingly, the Bank has recognised its share of the non-repayable deposit of HK$118,333,000 placed by the buyer as an other non-operating income upon the termination of the sale.

The Bank, being one of the existing shareholders of Hong Kong Life, continues with its ownership and supports the development of Hong Kong Life with proportionate subscription of its new share capital issued amounting to HK$75 million to maintain the shareholding of 16.67% in December 2018.

26 PROPERTIES AND EQUIPMENT

				Property under development			
	Leasehold land	Bank premises	Furniture, fittings and equipment	Leasehold land	Development cost	Right-of-use assets	Total
As at 1 January 2018							
Cost	1,391,652	1,098,904	827,425	120,244	4,914	–	3,443,139
Accumulated depreciation	(143,340)	(325,506)	(583,939)	(785)	–	–	(1,053,570)
Net book amount	1,248,312	773,398	243,486	119,459	4,914	–	2,389,569
Year ended 31 December 2018							
Opening net book amount	1,248,312	773,398	243,486	119,459	4,914	–	2,389,569
Additions	–	12,969	51,299	–	4,506	–	68,774
Transfers to properties for sale (Note 23)							
Cost	–	–	–	(23,966)	(983)	–	(24,949)
Accumulated depreciation	–	–	–	156	–	–	156
Disposals/write-off							
Cost	–	(67,371)	(39,895)	–	–	–	(107,266)
Accumulated depreciation	–	67,371	36,880	–	–	–	104,251
Depreciation charge	(17,432)	(24,941)	(54,111)	(109)	–	–	(96,593)
Exchange adjustments	–	(1,102)	(131)	–	–	–	(1,233)
Closing net book amount	1,230,880	760,324	237,528	95,540	8,437	–	2,332,709
As at 31 December 2018							
Cost	1,391,652	1,042,896	837,144	96,278	8,437	–	3,376,407
Accumulated depreciation	(160,772)	(282,572)	(599,616)	(738)	–	–	(1,043,698)
Net book amount	1,230,880	760,324	237,528	95,540	8,437	–	2,332,709
Year ended December 2019							
Opening net book amount	1,230,880	760,324	237,528	95,540	8,437	–	2,332,709
Change in accounting policy	–	–	–	–	–	349,689	349,689
Additions	–	32,755	63,620	–	8,279	136,833	241,487
Disposals/write-off/expiry							
Cost	–	–	(12,624)	–	–	(31,823)	(44,447)
Accumulated depreciation	–	–	12,517	–	–	31,707	44,224
Depreciation charge	(17,432)	(24,923)	(54,989)	(109)	–	(124,960)	(222,413)
Exchange adjustments	–	74	(49)	–	–	(1,260)	(1,235)
Closing net book amount	1,213,448	768,230	246,003	95,431	16,716	360,186	2,700,014
As at 31 December 2019							
Cost	1,391,652	1,075,785	888,175	96,278	16,716	691,488	4,160,094
Accumulated depreciation	(178,204)	(307,555)	(642,172)	(847)	–	(331,302)	(1,460,080)
Net book amount	1,213,448	768,230	246,003	95,431	16,716	360,186	2,700,014

The Group has undertaken a project to redevelop the properties located in West Point. As at 31 December 2019, the net book amount of land and building incurred for this project were HK$561,609,000 (2018: HK$520,323,000), of which HK$449,462,000 (2018: HK$416,346,000) were classified as properties held for sale (Note 23) while the remaining HK$112,147,000 (2018: HK$103,977,000) as bank premises under development in accordance with the redevelopment plan.

As at 31 December 2019, interests in freehold land outside Hong Kong amounted to HK$34,131,000 (2018: HK$33,823,000) are included as bank premises above.

27 INVESTMENT PROPERTIES

	Leasehold land	Buildings	Total
As at 1 January 2018			
Cost	725,305	317,922	1,043,227
Accumulated depreciation	(8,674)	(14,049)	(22,723)
Net book amount	716,631	303,873	1,020,504
Year ended 31 December 2018			
Opening net book amount	716,631	303,873	1,020,504
Additions	–	14,282	14,282
Depreciation charge	(865)	(8,029)	(8,894)
Closing net book amount	715,766	310,126	1,025,892
As at 31 December 2018			
Cost	725,305	332,204	1,057,509
Accumulated depreciation	(9,539)	(22,078)	(31,617)
Net book amount	715,766	310,126	1,025,892
Year ended December 2019			
Opening net book amount	**715,766**	**310,126**	**1,025,892**
Additions	**–**	**150**	**150**
Depreciation charge	**(866)**	**(8,028)**	**(8,894)**
Closing net book amount	**714,900**	**302,248**	**1,017,148**
As at 31 December 2019			
Cost	**725,305**	**332,354**	**1,057,659**
Accumulated depreciation	**(10,405)**	**(30,106)**	**(40,511)**
Net book amount	**714,900**	**302,248**	**1,017,148**

(a) Fair value measurement of investment properties

As at 31 December 2019, the Group's investment properties were valued at HK$3,361,000,000 (2018: HK$3,625,000,000) by an independent firm of chartered surveyors, Cushman & Wakefield Limited, who has among their staff Fellows of the Hong Kong Institute of Surveyors with recent experience in the location and category of properties being valued. The valuations were performed on an open market value basis.

The basis of the valuation of property was market value which is consistent with the definition of fair value under HKFRS 13 "Fair value measurement" and takes into account the highest and best use of the property from the perspective of market participants.

The major key input used in valuing the investment properties was the unit sale rate taking into account of time, location, and individual factors such as size and levels of buildings, which ranged from HK$34,000 (2018: HK$37,000) to HK$107,000 (2018: HK$130,000) per square foot. A decrease in unit sale rate would result in the decrease in fair value measurement of the investment properties by the same percentage and vice versa.

Investment properties are classified as Level 3 under the fair value hierarchy as defined in HKFRS 13 "Fair value measurement" as at 31 December 2019 and 2018.

27 INVESTMENT PROPERTIES (CONTINUED)

(b) Information about Level 3 fair value measurement

	Valuation technique(s)	Unobservable input(s)	Range 2019	Range 2018
Investment properties	Income capitalisation approach	Market yields	2.5% to 2.75%	2.5% to 2.75%
		Market rental	HK$76 to HK$243 per square foot	HK$77 to HK$303 per square foot

For investment properties of which the fair value is determined using the income capitalisation approach, the assessment is conducted on the basis of capitalisation of net income with due allowance for outgoings and reversionary income potential. The fair value measurement is positively correlated to the market rental and inversely correlated to the market yields.

(c) Operating lease commitments as a lessor

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

	2019	2018
No later than 1 year	92,066	55,667
1 to 2 years	62,859	35,771
2 to 3 years	13,904	18,480
	168,829	109,918

The Group leases its investment properties under operating lease arrangements, with leases typically for a period from 3 to 5 years. The terms of the leases generally require the tenants to pay security deposits and provide for rent adjustments according to the prevailing market conditions at the expiration of the lease.

28 OTHER ASSETS

	2019	2018
Accounts receivable and prepayments	882,889	504,725
Interest receivable	800,738	811,870
Others	131,263	105,082
	1,814,890	1,421,677
Less: Stage 1 impairment allowances	(623)	(182)
	1,814,267	1,421,495

29 DEPOSITS FROM CUSTOMERS

	2019	2018
Demand deposits and current accounts	15,060,867	17,545,031
Savings deposits	44,224,648	44,211,816
Time, call and notice deposits	112,763,783	92,466,346
Deposits from Hong Kong Government Exchange Fund	389,218	391,525
	172,438,516	154,614,718

30 SUBORDINATED DEBTS

	2019	2018
US$250 million fixed rate subordinated notes issued due 2027 at amortised cost (Note a)	1,935,108	1,945,079
US$300 million fixed rate subordinated notes issued due 2029 at amortised cost (Note b)	2,322,539	–
	4,257,647	1,945,079

Note a: This represents US$250,000,000 Basel III compliant 10-year subordinated fixed rate notes qualifying as Tier 2 capital of the Bank in accordance with the BCR, which are listed on the Hong Kong Stock Exchange. The notes will mature on 29 November 2027 with an optional redemption date falling on 29 November 2022. Interest at 3.75% p.a. is payable semi-annually from the issue date to the optional redemption date. Thereafter, if the notes are not redeemed, the interest rate will be reset and the notes will bear interest at the prevailing 5-year U.S. Treasury Rate plus 170.5 basis points. The Bank may, subject to receiving the prior approval of the HKMA, redeem the notes at the option of the Bank in whole but not in part, at par either on the optional redemption date or for tax or regulatory reasons at any time prior to maturity of the notes.

Note b: This represents US$300,000,000 Basel III compliant 10-year subordinated fixed rate notes qualifying as Tier 2 capital of the Bank in accordance with the BCR, which are listed on the Hong Kong Stock Exchange. The notes will mature on 17 January 2029 with an optional redemption date falling on 17 January 2024. Interest at 5.00% p.a. is payable semi-annually from the issue date to the optional redemption date. Thereafter, if the notes are not redeemed, the interest rate will be reset and the notes will bear interest at the prevailing 5-year U.S. Treasury Rate plus 250 basis points. The Bank may, subject to receiving the prior approval of the HKMA, redeem the notes at the option of the Bank in whole but not in part, at par either on the optional redemption date or for tax or regulatory reasons at any time prior to maturity of the notes.

31 OTHER LIABILITIES

	2019	2018
Accounts payable and accruals	672,886	836,180
Deferred income	187,183	158,127
Interest payable	684,983	433,454
Lease liabilities	376,523	–
Liabilities for insurance contracts (Note a)	107,363	104,413
Margin deposits	307,296	263,048
Stage 1 and Stage 2 impairment allowances for undrawn commitments and financial guarantees	12,103	12,758
Others (Note b)	465,546	608,209
	2,813,883	2,416,189

Note a: Amounts recoverable from reinsurance of liabilities under insurance contracts issued amounting to HK$6,859,000 (2018: HK$11,591,000) are included in "Other assets" in Note 28.

Note b: "Others" included "Accrual for staff bonus and staff related cost" which was previously classified as "Provisions" in 2018.

32 DEFERRED INCOME TAX

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current income tax assets against current income tax liabilities and when the deferred income taxes relate to the same fiscal authority. The offset amounts are as follows:

Deferred income tax assets

	Impairment allowances	Accelerated tax depreciation	Fair value losses on investment securities at FVOCI	Others	Total
As at 1 January 2018	16,737	(16,508)	31	22,119	22,379
(Charged)/credited to the statement of profit or loss	(2,969)	5,283	–	(375)	1,939
Exchange adjustments	(256)	129	–	17	(110)
Reclassified from/(to) deferred income tax liabilities	52,521	(27,590)	23,054	–	47,985
Balance as at 31 December 2018 as originally presented	66,033	(38,686)	23,085	21,761	72,193
Change in accounting policy	–	–	–	1,497	1,497
Restated as at 1 January 2019	66,033	(38,686)	23,085	23,258	73,690
Credited/(charged) to the statement of profit or loss	5,670	(10,328)	–	8,075	3,417
Exchange adjustments	(336)	(77)	–	(106)	(519)
Charged to equity	–	–	(67,341)	–	(67,341)
Reclassified (to)/from deferred income tax liabilities	(56,422)	45,150	44,253	(14,113)	18,868
As at 31 December 2019	14,945	(3,941)	(3)	17,114	28,115

Deferred income tax liabilities

	Impairment allowances	Accelerated tax depreciation	Fair value gains on investment securities at FVOCI	Others	Total
As at 1 January 2018	47,980	(25,276)	(392,087)	–	(369,383)
Credited/(charged) to the statement of profit or loss	4,541	(2,341)	–	–	2,200
Credited to equity (Note)	–	–	415,141	–	415,141
Reclassified (to)/from deferred income tax assets	(52,521)	27,590	(23,054)	–	(47,985)
As at 31 December 2018	–	(27)	–	–	(27)
Charged to the statement of profit or loss	–	(6)	–	–	(6)
Reclassified from/(to) deferred income tax assets	56,422	(45,150)	(44,253)	14,113	(18,868)
As at 31 December 2019	56,422	(45,183)	(44,253)	14,113	(18,901)

Note: In 2018, deferred income tax liabilities of HK$410,083,000 provided for the unrealised mark-to-market gains of Bank of Shanghai shares have been released in view of the fact that evidence supporting these shares are held for long term investment purpose was established.

33 SHARE CAPITAL

	2019	2018
Issued and fully paid: 20,000,000 shares	2,000,000	2,000,000

34 RESERVES ATTRIBUTABLE TO EQUITY HOLDERS

	Regulatory reserve	Investment revaluation reserve	General and other reserves	Total
As at 1 January 2018	740,723	2,008,820	7,278,527	10,028,070
Investment securities at fair value through other comprehensive income	–	577,420	–	577,420
Currency translation difference arising from overseas operations	(3,988)	–	(75,729)	(79,717)
Share of reserves of associates and joint venture	–	(22,461)	311	(22,150)
As at 31 December 2018	736,735	2,563,779	7,203,109	10,503,623
As at 1 January 2019	**736,735**	**2,563,779**	**7,203,109**	**10,503,623**
Investment securities at fair value through other comprehensive income	**–**	**682,298**	**–**	**682,298**
Currency translation difference arising from overseas operations	**(1,441)**	**–**	**(23,795)**	**(25,236)**
Share of reserves of associates and joint venture	**–**	**18,098**	**134**	**18,232**
Transfer from retained earnings	**200,000**	**–**	**–**	**200,000**
As at 31 December 2019	**935,294**	**3,264,175**	**7,179,448**	**11,378,917**

Nature and purpose of reserves:

(a) Regulatory reserve

The regulatory reserve is maintained to satisfy the provisions of the Hong Kong Banking Ordinance and local regulatory requirements of overseas branches for prudent supervision purpose. Any movements in the regulatory reserve for Hong Kong operations are made in consultation with the HKMA.

As at 31 December 2019, the regulatory reserves for Hong Kong and overseas branches operations were HK$812,455,000 (2018: HK$612,455,000) and HK$122,839,000 (2018: HK$124,280,000) respectively.

(b) Investment revaluation reserve

Investment revaluation reserve represents the cumulative net change in the fair value of investment securities at FVOCI until these investments are derecognised or impaired as stated in the accounting policy for financial assets (Note 2.7).

(c) General and other reserves

General and other reserves comprise previous years' transfers from retained earnings and translation reserve arising from translation of foreign operations during consolidation and share of changes in equity of associates and joint venture.

35 CASH AND CASH EQUIVALENTS AND OTHER CASH FLOW INFORMATION

(a) Reconciliation of liabilities arising from financing activities

	Subordinated debts	
	2019	2018
Balance as at 1 January	1,945,079	1,940,308
Cash inflow from issue of subordinated debts net of cost	2,338,326	–
Non-cash changes:		
– Foreign exchange movement	(29,232)	3,300
– Amortisation of discount and issuance cost	3,474	1,471
Balance as at 31 December	4,257,647	1,945,079

(b) Cash and cash equivalents

For the purposes of the consolidated statement of cash flows, cash and cash equivalents comprise the following balances which are with less than 3 months' maturity from the date of acquisition, and that are readily convertible to known amounts of cash, and which are subject to an insignificant risk of changes in value.

	2019	2018
Cash and balances with banks	33,395,356	25,745,537
Placements with banks	1,279,747	840,096
Debt securities – Exchange Fund Bills	5,137,510	8,116,974
	39,812,613	34,702,607

36 CONTINGENT LIABILITIES AND COMMITMENTS

(a) Credit commitments

The contract and credit risk weighted amounts of the Group's off-balance sheet financial instruments that commit it to extend credit to customers are as follows:

Contract amounts	2019	2018
Direct credit substitutes	2,411,445	2,437,965
Trade-related contingencies	2,243,403	2,221,392
Other commitments with an original maturity of:		
– under 1 year	1,215,399	596,418
– 1 year and over	10,168,005	10,822,955
– unconditionally cancellable	36,989,186	34,832,163
	53,027,438	50,910,893

The contractual maturity profile of credit commitments is analysed as follows:

	2019	2018
No later than 1 year	44,850,273	42,140,211
Later than 1 year and no later than 5 years	6,609,355	7,324,620
Later than 5 years	1,567,810	1,446,062
	53,027,438	50,910,893

	2019	2018
Credit risk weighted amounts	7,361,624	7,642,669

36 CONTINGENT LIABILITIES AND COMMITMENTS (CONTINUED)

(b) Capital commitments

Capital expenditure for the acquisition of properties and equipment outstanding as at the reporting date but not yet incurred is as follows:

	2019	2018
Contracted but not provided for	562,769	159,284

(c) 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 adequate grounds to defend against the claimants or the amounts involved in those actions are not expected to be material.

37 OFFSETTING FINANCIAL INSTRUMENTS

The following tables present details of financial instruments subject to offsetting, enforceable master netting arrangements and similar agreements.

As at 31 December 2019

	Gross amounts of recognised financial assets	Gross amounts of recognised financial liabilities set off in the statement of financial position	Net amounts of financial assets presented in the statement of financial position	Related amounts not set off in the statement of financial position		Net amounts
				Financial instruments	Cash collateral received	
Assets						
Derivative financial instruments	168,803	–	168,803	(137,896)	(16,269)	14,638
Other assets	472,378	(349,792)	122,586	–	–	122,586
Total	641,181	(349,792)	291,389	(137,896)	(16,269)	137,224

	Gross amounts of recognised financial liabilities	Gross amounts of recognised financial assets set off in the statement of financial position	Net amounts of financial liabilities presented in the statement of financial position	Related amounts not set off in the statement of financial position		Net amounts
				Financial instruments	Cash collateral pledged	
Liabilities						
Derivative financial instruments	209,196	–	209,196	(137,896)	(71,300)	–
Other liabilities	350,241	(349,792)	449	–	–	449
Total	559,437	(349,792)	209,645	(137,896)	(71,300)	449

37 OFFSETTING FINANCIAL INSTRUMENTS (CONTINUED)

As at 31 December 2018

	Gross amounts of recognised financial assets	Gross amounts of recognised financial liabilities set off in the statement of financial position	Net amounts of financial assets presented in the statement of financial position	Related amounts not set off in the statement of financial position		Net amounts
				Financial instruments	Cash collateral received	
Assets						
Derivative financial instruments	169,466	–	169,466	(118,650)	(33,471)	17,345
Other assets	243,057	(225,915)	17,142	–	–	17,142
Total	412,523	(225,915)	186,608	(118,650)	(33,471)	34,487

	Gross amounts of recognised financial liabilities	Gross amounts of recognised financial assets set off in the statement of financial position	Net amounts of financial liabilities presented in the statement of financial position	Related amounts not set off in the statement of financial position		Net amounts
				Financial instruments	Cash collateral pledged	
Liabilities						
Derivative financial instruments	186,612	–	186,612	(118,650)	(54,265)	13,697
Other liabilities	232,281	(225,915)	6,366	–	–	6,366
Total	418,893	(225,915)	192,978	(118,650)	(54,265)	20,063

Derivative financial instruments disclosed above are recorded on a gross basis in the statement of financial position. Since master netting agreements have been entered into for these derivative financial instruments, the net settlement amounts if an event of default or other precedent events occurred are disclosed under "Net amounts" to comply with the accounting requirements.

37 OFFSETTING FINANCIAL INSTRUMENTS (CONTINUED)

The tables below reconcile the amounts of derivative financial instruments, net amounts of other assets and other liabilities presented in the statement of financial position.

	2019	2018
Assets		
Net amounts of derivative financial instruments after offsetting as stated above	168,803	169,466
Derivative financial instruments not in scope of offsetting disclosures	116,286	143,854
Total derivative financial instruments	285,089	313,320
Net amounts of other assets after offsetting as stated above	122,586	17,142
Other assets not in scope of offsetting disclosures	1,691,681	1,404,353
Total other assets	1,814,267	1,421,495
Liabilities		
Net amounts of derivative financial instruments after offsetting as stated above	209,196	186,612
Derivative financial instruments not in scope of offsetting disclosures	83,403	119,119
Total derivative financial instruments	292,599	305,731
Net amounts of other liabilities after offsetting as stated above	449	6,366
Other liabilities not in scope of offsetting disclosures	2,813,434	2,409,823
Total other liabilities	2,813,883	2,416,189

38 INFORMATION ABOUT LOANS, QUASI-LOANS AND OTHER DEALINGS IN FAVOUR OF DIRECTORS, CONTROLLED BODIES CORPORATE AND CONNECTED ENTITIES

Balances below are disclosed pursuant to Section 383 of the Hong Kong Companies Ordinance (Cap. 622) and Companies (Disclosure of Information about Benefits of Directors) Regulation (Cap. 622G).

	Balance outstanding as at 31 December		Maximum balance during the year	
	2019	2018	2019	2018
Aggregate amount outstanding in respect of principal and interest	587,972	381,801	912,345	386,640

39 RELATED PARTY TRANSACTIONS

A number of banking transactions were entered into with related parties by the Group in the normal course of business and at arm's length basis. The outstanding balances of the related party transactions at the reporting date, and related expense and income for the year are as follows:

2019	Ultimate holding company and fellow subsidiaries	Associates and joint venture	Key management personnel (Note)	Other related parties	Total
Aggregate amounts outstanding at the year end					
– Loans and advances	–	–	580,528	–	580,528
– Cash and balances with banks	4,676	–	–	82,831	87,507
– Deposits and balances from banks and customers	473,908	578,367	2,058,623	3,480,544	6,591,442
– Investment securities at fair value through other comprehensive income	153,480	–	–	–	153,480
– Stage 1 and Stage 2 impairment allowances	–	1	914	–	915
– Contingent liabilities and other commitments	–	2,000	1,319,224	–	1,321,224
Interest income received from related parties	18	–	7,015	11,916	18,949
Interest expenses paid to related parties	5,969	7,819	17,312	88,699	119,799
Net fee and commission income/(expense) from/(to) related parties	(10,088)	63,792	–	(874)	52,830
Net other operating expense to related parties	(16)	(2,313)	(300)	(3,691)	(6,320)

39 RELATED PARTY TRANSACTIONS (CONTINUED)

2018

	Ultimate holding company and fellow subsidiaries	Associates and joint venture	Key management personnel (Note)	Other related parties	Total
Aggregate amounts outstanding at the year end					
– Loans and advances	–	–	432,360	–	432,360
– Cash and balances with banks	5	–	–	1,486,842	1,486,847
– Deposits and balances from banks and customers	519,059	476,320	1,394,176	3,023,366	5,412,921
– Investment securities at fair value through other comprehensive income	116,968	–	–	–	116,968
– Stage 1 and Stage 2 impairment allowances	–	1	659	–	660
– Contingent liabilities and other commitments	–	2,000	55,958	–	57,958
Interest income received from related parties	83	–	5,193	8,275	13,551
Interest expenses paid to related parties	3,850	3,192	17,534	63,493	88,069
Net fee and commission income/(expense) from/(to) related parties	(12,444)	81,940	–	(286)	69,210
Net other operating income/(expense) from/(to) related parties	32	(1,363)	–	(633)	(1,964)

Note: Include key management personnel and Directors of the Bank and the ultimate holding company, their close family members and entities that are controlled or jointly controlled, directly or indirectly, by key management personnel or Directors.

Key management personnel compensation

The compensation for Directors and key management personnel of the Bank is as follows:

	2019	2018
Salaries and other short-term employee benefits	99,680	106,091

40 STATEMENT OF FINANCIAL POSITION AND RESERVE MOVEMENT OF THE BANK

(a) Statement of Financial Position of the Bank

	As at 31 December	
	2019	2018
ASSETS		
Cash and balances with banks	34,127,171	28,606,224
Placements with banks	7,090,556	8,643,722
Loans and advances to customers	98,773,691	86,725,546
Financial assets at fair value through profit or loss	1,860,634	1,838,890
Derivative financial instruments	285,089	313,320
Investment securities at fair value through other comprehensive income	71,543,427	63,343,900
Investment securities at amortised cost	435,918	388,860
Investments in associates and joint venture	188,000	188,000
Investments in and loans to subsidiaries	3,047,476	3,032,411
Properties and equipment	1,996,114	1,558,547
Investment properties	1,047,150	1,056,322
Deferred income tax assets	28,152	72,005
Other assets	1,747,092	1,343,388
TOTAL ASSETS	222,170,470	197,111,135
LIABILITIES		
Deposits and balances from banks	11,677,610	10,344,988
Deposits from customers	172,438,516	154,614,718
Derivative financial instruments	292,599	305,731
Subordinated debts	4,257,647	1,945,079
Other liabilities	2,715,812	2,252,235
Current income tax liabilities	501,011	91,257
Deferred income tax liabilities	17,086	–
TOTAL LIABILITIES	191,900,281	169,554,008
EQUITY		
CAPITAL AND RESERVES ATTRIBUTABLE TO EQUITY HOLDERS		
Share capital	2,000,000	2,000,000
Retained earnings	16,907,082	15,051,030
Reserves	11,363,107	10,506,097
	30,270,189	27,557,127
TOTAL EQUITY AND LIABILITIES	222,170,470	197,111,135

Approved and authorised for issue by the Board of Directors on 18 March 2020.

Stephen Ching Yen LEE
Chairman

Hung-ching YUNG
Director

Gordon Che Keung KWONG
Director

David Sek-chi KWOK
Managing Director & Chief Executive

40 STATEMENT OF FINANCIAL POSITION AND RESERVE MOVEMENT OF THE BANK (CONTINUED)

(b) Reserve movement of the Bank

	Regulatory reserve	Investment revaluation reserve	General reserve	Total
As at 1 January 2018	740,723	1,989,910	7,277,650	10,008,283
Investment securities at fair value through other comprehensive income	–	577,488	–	577,488
Currency translation difference arising from overseas operations	(3,988)	–	(75,686)	(79,674)
As at 31 December 2018	736,735	2,567,398	7,201,964	10,506,097
As at 1 January 2019	**736,735**	**2,567,398**	**7,201,964**	**10,506,097**
Investment securities at fair value through other comprehensive income	**–**	**682,266**	**–**	**682,266**
Currency translation difference arising from overseas operations	**(1,441)**	**–**	**(23,815)**	**(25,256)**
Transfer from retained earnings	**200,000**	**–**	**–**	**200,000**
As at 31 December 2019	**935,294**	**3,249,664**	**7,178,149**	**11,363,107**

41 COMPARATIVE FIGURES

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

42 EVENTS AFTER THE REPORTING PERIOD

The ECL as at 31 December 2019 was estimated based on a range of forecast economic conditions as at that date. The coronavirus outbreak around the globe since early January 2020 has interrupted the business and economic activity. While the estimated financial effect cannot be made at the moment, the Group has been closely monitoring the impact on key economic indicators when determining the severity and likelihood of downside economic scenarios that will be used to estimate ECL under HKFRS 9 which might have a negative impact on the ECL in 2020.

REGULATORY DISCLOSURES (UNAUDITED)

(All amounts in HK dollar thousands unless otherwise stated)

The Regulatory Disclosures, together with the disclosures in this Annual Report, contain all the disclosures required by the Banking (Disclosure) Rules issued by the Hong Kong Monetary Authority ("HKMA").

This Annual Report and the Regulatory Disclosures are prepared according to the Group's disclosure policy. The disclosure policy sets out a robust mechanism for the Group's disclosures of financial information on a legitimate and compliant basis. It depicts the principles and internal control measures to ensure the timeliness, fairness, accuracy, integrity, completeness and legitimacy of financial disclosures.

The following disclosures are prepared under regulatory scope of consolidation to comply with the Banking (Disclosure) Rules and do not form part of the audited financial statements.

1 Key prudential ratios

		31 December 2019	30 September 2019	30 June 2019	31 March 2019	31 December 2018
	Regulatory capital (amount)					
1	Common Equity Tier 1 (CET1)	**27,572,305**	26,887,182	26,160,646	26,258,408	25,126,647
2	Tier 1	**27,572,305**	26,887,182	26,160,646	26,258,408	25,126,647
3	Total capital	**33,162,681**	32,506,175	31,660,713	31,650,412	28,160,772
	Risk Weighted Amounts (RWA)					
4	Total RWA	**169,830,908**	164,933,019	165,578,250	155,303,910	151,367,613
	Risk-based regulatory capital ratios (as a percentage of RWA)					
5	CET1 ratio (%)	**16.2%**	16.3%	15.8%	16.9%	16.6%
6	Tier 1 ratio (%)	**16.2%**	16.3%	15.8%	16.9%	16.6%
7	Total capital ratio (%)	**19.5%**	19.7%	19.1%	20.4%	18.6%
	Additional CET1 buffer requirements (as a percentage of RWA)					
8	Capital conservation buffer requirement (%)	**2.5%**	2.5%	2.5%	2.5%	1.9%
9	Countercyclical capital buffer requirement (%)	**1.3%**	1.6%	1.6%	1.5%	1.1%
10	Higher loss absorbency requirements (%) (applicable only to G-SIBs or D-SIBs)	**0.0%**	0.0%	0.0%	0.0%	0.0%
11	Total AI-specific CET1 buffer requirements (%)	**3.8%**	4.1%	4.1%	4.0%	3.0%
12	CET1 available after meeting the AI's minimum capital requirements (%)	**10.2%**	10.3%	9.8%	10.9%	10.6%
	Basel III leverage ratio					
13	Total leverage ratio (LR) exposure measure	**233,630,690**	225,238,494	228,115,200	213,839,604	208,591,012
14	LR (%)	**11.8%**	11.9%	11.5%	12.3%	12.0%
	Liquidity Coverage Ratio (LCR) / Liquidity Maintenance Ratio (LMR)					
	Applicable to category 1 institution only:					
15	Total high quality liquid assets (HQLA)	**N/A**	N/A	N/A	N/A	N/A
16	Total net cash outflows	**N/A**	N/A	N/A	N/A	N/A
17	LCR (%)	**N/A**	N/A	N/A	N/A	N/A
	Applicable to category 2 institution only:					
17a	LMR (%)	**57.3%**	53.6%	49.9%	52.7%	48.2%
	Net Stable Funding Ratio (NSFR) / Core Funding Ratio (CFR)					
	Applicable to category 1 institution only:					
18	Total available stable funding	**N/A**	N/A	N/A	N/A	N/A
19	Total required stable funding	**N/A**	N/A	N/A	N/A	N/A
20	NSFR (%)	**N/A**	N/A	N/A	N/A	N/A
	Applicable to category 2A institution only:					
20a	CFR (%)	**194.0%**	181.3%	178.3%	189.5%	191.7%

Footnote:

N/A Not applicable

2 Capital structure and adequacy

The calculation of the capital adequacy ratio as at 31 December 2019 is based on the Banking (Capital) Rules ("BCR"). The capital adequacy ratio represents the consolidated ratio of the Bank's Hong Kong offices, overseas branches, Shacom Property (CA), Inc., Shacom Property (NY), Inc., Shacom Property Holdings (BVI) Limited, Shacom Investment Limited, Shacom Assets Investments Limited, Right Honour Investments Limited, Glory Step Westpoint Investments Limited, Silver Wisdom Westpoint Investments Limited, Shacom Insurance Brokers Limited, KCC 23F Limited, KCC 25F Limited, and KCC 26F Limited computed in accordance with Section 3C(1) of the BCR.

For accounting purposes, the basis of consolidation is described in Note 2.2 to the consolidated financial statements.

The table below shows the balance sheet based on accounting scope of consolidation and the regulatory scope of consolidation, and the reconciliation of the capital components from balance sheet based on regulatory scope of consolidation to the Composition of Regulatory Capital as at 31 December 2019.

Reconciliation of regulatory capital to balance sheet

	Balance sheet as in published financial statements	Under regulatory scope of consolidation	Cross-referenced to Composition of Regulatory Capital
Assets			
Cash and balances with banks	**34,128,614**	**34,127,171**	
of which: Stage 1 and Stage 2 impairment allowances reflected in regulatory capital		***(503)***	(1)
Placements with banks	**7,090,556**	**7,090,556**	
of which: Stage 1 and Stage 2 impairment allowances reflected in regulatory capital		***(106)***	(2)
Loans and advances to customers	**98,773,691**	**98,773,691**	
of which: Stage 1 and Stage 2 impairment allowances reflected in regulatory capital		***(375,465)***	(3)
Financial assets at fair value through profit or loss	**1,881,025**	**1,860,634**	
Derivative financial instruments	**285,089**	**285,089**	
Investment securities at fair value through other comprehensive income	**71,558,546**	**71,543,427**	
of which: insignificant capital investments in financial sector entities exceeding 10% threshold		***1,650,384***	(4)
Investment securities at amortised cost	**2,480,924**	**2,479,796**	
of which: Stage 1 and Stage 2 impairment allowances reflected in regulatory capital		***(20)***	(5)
Properties for sale	**449,462**	**449,462**	
Investments in associates and joint venture	**417,663**	**188,000**	
Investments in and amounts due from subsidiaries	**–**	**305,080**	
of which: Stage 1 and Stage 2 impairment allowances reflected in regulatory capital		***(8,839)***	(6)
Properties and equipment	**2,700,014**	**2,602,862**	
Investment properties	**1,017,148**	**1,047,150**	
Deferred income tax assets	**28,115**	**28,154**	(7)
Other assets	**1,814,267**	**1,764,051**	
of which: Stage 1 and Stage 2 impairment allowances reflected in regulatory capital		***(400)***	(8)
Total assets	**222,625,114**	**222,545,123**	

2 Capital structure and adequacy (Continued)

Reconciliation of regulatory capital to balance sheet (Continued)

	Balance sheet as in published financial statements	Under regulatory scope of consolidation	Cross-referenced to Composition of Regulatory Capital
Liabilities			
Deposits and balances from banks	11,677,610	11,677,610	
Deposits from customers	172,438,516	172,438,516	
Derivative financial instruments	292,599	292,599	
Amounts due to subsidiaries	–	505,722	
Subordinated debts	4,257,647	4,257,647	(9)
Other liabilities	2,813,883	2,668,478	
of which: Stage 1 and Stage 2 impairment allowances reflected in regulatory capital		*12,103*	(10)
Current income tax liabilities	501,694	501,011	
Deferred income tax liabilities	18,901	17,404	
Total liabilities	192,000,850	192,358,987	
Equity			
Share capital	2,000,000	2,000,000	(11)
Retained earnings	17,158,968	16,823,011	(12)
Reserves	11,378,917	11,363,125	
of which: accumulated other comprehensive income/(loss), other than regulatory reserve		*10,427,832*	(13)
regulatory reserve		*935,293*	(14)
Non-controlling interests	86,379	–	
Total equity	30,624,264	30,186,136	
Total equity and liabilities	222,625,114	222,545,123	

2 Capital structure and adequacy (Continued)

Composition of regulatory capital

The Bank has already applied full capital deductions under the BCR. The Composition of Regulatory Capital as at 31 December 2019 is shown below:

		Component of regulatory capital reported by bank	Cross-referenced to balance sheet under regulatory scope of consolidation
CET1 capital: instruments and reserves			
1	Directly issued qualifying CET1 capital instruments plus any related share premium	2,000,000	(11)
2	Retained earnings	16,823,011	(12)
3	Disclosed reserves	11,363,125	(13) + (14)
4	Directly issued capital subject to phase out arrangements from CET1 (only applicable to non-joint stock companies)	Not applicable	
5	Minority interests arising from CET1 capital instruments issued by consolidated bank subsidiaries and held by third parties (amount allowed in CET1 capital of the consolidation group)	–	
6	**CET1 capital before regulatory deductions**	**30,186,136**	
CET1 capital: regulatory deductions			
7	Valuation adjustments	–	
8	Goodwill (net of associated deferred tax liabilities)	–	
9	Other intangible assets (net of associated deferred tax liabilities)	–	
10	Deferred tax assets (net of associated deferred tax liabilities)	28,154	(7)
11	Cash flow hedge reserve	–	
12	Excess of total EL amount over total eligible provisions under the IRB approach	–	
13	Credit-enhancing interest-only strip, and any gain-on-sale and other increase in the CET1 capital arising from securitization transactions	–	
14	Gains and losses due to changes in own credit risk on fair valued liabilities	–	
15	Defined benefit pension fund net assets (net of associated deferred tax liabilities)	–	
16	Investments in own CET1 capital instruments (if not already netted off paid-in capital on reported balance sheet)	–	
17	Reciprocal cross-holdings in CET1 capital instruments	–	
18	Insignificant LAC investments in CET1 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation (amount above 10% threshold)	1,650,384	(4)
19	Significant LAC investments in CET1 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation (amount above 10% threshold)	–	
20	Mortgage servicing rights (net of associated deferred tax liabilities)	Not applicable	
21	Deferred tax assets arising from temporary differences (net of associated deferred tax liabilities)	Not applicable	
22	Amount exceeding the 15% threshold	Not applicable	
23	of which: significant investments in the ordinary share of financial sector entities	Not applicable	

2 Capital structure and adequacy (Continued)

Composition of regulatory capital (Continued)

		Component of regulatory capital reported by bank	Cross-referenced to balance sheet under regulatory scope of consolidation
24	of which: mortgage servicing rights	Not applicable	
25	of which: deferred tax assets arising from temporary differences	Not applicable	
26	National specific regulatory adjustments applied to CET1 capital	935,293	
26a	Cumulative fair value gains arising from the revaluation of land and buildings (own-use and investment properties)	–	
26b	Regulatory reserve for general banking risks	935,293	(14)
26c	Securitization exposures specified in a notice given by the Monetary Authority	–	
26d	Cumulative losses below depreciated cost arising from the institution's holdings of land and buildings	–	
26e	Capital shortfall of regulated non-bank subsidiaries	–	
26f	Capital investment in a connected company which is a commercial entity (amount above 15% of the reporting institution's capital base)	–	
27	Regulatory deductions applied to CET1 capital due to insufficient AT1 capital and Tier 2 capital to cover deductions	–	
28	**Total regulatory deductions to CET1 capital**	**2,613,831**	
29	**CET1 capital**	**27,572,305**	
	AT1 capital: instruments		
30	Qualifying AT1 capital instruments plus any related share premium	–	
31	of which: classified as equity under applicable accounting standards	–	
32	of which: classified as liabilities under applicable accounting standards	–	
33	Capital instruments subject to phase out arrangements from AT1 capital	–	
34	AT1 capital instruments issued by consolidated bank subsidiaries and held by third parties (amount allowed in AT1 capital of the consolidation group)	–	
35	of which: AT1 capital instruments issued by subsidiaries subject to phase out arrangements	–	
36	**AT1 capital before regulatory deductions**	**–**	
	AT1 capital: regulatory deductions		
37	Investments in own AT1 capital instruments	–	
38	Reciprocal cross-holdings in AT1 capital instruments	–	
39	Insignificant LAC investments in AT1 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation (amount above 10% threshold)	–	
40	Significant LAC investments in AT1 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation	–	
41	National specific regulatory adjustments applied to AT1 capital	–	
42	Regulatory deductions applied to AT1 capital due to insufficient Tier 2 capital to cover deductions	–	
43	**Total regulatory deductions to AT1 capital**	**–**	
44	**AT1 capital**	**–**	
45	**Tier 1 capital (Tier 1 = CET1 + AT1)**	**27,572,305**	

2 Capital structure and adequacy (Continued)

Composition of regulatory capital (Continued)

		Component of regulatory capital reported by bank	Cross-referenced to balance sheet under regulatory scope of consolidation
	Tier 2 capital: instruments and provisions		
46	Qualifying Tier 2 capital instruments plus any related share premium	4,257,647	(9)
47	Capital instruments subject to phase out arrangements from Tier 2 capital	–	
48	Tier 2 capital instruments issued by consolidated bank subsidiaries and held by third parties (amount allowed in Tier 2 capital of the consolidation group)	–	
49	of which: capital instruments issued by subsidiaries subject to phase out arrangements	–	
50	Collective provisions and regulatory reserve for general banking risks eligible for inclusion in Tier 2 capital	1,332,729	(10) + (14) – (1) – (2) – (3) – (5) – (6) – (8)
51	**Tier 2 capital before regulatory deductions**	**5,590,376**	
	Tier 2 capital: regulatory deductions		
52	Investments in own Tier 2 capital instruments	–	
53	Reciprocal cross-holdings in Tier 2 capital instruments and non-capital LAC liabilities	–	
54	Insignificant LAC investments in Tier 2 capital instruments issued by, and non-capital LAC liabilities of, financial sector entities that are outside the scope of regulatory consolidation (amount above 10% threshold and, where applicable, 5% threshold)	–	
54a	Insignificant LAC investments in non-capital LAC liabilities of financial sector entities that are outside the scope of regulatory consolidation (amount formerly designated for the 5% threshold but no longer meets the conditions) (for institutions defined as "section 2 institution" under §2(1) of Schedule 4F to BCR only)	–	
55	Significant LAC investments in Tier 2 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation (net of eligible short positions)	–	
55a	Significant LAC investments in non-capital LAC liabilities of financial sector entities that are outside the scope of regulatory consolidation (net of eligible short positions)	–	
56	National specific regulatory adjustments applied to Tier 2 capital	–	
56a	Add back of cumulative fair value gains arising from the revaluation of land and buildings (own-use and investment properties) eligible for inclusion in Tier 2 capital	–	
56b	Regulatory deductions applied to Tier 2 capital to cover the required deductions falling within §48(1)(g) of BCR	–	
57	**Total regulatory adjustments to Tier 2 capital**	**–**	
58	**Tier 2 capital**	**5,590,376**	
59	**Total regulatory capital (TC = Tier 1 + Tier 2)**	**33,162,681**	
60	**Total risk weighted assets**	**169,830,908**	

2 Capital structure and adequacy (Continued)

Composition of regulatory capital (Continued)

		Component of regulatory capital reported by bank	Cross-referenced to balance sheet under regulatory scope of consolidation
Capital ratios (as a percentage of risk weighted assets)			
61	**CET1 capital ratio**	**16.2%**	
62	**Tier 1 capital ratio**	**16.2%**	
63	**Total capital ratio**	**19.5%**	
64	**Institution-specific buffer requirement (capital conservation buffer plus countercyclical capital buffer plus higher loss absorbency requirements)**	**3.8%**	
65	of which: capital conservation buffer requirement	2.5%	
66	of which: bank specific countercyclical capital buffer requirement	1.3%	
67	of which: higher loss absorbency requirement	0.0%	
68	**CET1 (as a percentage of RWA) available after meeting minimum capital requirements**	**10.2%**	
National minima (if different from Basel 3 minimum)			
69	National CET1 minimum ratio	Not applicable	
70	National Tier 1 minimum ratio	Not applicable	
71	National Total capital minimum ratio	Not applicable	
Amounts below the thresholds for deduction (before risk weighting)			
72	Insignificant LAC investments in CET1, AT1 and Tier 2 capital instruments issued by, and non-capital LAC liabilities of, financial sector entities that are outside the scope of regulatory consolidation	2,922,269	
73	Significant LAC investments in CET1 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation	712,015	
74	Mortgage servicing rights (net of associated deferred tax liabilities)	Not applicable	
75	Deferred tax assets arising from temporary differences (net of associated deferred tax liabilities)	Not applicable	
Applicable caps on the inclusion of provisions in Tier 2 capital			
76	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to the BSC approach, or the STC approach and SEC-ERBA, SEC-SA and SEC-FBA (prior to application of cap)	1,332,729	
77	Cap on inclusion of provisions in Tier 2 under the BSC approach, or the STC approach, and SEC-ERBA, SEC-SA and SEC-FBA	1,903,880	
78	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to the IRB approach and SEC-IRBA (prior to application of cap)	–	
79	Cap for inclusion of provisions in Tier 2 under the IRB approach and SEC-IRBA	–	

2 Capital structure and adequacy (Continued)

Composition of regulatory capital (Continued)

		Component of regulatory capital reported by bank	Cross-referenced to balance sheet under regulatory scope of consolidation
Capital instruments subject to phase-out arrangements (only applicable between 1 January 2018 and 1 January 2022)			
80	Current cap on CET1 capital instruments subject to phase out arrangements	Not applicable	
81	Amount excluded from CET1 capital due to cap (excess over cap after redemptions and maturities)	Not applicable	
82	Current cap on AT1 capital instruments subject to phase out arrangements	–	
83	Amount excluded from AT1 capital due to cap (excess over cap after redemptions and maturities)	–	
84	Current cap on Tier 2 capital instruments subject to phase out arrangements	–	
85	Amount excluded from Tier 2 capital due to cap (excess over cap after redemptions and maturities)	–	

Note to the template:

Element where a more conservative definition has been applied in the BCR relative to that set out in Basel III capital standards:

Row No.	Description	Hong Kong basis	Basel III basis
10	**Deferred tax assets ("DTA") (net of associated deferred tax liabilities)**	**28,154**	**–**
	Explanation As set out in paragraphs 69 and 87 of the Basel III text issued by the Basel Committee (December 2010), DTAs of the bank to be realized are to be deducted, whereas DTAs which relate to temporary differences may be given limited recognition in CET1 capital (and hence be excluded from deduction from CET1 capital up to the specified threshold). In Hong Kong, an AI is required to deduct all DTAs in full, irrespective of their origin, from CET1 capital. Therefore, the amount to be deducted as reported in row 10 may be greater than that required under Basel III. The amount reported under the column "Basel III basis" in this box represents the amount reported in row 10 (i.e. the amount reported under the "Hong Kong basis") adjusted by reducing the amount of DTAs to be deducted which relate to temporary differences to the extent not in excess of the 10% threshold set for DTAs arising from temporary differences and the aggregate 15% threshold set for MSRs, DTAs arising from temporary differences and significant investments in CET1 capital instruments issued by financial sector entities (excluding those that are loans, facilities or other credit exposures to connected companies) under Basel III.		
Remarks: The amount of the 10% threshold mentioned above is calculated based on the amount of CET1 capital determined in accordance with the deduction methods set out in BCR Schedule 4F. The 15% threshold is referring to paragraph 88 of the Basel III text issued by the Basel Committee (December 2010) and has no effect to the Hong Kong regime.			

Footnote:
CET1 Common Equity Tier 1
AT1 Additional Tier 1

2 Capital structure and adequacy (Continued)

Main features of regulatory capital instruments

The main features of regulatory capital instruments as at 31 December 2019 are shown below. Full terms and conditions are published in the Bank's website of http://www.shacombank.com.hk and are accessible at the following direct link: http://www.shacombank.com.hk/eng/about/regulatory/20191231.jsp

		Ordinary shares	Subordinated notes due 2027	Subordinated notes due 2029
1	Issuer	Shanghai Commercial Bank Limited	Shanghai Commercial Bank Limited	Shanghai Commercial Bank Limited
2	Unique identifier (eg CUSIP, ISIN or Bloomberg identifier for private placement)	N/A	ISIN: XS1720518478	ISIN: XS1892105823
3	Governing law(s) of the instrument	Laws of Hong Kong	English law, except that the subordination provisions shall be governed by the laws of Hong Kong.	English Law, except that the subordination provisions shall be governed by the laws of Hong Kong.
	Regulatory treatment			
4	Transitional Basel III rules[#]	N/A	N/A	N/A
5	Post-transitional Basel III rules[+]	Common Equity Tier 1	Tier 2	Tier 2
6	Eligible at solo*/group/ group & solo	Solo and Group	Solo and Group	Solo and Group
7	Instrument type (types to be specified by each jurisdiction)	Ordinary shares	Other Tier 2 instruments	Other Tier 2 instruments
8	Amount recognised in regulatory capital (Currency in million, as of most recent reporting date)	HK$2,000 million	HK$1,935 million	HK$2,323 million
9	Par value of instrument	N/A	US$250 million	US$300 million
10	Accounting classification	Shareholders' equity	Liability-amortised cost	Liability-amortised cost
11	Original date of issuance	1951, 1968, 1969 ,1970, 1972, 1973, 1975, 1979, 1981, 1985, 1988, 1990, 1991, 1996, 2000	29 November 2017	17 January 2019
12	Perpetual or dated	Perpetual	Dated	Dated
13	Original maturity date	No maturity	29 November 2027	17 January 2029
14	Issuer call subject to prior supervisory approval	No	Yes	Yes
15	Optional call date, contingent call dates and redemption amount	N/A	One-off call date: 29 November 2022. Additional optional redemption in whole at 100% of principal amount with accrued interest for taxation reasons, tax deductions reasons and regulatory reasons. Redemption amount subject to adjustment following occurrence of a Non-Viability Event. Redemption subject to prior written consent of the HKMA.	One-off call date: 17 January 2024. Additional optional redemption in whole at 100% of principal amount with accrued interest for taxation reasons, tax deductions reasons and regulatory reasons. Redemption amount subject to adjustment following occurrence of a Non-Viability Event. Redemption subject to prior written consent of the HKMA.
16	Subsequent call dates, if applicable	N/A	N/A	N/A

2 Capital structure and adequacy (Continued)

Main features of regulatory capital instruments (Continued)

		Ordinary shares	Subordinated notes due 2027	Subordinated notes due 2029
	Coupons/dividends			
17	Fixed or floating dividend/ coupon	Floating	Fixed	Fixed
18	Coupon rate and any related index	N/A	3.75% p.a. Fixed until 29 November 2022 and thereafter reset to a new fixed rate equal to the sum of the then prevailing U.S. Treasury Rate and the Spread at Pricing.	5.00% p.a. Fixed until 17 January 2024 and thereafter reset to a new fixed rate equal to the sum of the then prevailing U.S. Treasury Rate and the Spread at Pricing.
19	Existence of a dividend stopper	No	No	No
20	Fully discretionary, partially discretionary or mandatory	Fully discretionary	Mandatory	Mandatory
21	Existence of step up or other incentive to redeem	No	No	No
22	Non-cumulative or cumulative	Non-cumulative	Cumulative	Cumulative
23	Convertible or non-convertible	Non-convertible	Non-convertible	Non-convertible
24	If convertible, conversion trigger (s)	N/A	N/A	N/A
25	If convertible, fully or partially	N/A	N/A	N/A
26	If convertible, conversion rate	N/A	N/A	N/A
27	If convertible, mandatory or optional conversion	N/A	N/A	N/A
28	If convertible, specify instrument type convertible into	N/A	N/A	N/A
29	If convertible, specify issuer of instrument it converts into	N/A	N/A	N/A
30	Write-down feature	No	Yes	Yes
31	If write-down, write-down trigger(s)	N/A	The earlier of the HKMA notifying the issuer in writing: (i) that the HKMA is of the opinion that a write-off or conversion is necessary, without which the Issuer would become non-viable or (ii) that a decision has been made by the government body, a government officer or other relevant regulatory body with the authority to make such a decision, that a public sector injection of capital or equivalent support is necessary, without which the Issuer would become non-viable.	The earlier of the HKMA notifying the issuer in writing: (i) that the HKMA is of the opinion that a write-off or conversion is necessary, without which the Issuer would become non-viable or (ii) that a decision has been made by the government body, a government officer or other relevant regulatory body with the authority to make such a decision, that a public sector injection of capital or equivalent support is necessary, without which the Issuer would become non-viable.

2 Capital structure and adequacy (Continued)

Main features of regulatory capital instruments (Continued)

		Ordinary shares	Subordinated notes due 2027	Subordinated notes due 2029
32	If write-down, full or partial	N/A	May be in part or in full	May be in part or in full
33	If write-down, permanent or temporary	N/A	Permanent	Permanent
34	If temporary write-down, description of write-up mechanism	N/A	N/A	N/A
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument in the insolvency creditor hierarchy of the legal entity concerned).	N/A	The rights of the holders will, in the event of the winding up of the Bank, rank (i) subordinate and junior in right of payment to, and of all claims of, (a) all unsubordinated creditors of the Issuer (including its depositors), and (b) all other Subordinated Creditors of the Issuer whose claims are stated to rank senior to the Notes or rank senior to the Notes by operation of law or contract; (ii) pari passu in right of payment to and of all claims of the holders of Parity Obligations; and (iii) senior in right of payment to, and of all claims of, (a) the holders of Junior Obligations, and (b) holders of Tier 1 Capital Instruments of the Issuer.	The rights of the holders will, in the event of the winding up of the Bank, rank (i) subordinate and junior in right of payment to, and of all claims of, (a) all unsubordinated creditors of the Issuer (including its depositors), and (b) all other Subordinated Creditors of the Issuer whose claims are stated to rank senior to the Notes or rank senior to the Notes by operation of law or contract; (ii) pari passu in right of payment to and of all claims of the holders of Parity Obligations; and (iii) senior in right of payment to, and of all claims of, (a) the holders of Junior Obligations, and (b) holders of Tier 1 Capital Instruments of the Issuer.
36	Non-compliant transitioned features	No	No	No
37	If yes, specify non-compliant features	N/A	N/A	N/A

Footnote:

[#] Regulatory treatment of capital instruments subject to transitional arrangements provided for in Schedule 4H of the BCR

[+] Regulatory treatment of capital instruments not subject to transitional arrangement provided for in Schedule 4H of the BCR

* Include solo-consolidated

N/A Not applicable

3 Overview of risk management and RWA

(a) Overview of risk management

The Group's risk management framework is designed to cover all business processes and ensure various risks are properly managed and controlled in the course of conducting business. The key financial risks related to the Group's business include credit risk, counterparty credit risk, market risk, liquidity risk, interest rate risk and operational risk. Further information on the management of these risks is set out within the Regulatory Disclosures and Notes to the Consolidated Financial Statements as follows:

– Credit risk	– Note 7 of Regulatory Disclosures and Note 3.1 of Notes to the Consolidated Financial Statements
– Counterparty credit risk	– Note 8 of Regulatory Disclosures
– Market risk	– Note 9 of Regulatory Disclosures and Note 3.2 of Notes to the Consolidated Financial Statements
– Liquidity risk	– Note 10 of Regulatory Disclosures and Note 3.3 of Notes to the Consolidated Financial Statements
– Interest rate risk in the banking book	– Note 11 of Regulatory Disclosures and Note 3.2.4 of Notes to the Consolidated Financial Statements
– Operational risk	– Note 3.6 of Notes to the Consolidated Financial Statements

Risk culture

The Group has long recognised the importance of a strong risk culture which is the core value of the Group and is endorsed by the Board of Directors ("the Board") and being followed by the senior management. The risk culture of the Group is created through setting and complying with the risk management strategies and core risk management principles as well as establishing a sound risk management systems and effective risk management process to address material risks under normal and stressed conditions in a forward-looking approach. Risk awareness is promoted to all staff to enhance the Group's overall risk management through appropriate training. The Group's risk culture is further reinforced by the Group's remuneration system that is established to ensure that incentives would not create excessive or undue risk exposure and unethical behaviour which could threaten the reputation as well as safety and soundness of the Group.

Risk governance

The Board has the ultimate responsibility for the effective management of risk and approves and oversees the Group's overall risk management framework. The Board delegates its power to supervise the Group's major functional areas, including treasury, retail banking, corporate banking, risk management, wealth management, credit control and financial control, and the risks associated with them to the Risk Committee, the Audit Committee, and the Executive Committee. The Risk Committee in particular has the authority and responsibility to oversee and guide the overall management of the collective set of different risks undertaken by the Group.

The Chief Executive, Chief Risk Officer and the senior management have the responsibility to ensure various risk limits are appropriately established according to the risk management strategies set by the Board, and to oversee the effectiveness of managing and controlling risk in the day-to-day management of the Group.

Various business and functional units of the Group have their respective risk management responsibilities. Business units act as the first line of defense in risk management while other functional units, in particular Risk Management Division and Credit Division, which are independent from the business units and act as the second line of defense, assist in managing different kinds of risks.

Internal Audit Department as the third line of defense is responsible for providing independent assurance through conducting internal audits, and reporting to the Audit Committee on the quality of risk controls and management, the adequacy and the compliance of internal policies and procedures.

3 Overview of risk management and RWA (Continued)

(a) Overview of risk management (Continued)

Risk appetite

The Group's Risk Appetite Statement is reviewed and approved by the Board from time to time but at least annually with reference to evolving industry and market development, which describes the level of risk that the Group is prepared to accept in pursuit of the Group's strategic objectives. The Group adopts a low risk appetite in managing and controlling risks in a prudent manner with a view to achieving steady growth and reasonable returns.

Various ratios and risk limits are set according to the legal and regulatory requirements to limit and control the risk exposure of the Group under a risk tolerance level acceptable to the Group and commensurate with the risk adverse culture as well as prudent management practice.

Stress testing

Stress testing is a risk management tool and involves the use of various techniques to assess the Group's potential vulnerability to adverse changes in market conditions. It is conducted with hypothetical as well as historical assumptions. With the establishment of various alerting levels under different scenarios, it helps to alert the management to adverse unexpected outcomes related to a variety of risks and provides an indication to the amount of financial resources (including capital and liquidity) that might be necessary for absorbing losses caused by, or to withstand, severe stressed conditions.

Risk information reporting, risk measurement and reporting systems

The Group has developed various systems for risk measurement and reporting for different risk exposures. Further information on the measurement and reporting of credit risk, market risk, liquidity risk and interest rate risk in the banking book exposures are provided in Note 7(a), Note 9(a), Note 10 and Note 11 of Regulatory Disclosures respectively.

A quarterly report on risk exposures and risk management activities of the Group is presented to the Risk Committee; which covers the assessment on major risk exposures including credit risk, market risk, interest rate risk in the banking book, liquidity risk, legal risk, compliance and regulatory risk, operational risk, reputation risk, strategic risk and technology risk. Besides, the results of stress tests, maintenance of regulatory risk limits and risk monitoring on overseas branches are also presented.

The Group continues to invest significant resources in IT systems and processes in order to maintain and improve the risk management capabilities. A number of key initiatives and projects to enhance consistent data aggregation, reporting and management, and work towards meeting new regulatory standards are in progress.

Risk mitigation

The Group applies different strategies and processes to hedge and mitigate different risks. Exposure to credit risk is mitigated 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. Collateral or other security is not usually obtained for credit risk exposures on derivatives instruments, except where the Group requires margin deposits from counterparties. For liquidity risk management, the Group uses results of stress-testing and reverse stress-testing to strengthen resilience to liquidity stress and serve as early-warning triggers for the formulation of management actions and contingency funding plan to mitigate potential stress and vulnerability which the Group might face.

3 Overview of risk management and RWA (Continued)

(b) Overview of RWA

The table below shows the breakdowns of RWA for various risks as at 31 December 2019 and 30 September 2019 and the minimum capital requirements as at 31 December 2019 are calculated by multiplying the Group's RWA by 8%.

		RWA		Minimum capital requirements
		31 December 2019	30 September 2019	**31 December 2019**
1	Credit risk for non-securitization exposures	**149,312,666**	144,315,588	**11,945,013**
2	Of which STC approach	**149,312,666**	144,315,588	**11,945,013**
2a	Of which BSC approach	**–**	–	**–**
3	Of which foundation IRB approach	**–**	–	**–**
4	Of which supervisory slotting criteria approach	**–**	–	**–**
5	Of which advanced IRB approach	**–**	–	**–**
6	Counterparty default risk and default fund contributions	**1,217,716**	1,706,279	**97,417**
7	Of which SA-CCR	**Not Applicable**	Not Applicable	**Not Applicable**
7a	Of which CEM	**1,217,716**	1,706,279	**97,417**
8	Of which IMM(CCR) approach	**–**	–	**–**
9	Of which others	**–**	–	**–**
10	CVA risk	**308,988**	413,788	**24,719**
11	Equity positions in banking book under the simple risk-weight method and internal models method	**–**	–	**–**
12	Collective investment scheme ("CIS") exposures - LTA	**Not Applicable**	Not Applicable	**Not Applicable**
13	CIS exposures - MBA	**Not Applicable**	Not Applicable	**Not Applicable**
14	CIS exposures - FBA	**Not Applicable**	Not Applicable	**Not Applicable**
14a	CIS exposures - combination of approaches	**Not Applicable**	Not Applicable	**Not Applicable**
15	Settlement risk	**–**	–	**–**
16	Securitization exposures in banking book	**–**	–	**–**
17	Of which SEC-IRBA	**–**	–	**–**
18	Of which SEC-ERBA (including IAA)	**–**	–	**–**
19	Of which SEC-SA	**–**	–	**–**
19a	Of which SEC-FBA	**–**	–	**–**
20	Market risk	**7,906,600**	7,863,763	**632,528**
21	Of which STM approach	**7,906,600**	7,863,763	**632,528**
22	Of which IMM approach	**–**	–	**–**
23	Capital charge for switch between exposures in trading book and banking book (not applicable before the revised market risk framework takes effect)	**Not Applicable**	Not Applicable	**Not Applicable**
24	Operational risk	**9,304,900**	9,139,838	**744,392**
24a	Sovereign concentration risk	**–**	–	**–**
25	Amounts below the thresholds for deduction (subject to 250% RW)	**1,780,038**	1,493,763	**142,403**
26	Capital floor adjustment	**–**	–	**–**
26a	Deduction to RWA	**–**	–	**–**
26b	Of which portion of regulatory reserve for general banking risks and collective provisions which is not included in Tier 2 Capital	**–**	–	**–**
26c	Of which portion of cumulative fair value gains arising from the revaluation of land and buildings which is not included in Tier 2 Capital	**–**	–	**–**
27	**Total**	**169,830,908**	**164,933,019**	**13,586,472**

4 Linkages between financial statements and regulatory exposures

(a) Linkages between accounting and regulatory scopes of consolidation and mapping of financial statement categories with regulatory risk categories

			Carrying values of items:				
	Carrying values as reported in published financial statements	Carrying values under scope of regulatory consolidation	subject to credit risk framework	subject to counterparty credit risk framework	subject to the securitisation framework	subject to market risk framework	not subject to capital requirements or subject to deduction from capital
Assets							
Cash and balances with banks	34,128,614	34,127,171	34,127,171	–	–	–	–
Placements with banks	7,090,556	7,090,556	7,090,556	–	–	–	–
Loans and advances to customers	98,773,691	98,773,691	98,773,691	–	–	–	–
Financial assets at fair value through profit or loss	1,881,025	1,860,634	7,194	–	–	1,853,440	–
Derivative financial instruments	285,089	285,089	–	284,671	–	284,671	418
Investment securities at fair value through other comprehensive income	71,558,546	71,543,427	69,893,043	–	–	–	1,650,384
Investment securities at amortised cost	2,480,924	2,479,796	2,479,796	–	–	–	–
Properties for sale	449,462	449,462	449,462	–	–	–	–
Investments in associates and joint venture	417,663	188,000	188,000	–	–	–	–
Investments in and amounts due from subsidiaries	–	305,080	305,080	–	–	–	–
Properties and equipment	2,700,014	2,602,862	2,602,862	–	–	–	–
Investment properties	1,017,148	1,047,150	1,047,150	–	–	–	-
Deferred income tax assets	28,115	28,154	–	–	–	–	28,154
Other assets	1,814,267	1,764,051	1,349,650	–	–	–	414,401
Total assets	**222,625,114**	**222,545,123**	**218,313,655**	**284,671**	**–**	**2,138,111**	**2,093,357**
Liabilities							
Deposits and balances from banks	11,677,610	11,677,610	–	–	–	–	11,677,610
Deposits from customers	172,438,516	172,438,516	–	–	–	–	172,438,516
Derivative financial instruments	292,599	292,599	–	–	–	–	292,599
Amounts due to subsidiaries	–	505,722	–	–	–	–	505,722
Subordinated debts	4,257,647	4,257,647	–	–	–	–	4,257,647
Other liabilities	2,813,883	2,668,478	–	–	–	–	2,668,478
Current income tax liabilities	501,694	501,011	–	–	–	–	501,011
Deferred income tax liabilities	18,901	17,404	–	–	–	–	17,404
Total liabilities	**192,000,850**	**192,358,987**	–	–	–	–	**192,358,987**

4 Linkages between financial statements and regulatory exposures (Continued)

(b) Main sources of differences between regulatory exposure amounts and carrying values in financial statements

		Items subject to:			
	Total	credit risk framework	securitisation framework	counterparty credit risk framework	market risk framework
Asset carrying value amount under scope of regulatory consolidation (as per Regulatory Disclosures Note 4(a))	220,451,766	218,313,655	–	284,671	2,138,111
Liabilities carrying value amount under regulatory scope of consolidation (as per Regulatory Disclosures Note 4(a))	–	–	–	–	–
Total net amount under regulatory scope of consolidation	220,451,766	218,313,655	–	284,671	2,138,111
Off-balance sheet amounts	53,027,438	8,187,209	–	–	–
Differences due to consideration of provisions	385,332	385,332	–	–	–
Differences due to potential exposures for counterparty risk	1,813,271	–	–	1,813,271	–
Differences due to reversal of credit balance of other assets	16,252	16,252	–	–	–
Exposure amounts considered for regulatory purposes	275,694,059	226,902,448	–	2,097,942	2,138,111

(c) Explanations of differences between accounting and regulatory exposure amount

Basis of consolidation

The basis of consolidation for regulatory purposes is different from that for accounting purposes. Subsidiaries included in the consolidation for regulatory purposes are specified by the HKMA. Subsidiaries not included in consolidation for regulatory purposes are mainly securities and insurance companies that are authorised and supervised by the Securities and Futures Commission and Insurance Authority respectively.

Most of the principal subsidiaries of the Group are included under scope of regulatory consolidation that there are no material differences between the carrying values of assets as reported in published financial statements and under scope of regulatory consolidation.

Exposure amounts considered for regulatory purposes require adjustments to be made to the carrying value of assets as reported in published financial statements. The main adjustments taken by the Group include the consideration of provisions, off-balance sheet exposures and potential exposure of default risk.

The Group uses the standardised approach to calculate the risk-weighted assets for its credit risk and market risk exposures. For operational risk, the Group uses the basic indicator approach to calculate its operational risk capital charge. During the reporting period, the Group did not have any securitisation exposure. Stage 1 and Stage 2 impairment allowances that are deducted from the carrying amount of exposures in the financial statements need to be reintegrated in the regulatory exposure value under the standardised approach. Off-balance sheet contracts, such as guarantees and commitments, also carry credit risks. These exposures are converted to credit equivalent amounts and added to the regulatory exposure amounts. The default risk exposures of OTC derivative contracts as reported in the published financial statements include their fair value only. Potential exposures for counterparty credit risk of OTC derivative contracts are therefore needed to be added to the regulatory exposure amount.

4 Linkages between financial statements and regulatory exposures (Continued)

(c) Explanations of differences between accounting and regulatory exposure amount (Continued)

Valuation control framework

The Group has in place fair valuation policy to ensure adequate governance and control processes for the designation and valuation of financial instruments to be measured at fair value for financial reporting, risk management and regulatory capital purposes.

The Risk Committee is delegated by the Board to approve the fair valuation policy and to review the governance structure and control framework to ensure that fair values are either determined or validated by control units independent of risk taking units. Control units have overall responsibility for independent verification of valuation results from risk taking units and ensuring the valuation process for financial instruments is conducted effectively and appropriately. Revaluation reports of trading and non-trading positions are compiled regularly and submitted to senior management for review. Any significant valuation issues are reported to senior management, Asset and Liability Committee and Risk Committee.

Valuation methodologies and process

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market at the measurement date under current market conditions (i.e. an exit price) regardless whether the price is directly observable or estimated using another valuation technique.

For financial instrument with bid-offer close-out price, its fair value can be the price within the bid-offer price that is the most representative of fair value. All bid-offer market prices of the financial products, including foreign exchange, equities, debt securities and interest rate swap will be obtained from designated financial data service providers.

For financial instrument without bid-offer close-out price, the Group uses valuation techniques to establish the fair value of instruments including the use of recent arm's length market transactions between knowledgeable and willing parties, reference to the current fair value of another financial instrument that is substantially the same, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

Valuation adjustments

Valuation adjustments are an integral part of the valuation process. Appropriate valuation adjustments are made when the Group considers that there are additional factors that are not incorporated within the valuation methodologies or models such as illiquidity adjustment, concentration adjustment and valuation uncertainty adjustment.

Illiquidity adjustment will be taken if the securities are deemed illiquid that cannot be sold quickly due to a shortage of interested buyers or a lack of an established trading market. Where the Group holds a security that has a significant concentration ratio (ratio of amount of security held by the Group to the total issuance size), concentration adjustment may be required. To adopt illiquidity or concentration adjustment, securities with the same issuer and have nearby maturities as the security in subject would be selected and the yields of these securities would be extracted and interpolated as the yield of security in subject and the price of the illiquid security would then be calculated and compared with the price calculated by the usual valuation methodologies and processes.

The prices of certain debt securities may be less readily determinable from market data. If there is no quotation from designated financial data service providers, other sources will be sought such as the prices of most recent executed transactions. Standard deviation of the prices of the debt securities quoted by different rate sources will be calculated as the uncertainty of the prices quoted of the securities. If the standard deviation exceeds 2%, valuation uncertainty adjustment may be required. The fair value of the debt securities will be adjusted by the standard deviation of the prices of the corresponding securities.

As at 31 December 2019, no valuation adjustment was required as most of the Group's investments were listed equities or debt securities of straight bonds that did not contain any complex features.

5 Countercyclical capital buffer ("CCyB") ratio

CCyB ratio is calculated as the weighted average of the applicable jurisdictional CCyB ("JCCyB") ratio effective at the date for which the determination is made, in respect of the jurisdictions (including Hong Kong) where the Bank has private sector credit exposures. The weight to be attributed to a given jurisdiction's applicable CCyB ratio is the ratio of the Bank's aggregate RWA for its private sector credit exposures (in both the banking book and the trading book) in that jurisdiction where the location of the exposures is determined as far as possible on an ultimate risk basis to the sum of the Bank's aggregate RWA across all jurisdictions in which the Bank has private sector credit exposures.

Key drivers for the changes in exposure amounts include asset quality, credit growth and credit portfolio. The applicable JCCyB ratio for Hong Kong is determined by the HKMA based on the Initial Reference Calculator that is transparently calculated and made public, while the applicable JCCyB ratio in respect of a given jurisdiction outside Hong Kong may differ from the JCCyB ratio as determined by the relevant authority in that jurisdiction if the HKMA has determined and announced the application of a higher or lower rate.

The following table shows the CCyB ratio, the geographical breakdown of the RWA in relation to private sector credit exposures that are relevant to the calculation of CCyB ratio and which have an applicable JCCyB ratio greater than zero as at 31 December 2019.

	Jurisdiction	Applicable JCCyB ratio in effect	Total RWA used in computation of CCyB ratio	CCyB ratio	CCyB amount
		%	HK$'000	%	HK$'000
1	Hong Kong SAR	2.0%	78,481,404		
2	France	0.3%	23,017		
3	United Kingdom	1.0%	433,721		
	Sum		**78,938,142**		
	Total		**123,932,021**	**1.3%**	**2,156,853**

6 Leverage ratio

The leverage ratio ("LR") represents the consolidated ratio computed in the same regulatory consolidation basis as the capital adequacy ratio. The table below presents the summary comparison of accounting assets against leverage ratio exposure measure as at 31 December 2019.

Item		Value under the LR framework
1	Total consolidated assets as per published financial statements (before adjustments for specific and collective provisions)	223,060,485
2	Adjustment for investments in banking, financial, insurance or commercial entities that are consolidated for accounting purposes but outside the scope of regulatory consolidation	(79,991)
3	Adjustment for fiduciary assets recognised on the balance sheet pursuant to the applicable accounting standard but excluded from the LR exposure measure	–
4	Adjustments for derivative contracts	1,813,271
5	Adjustment for SFTs (i.e. repos and similar secured lending)	–
6	Adjustment for off-balance sheet ("OBS") items (i.e. conversion to credit equivalent amounts of OBS exposures)	11,886,127
6a	Adjustment for specific and collective provisions that are allowed to be excluded from exposure measure	(435,371)
7	Other adjustments	(2,613,831)
8	**Leverage ratio exposure measure**	233,630,690

The leverage ratios as at 31 December 2019 and 30 September 2019 are shown below:

		31 December 2019	30 September 2019
	On-balance sheet exposures		
1	On-balance sheet exposures (excluding those arising from derivative contracts and SFTs, but including collateral)	222,695,405	214,146,412
2	Less: Asset amounts deducted in determining Tier 1 capital	(2,613,831)	(2,555,491)
3	**Total on-balance sheet exposures (excluding derivative contracts and SFTs)**	220,081,574	211,590,921
	Exposures arising from derivative contracts		
4	Replacement cost associated with all derivative contracts (where applicable net of eligible cash variation margin and/or with bilateral netting)	285,089	309,248
5	Add-on amounts for PFE associated with all derivative contracts	1,813,271	2,376,137
6	Gross-up for derivatives collateral provided where deducted from the balance sheet assets pursuant to the applicable accounting framework	–	–
7	Less: Deductions of receivables assets for cash variation margin provided under derivative contracts	–	–
8	Less: Exempted CCP leg of client-cleared trade exposures	–	–
9	Adjusted effective notional amount of written credit derivative contracts	–	–
10	Less: Adjusted effective notional offsets and add-on deductions for written credit derivative contracts	–	–
11	**Total exposures arising from derivative contracts**	2,098,360	2,685,385

6 Leverage ratio (Continued)

		31 December 2019	30 September 2019
	Exposures arising from SFTs		
12	Gross SFT assets (with no recognition of netting), after adjusting for sale accounting transactions	–	–
13	Less: Netted amounts of cash payables and cash receivables of gross SFT assets	–	–
14	CCR exposure for SFT assets	–	–
15	Agent transaction exposures	–	–
16	**Total exposures arising from SFTs**	–	–
	Other off-balance sheet exposures		
17	Off-balance sheet exposure at gross notional amount	53,027,438	50,063,581
18	Less: Adjustments for conversion to credit equivalent amounts	(41,141,311)	(38,661,837)
19	**Off-balance sheet items**	11,886,127	11,401,744
	Capital and total exposures		
20	**Tier 1 capital**	27,572,305	26,887,182
20a	**Total exposures before adjustments for specific and collective provisions**	234,066,061	225,678,050
20b	**Adjustments for specific and collective provisions**	(435,371)	(439,556)
21	**Total exposures after adjustments for specific and collective provisions**	233,630,690	225,238,494
	Leverage ratio		
22	**Leverage ratio**	11.8%	11.9%

Footnote:

CCP	Central counterparty
CCR	Counterparty credit risk
PFE	Potential future exposure
SFT	Securities financing transactions

7 Credit risk

(a) General information about 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. The Group's exposure to credit risk arises from a range of customer and product types, including exposures to corporate, retail and high net worth customers. The major corporate banking products offered by the Group include commercial loans and trade finance. The retail loans cover mortgage loans, consumer loans and credit cards.

The approach used for defining credit risk management policy and setting credit risk limits is described in Note 3.1 of Notes to the Consolidated Financial Statements.

Various analytical reports on credit risk exposures and credit risk management are provided monthly to senior management; including reports on loans and advances to customers, the credit risk profile of the Group, the portfolio distribution and credit quality, credit portfolio risk monitoring and compliance, impairment allowance and large exposures and risk concentrations.

7 Credit risk (Continued)

(a) General information about credit risk (Continued)

Credit risk management framework

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

The Credit Committee is responsible for establishing credit policies, monitoring loan portfolio quality and impairment charge, ensuring compliance with statutory and internal lending limits, evaluating credit applications, making credit decisions and etc. Further information on the Credit Committee is set out in the Corporate Governance Report included in the 2019 Annual Report.

The Chief Risk Officer takes charges of the Group's overall credit risk management. He is responsible for ensuring that the Group's risk management framework, all related policies and control procedures, and business processes are effective, adequate and properly implemented and consistent with the overall risk appetite of the Group and credit related regulatory requirements. He is also responsible for assessing, evaluating and monitoring the use of risk limits and ensuring that quantifiable risks are within the approved limits.

Various units of the Group have their respective credit risk management responsibilities. Business units including branches and business departments, being the first line of defence, are responsible for performing on-going 'know your customer' checks. The Credit Appraisal Department, Credit Control Department, Market Risk Management Department and the Compliance Department, which are independent from the business units, act as the second line of defence. The Credit Appraisal Department is responsible for independent evaluation of credit applications while Credit Control Department is responsible for performing credit monitoring and review. The Market Risk Management Department is responsible for monitoring the day-to-day management of the credit risk related to treasury operation. The Compliance Department is responsible for monitoring and ensuring that all the relevant regulatory and statutory requirements and limits are complied with by the Group. The Internal Audit Department, being the third line of defence, is responsible for examining and evaluating the adequacy, effectiveness, efficiency and reasonableness of the internal controls, risk management and governance systems and processes of the Group; and assessing compliance with regulatory and statutory requirements.

(b) Credit quality of exposures as at 31 December 2019

		Gross carrying amounts of		Allowances/ impairments	Of which ECL accounting provisions for credit losses on STC approach exposures		Of which ECL accounting provisions for credit losses on IRB approach exposures	Net values
		Defaulted exposures	Non-defaulted exposures		Allocated in regulatory category of specific provisions	Allocated in regulatory category of collective provisions		
1	Loans	479,466	98,707,625	413,400	37,935	375,465	–	98,773,691
2	Debt securities	–	69,304,304	20	–	20	–	69,304,284
3	Off-balance sheet exposures	–	16,038,252	4,103	–	4,103	–	16,034,149
4	**Total**	**479,466**	**184,050,181**	**417,523**	**37,935**	**379,588**	**–**	**184,112,124**

7 Credit risk (Continued)

(c) Changes in defaulted loans and debt securities

		Amount
1	Defaulted loans and debt securities as at end June 2019	434,930
2	Loans and debt securities that have defaulted since the last reporting period	67,952
3	Returned to non-defaulted status	–
4	Amounts written off	(6,532)
5	Other changes	(16,884)
6	**Defaulted loans and debt securities as at end December 2019**	**479,466**

(d) Additional disclosures related to credit quality of exposures

The accounting definition of impaired exposures and the regulatory definition of defaulted exposures are generally aligned. In general, loans and advances overdue for more than 90 days are considered impaired unless other information is available to indicate the contrary. Loans and advances with a specific repayment date are classified as overdue when the principal or interest is past due and remains unpaid. Loans and advances repayable by regular instalments are classified as overdue when an instalment payment is past due and remains unpaid. Loans and advances repayable on demand are classified as overdue when a demand for repayment has been served on the borrower but repayment has not been made in accordance with the instruction.

The approach for determining impairment of financial assets is provided in Notes 2.7 and 3.1.1 of Notes to the Consolidated Financial Statements.

As at 31 December 2019, loans and advances which were past due for more than 90 days were all impaired.

Rescheduled loans and advances to customers are those loans and advances that have been rescheduled or renegotiated for reasons related to the borrower's financial difficulties. A rescheduled loan will normally require an adverse classification under the loan classification system (i.e. substandard or doubtful).

7 Credit risk (Continued)

(d) Additional disclosures related to credit quality of exposures (Continued)

(i) Breakdown of credit risk exposures as at 31 December 2019 by industry sector, geographical region and residual maturity

	Total	Impaired exposure	Stage 3 impairment allowances	Amounts written-off
Credit risk exposure – By industry sector				
– Property investment	26,569,112	6,452	–	2,164
– Property development	27,619,550	391,170	–	–
– Banks and financial institutions	44,794,895	–	–	–
– International, wholesale and retail trade	18,686,888	92,544	30,465	3,787
– Personal	16,246,545	31,959	3,251	4,857
– Others*	50,195,134	46,266	4,219	–
Total	**184,112,124**	**568,391**	**37,935**	**10,808**
Credit risk exposure – By geographical region				
– Hong Kong	96,689,154	496,248	20,500	6,179
– Mainland China	29,674,690	60,507	17,435	–
– United States	31,523,574	6,675	–	2,465
– Others	26,224,706	4,961	–	2,164
Total	**184,112,124**	**568,391**	**37,935**	**10,808**
Credit risk exposure – By residual maturity				
– Repayable on demand	5,598,014			
– Up to 1 month	12,626,276			
– 1-3 months	24,291,113			
– 3-12 months	49,202,482			
– 1-5 years	68,091,028			
– Over 5 years	23,688,555			
– Indefinite	614,656			
Total	**184,112,124**			

* Others include exposures to manufacturing, hotels, catering, telecommunication, transport and other commercial and industrial activities where exposure to each of these sectors is less than 10% of the Group's total RWA for credit risk.

(ii) Aging analysis of accounting past due exposures as at 31 December 2019

	Gross carrying amount
Past due over 3 months but less than 6 months	46,975
Past due over 6 month but less than 1 year	2,049
Past due over 1 year	430,442
Total	**479,466**

(iii) Breakdown of restructured exposures between impaired and non-impaired exposures as at 31 December 2019

	Gross carrying amount of	
	Impaired	Not impaired
Rescheduled loans and advances	17,768	–

7 Credit risk (Continued)

(e) Qualitative disclosures related to credit risk mitigation

Collateral

The Group employs a range of policies and practices to mitigate credit risk which is described in Note 3.1.4(a) of Notes to the Consolidated Financial Statements.

Revaluation and management of collateral

To ascertain the estimated fair value of the collateral offered to the Group, collateral other than the bank deposits is revalued according to the Policy on Management of Collateral and Guarantees for monitoring the collateral position against relevant credit exposure.

The revaluation frequency depends on the collateral type but at least annually such as real estate, debt securities and equities. More frequent revaluation is needed for certain products, such as listed stocks which are revalued at least twice daily. The collateral value may be adjusted to reflect the likely net realizable value of such collateral.

Advice and service will be sought and employed from external legal professional whenever required to ensure all documentation creating the collateral and providing for the obligation of the parties with respect to each other in respect of the collateral is binding on all parties and legally enforceable in all relevant jurisdictions.

Recognition of risk mitigation under the standardised approach

The Group applies the simple approach for credit risk mitigation to all its on- and off-balance sheet banking book exposures that are subject to risk mitigation, where a claim on a counterparty is secured against eligible collateral, the secured portion of the claim must be weighted according to the risk-weight applicable to the collateral (unless that produces a higher risk-weight than would be applicable to the original counterparty, in which case the risk-weight applicable to that counterparty should apply). The unsecured portion of the claim must be weighted according to the risk-weight applicable to the original counterparty. The main types of recognised credit risk mitigant used by the Group include deposits and bank guarantee. In addition, real estate collateral is also recognised for past due exposures.

Where a claim on a counterparty is secured by a guarantee from an eligible guarantor, the portion of the claim that is supported by the guarantee is to be weighted according to the risk-weight applicable to the guarantor (unless the risk-weight applicable to the original counterparty is lower). The unsecured portion of the claim must be weighted according to the risk-weight applicable to the original counterparty.

For capital calculation, the Group has not used any on-balance sheet or off-balance sheet recognised netting for credit risk mitigation.

Concentrations within credit risk mitigations

Concentrations within credit risk mitigations taken may occur if a number of guarantors and collaterals with similar economic characteristics are engaged in comparable activities with changes in economic or industry conditions affecting their ability to meet contractual obligations. A range of quantitative tools is used to monitor the Group's credit risk mitigating activities including dedicated stress tests.

Stress-tests and scenario analysis are conducted on the Group's portfolio of collateral to assess the impact under unusual market conditions and relevant reports are submitted to the senior management for review in accordance with the Stress-Testing Policy of the Group.

The credit concentrations within the credit risk mitigation (recognised collateral and guarantees for capital calculation) used by the Group are within acceptable levels.

7 Credit risk (Continued)

(f) Overview of recognised credit risk mitigation as at 31 December 2019

		Exposures unsecured: carrying amount	Exposures to be secured	Exposures secured by recognised collateral	Exposures secured by recognised guarantees	Exposures secured by recognised credit derivative contracts
1	Loans	95,581,106	3,192,585	2,043,497	1,149,088	–
2	Debt securities	69,304,284	–	–	–	–
3	**Total**	**164,885,390**	**3,192,585**	**2,043,497**	**1,149,088**	**–**
4	Of which defaulted	18,649	426,142	426,142	–	–

(g) Qualitative disclosures on use of ECAI ratings under STC approach

Under the standardised approach ("STC") for the calculation of credit risk within the Basel capital framework, banks are required to use credit assessments provided by external credit assessment institutions ("ECAIs"), recognised by the HKMA for the purposes of regulatory capital calculation, to determine the risk-weights of the banks' credit exposures.

Standard & Poor's Ratings Services, Moody's Investors Service, Fitch Ratings and Rating and Investment Information, Inc. are the ECAIs that the Group has used for the determination of risk weightings for the following classes of exposure:

- Sovereign exposures;
- Public sector entity exposures;
- Bank exposures;
- Securities firm exposures;
- Corporate exposures; and
- Collective investment scheme exposures

The mapping of ECAI ratings of the above six classes of exposure to the risk weights under standardised approach follows the process as prescribed in Part 4 of the BCR. Where an exposure of debt securities has an issue-specific external credit assessment, such assessment will be used. In case there is no specific issue rating published by the ECAI, the issuer rating is applied to the senior unsecured claims of that issuer subject to the conditions prescribed by the BCR.

7 Credit risk (Continued)

(h) Credit risk exposures and effects of recognised credit risk mitigation – for STC approach as at 31 December 2019

	Exposure classes	Exposures pre-CCF and pre-CRM		Exposures post-CCF and post-CRM		RWA and RWA density	
		On-balance sheet amount	Off-balance sheet amount	On-balance sheet amount	Off-balance sheet amount	RWA	RWA density
1	Sovereign exposures	13,276,499	–	13,276,499	–	57,771	0%
2	PSE exposures	45,469	–	45,469	–	9,094	20%
2a	Of which: domestic PSEs	45,469	–	45,469	–	9,094	20%
2b	Of which: foreign PSEs	–	–	–	–	–	–
3	Multilateral development bank exposures	–	–	–	–	–	–
4	Bank exposures	72,872,889	964,401	73,719,297	192,880	24,932,886	34%
5	Securities firm exposures	93,492	1,357,346	93,492	–	46,746	50%
6	Corporate exposures	100,927,039	39,677,201	99,413,664	6,724,429	99,821,288	94%
7	CIS exposures	–	–	–	–	–	–
8	Cash items	781,309	–	1,965,455	–	109,137	6%
9	Exposures in respect of failed delivery on transactions entered into on a basis other than a delivery-versus-payment basis	–	–	–	–	–	–
10	Regulatory retail exposures	4,275,457	1,404,375	4,152,463	176,850	3,246,985	75%
11	Residential mortgage loans	9,766,859	1,953,426	9,764,529	964,750	5,378,778	50%
12	Other exposures which are not past due exposures	15,484,336	7,670,689	15,092,481	128,300	15,220,781	100%
13	Past due exposures	479,875	–	479,875	–	489,200	102%
14	Significant exposures to commercial entities	–	–	–	–	–	–
15	**Total**	**218,003,224**	**53,027,438**	**218,003,224**	**8,187,209**	**149,312,666**	**66%**

7 Credit risk (Continued)

(i) Credit risk exposures by asset classes and by risk weights – for STC approach as at 31 December 2019

	Exposure class \ Risk Weight	0%	10%	20%	35%	50%	75%	100%	150%	250%	Others	Total credit risk exposures amount (post CCF and post CRM)
1	Sovereign exposures	12,987,645	–	288,854	–	–	–	–	–	–	–	**13,276,499**
2	PSE exposures	–	–	45,469	–	–	–	–	–	–	–	**45,469**
2a	Of which: domestic PSEs	–	–	45,469	–	–	–	–	–	–	–	**45,469**
2b	Of which: foreign PSEs	–	–	–	–	–	–	–	–	–	–	**–**
3	Multilateral development bank exposures	–	–	–	–	–	–	–	–	–	–	**–**
4	Bank exposures	–	–	40,087,599	–	33,818,425	–	6,153	–	–	–	**73,912,177**
5	Securities firm exposures	–	–	–	–	93,492	–	–	–	–	–	**93,492**
6	Corporate exposures	–	–	373,512	–	12,035,985	–	93,728,596	–	–	–	**106,138,093**
7	CIS exposures	–	–	–	–	–	–	–	–	–	–	**–**
8	Cash items	1,492,020	–	455,373	–	–	–	18,062	–	–	–	**1,965,455**
9	Exposures in respect of failed delivery on transactions entered into on a basis other than a delivery-versus-payment basis	–	–	–	–	–	–	–	–	–	–	**–**
10	Regulatory retail exposures	–	–	–	–	–	4,329,313	–	–	–	–	**4,329,313**
11	Residential mortgage loans	–	–	–	8,131,793	–	259,349	2,338,137	–	–	–	**10,729,279**
12	Other exposures which are not past due exposures	–	–	–	–	–	–	15,220,781	–	–	–	**15,220,781**
13	Past due exposures	–	–	–	–	–	–	461,226	18,649	–	–	**479,875**
14	Significant exposures to commercial entities	–	–	–	–	–	–	–	–	–	–	**–**
15	**Total**	**14,479,665**	**–**	**41,250,807**	**8,131,793**	**45,947,902**	**4,588,662**	**111,772,955**	**18,649**	**–**	**–**	**226,190,433**

8 Counterparty credit risk

(a) Qualitative disclosures related to counterparty credit risk (including those arising from clearing through CCPs)

Counterparty credit risk arises from over-the-counter ("OTC") derivative contracts and securities financing transactions both in trading and banking book, and is subject to the same risk management framework. Credit equivalent amount and capital charge for the relevant counterparty credit exposures are determined following the regulatory capital requirements. The Group adopts the current exposure method to measure the credit equivalent amount, which comprises current exposures and potential future exposures. The relevant counterparty default risk capital charge is calculated under the standardised approach. The Group also adopts the standardised credit valuation adjustment ("CVA") method to calculate the relevant counterparty CVA capital charge.

The Group exercises strict control over counterparty credit risk exposure, including central counterparty ("CCP"). All credit limits are established in advance of transaction. Credit and settlement risk is captured, monitored and reported in accordance with the Group risk methodologies. The credit risk exposures associated with these contracts are predominantly their positive marked-to-market values. These credit risk exposures together with potential exposures from market movements are managed as part of the overall lending limits allowed to counterparties. Collateral or other security is not usually obtained for such credit risk exposures, except where the Group requires margin deposits from counterparties. In the case of a 2-notch downgrade of the Group's credit rating, the impact on the Group's derivative collateral requirements is minimal.

Wrong-way risk occurs when exposure to a counterparty is adversely correlated with the credit quality of that counterparty. It arises when default risk and credit exposure increase together. The OTC derivative contracts entered into by the Group are mainly foreign exchange contracts, most of which are not exposed to wrong-way risk. In instances where the Group has identified any significant general wrong-way risk, immediate and appropriate actions will be taken and the respective exposure will be under close monitoring in order to effectively manage the credit exposure and minimize losses. Specific wrong-way risk transactions are generally not allowed.

(b) Analysis of counterparty default risk exposures (other than those to CCPs) by approaches as at 31 December 2019

		Replacement cost (RC)	PFE	Effective EPE	Alpha (α) used for computing default risk exposure	Default risk exposure after CRM	RWA
1	SA-CCR (for derivative contracts)	–	–		1.4	–	–
1a	CEM	284,671	1,813,271		–	2,097,942	1,217,716
2	IMM (CCR) approach			–	–	–	–
3	Simple Approach (for SFTs)					–	–
4	Comprehensive Approach (for SFTs)					–	–
5	VaR (for SFTs)					–	–
6	**Total**						**1,217,716**

8 Counterparty credit risk (Continued)

(c) CVA capital charge as at 31 December 2019

		EAD post CRM	RWA
	Netting sets for which CVA capital charge is calculated by the advanced CVA method		
1	(i) VaR (after application of multiplication factor if applicable)		–
2	(ii) Stressed VaR (after application of multiplication factor if applicable)		–
3	Netting sets for which CVA capital charge is calculated by the standardized CVA method	2,097,942	308,988
4	**Total**	**2,097,942**	**308,988**

(d) Counterparty default risk exposures (other than those to CCPs) by asset classes and by risk weights – for STC approach as at 31 December 2019

	Exposure class \ Risk Weight	0%	10%	20%	35%	50%	75%	100%	150%	250%	Others	Total default risk exposure after CRM
1	Sovereign exposures	–	–	–	–	–	–	–	–	–	–	–
2	PSE exposures	–	–	–	–	–	–	–	–	–	–	–
2a	Of which: domestic PSEs	–	–	–	–	–	–	–	–	–	–	–
2b	Of which: foreign PSEs	–	–	–	–	–	–	–	–	–	–	–
3	Multilateral development bank exposures	–	–	–	–	–	–	–	–	–	–	–
4	Bank exposures	–	–	589,951	–	594,067	–	11,989	–	–	–	1,196,007
5	Securities firm exposures	–	–	–	–	–	–	–	–	–	–	–
6	Corporate exposures	–	–	–	–	222,463	–	233,932	–	–	–	456,395
7	CIS exposures	–	–	–	–	–	–	–	–	–	–	–
8	Regulatory retail exposures	–	–	–	–	–	–	–	–	–	–	–
9	Residential mortgage loans	–	–	–	–	–	–	–	–	–	–	–
10	Other exposures which are not past due exposures	–	–	–	–	–	–	445,540	–	–	–	445,540
11	Significant exposures to commercial entities	–	–	–	–	–	–	–	–	–	–	–
12	**Total**	**–**	**–**	**589,951**	**–**	**816,530**	**–**	**691,461**	**–**	**–**	**–**	**2,097,942**

8 Counterparty credit risk (Continued)

(e) Composition of collateral for counterparty default risk exposures (including those for contracts or transactions cleared through CCPs) as at 31 December 2019

		Derivative contracts				SFTs	
		Fair value of recognised collateral received		Fair value of posted collateral		Fair value of recognised collateral	Fair value of posted collateral
		Segregated	Unsegregated	Segregated	Unsegregated		
1	Cash – other currencies	–	–	–	71,300	–	–
2	**Total**	**–**	**–**	**–**	**71,300**	**–**	**–**

(f) Credit-related derivatives contracts

The Group did not have any credit-related derivatives contracts as at 31 December 2019.

(g) Exposures to CCPs

The Group did not have any exposures to CCPs as at 31 December 2019.

9 Market risk

(a) Qualitative disclosures related to 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 foreign exchange contracts, that comprise transactions initiated for the Group's own account and customer needs.

The Group's positions are managed by the Treasury Division under the limits and guidelines laid down in the foreign exchange risk management policy and the policy on allocating transactions of financial instruments to the trading, non-trading or investment book, which are approved by the Executive Committee. The Risk Management Division is responsible for monitoring the transactions to ensure the activities are within the relevant limits and guidelines.

Further information on the management of foreign exchange risk and interest rate risk is provided in Note 3.2.3 and Note 3.2.4 of Notes to the Consolidated Financial Statements respectively.

Market risk measurement

The measuring procedures and limit system used for market risk management have been approved by the Executive Committee (and also Risk Committee for the measuring procedures). Limits on notional, stop loss and sensitivity are set for trading positions which are marked-to-market daily. 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, the Asset and Liability Committee, the Risk Committee and the Board.

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

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 foreign exchange rate and interest rate contracts which are typically made OTC and are managed within limits approved by the Executive Committee and Risk Committee. The policy on the use of derivatives is reviewed by Risk Committee and recommended changes and amendments are approved by the Executive Committee or the Risk Committee. The Group has not designated any derivatives in any hedge relationship for the application of hedge accounting.

9 Market risk (Continued)

(b) Market risk under STM approach as at 31 December 2019

		RWA
	Outright product exposures	
1	Interest rate exposures (general and specific risk)	2,415,600
2	Equity exposures (general and specific risk)	–
3	Foreign exchange (including gold) exposures	5,491,000
4	Commodity exposures	–
	Option exposures	
5	Simplified approach	–
6	Delta-plus approach	–
7	Other approach	–
8	Securitization exposures	–
9	**Total**	**7,906,600**

10 Liquidity risk

(a) Qualitative disclosure related to liquidity risk management

Governance of liquidity risk management

The Group's risk tolerance describes the level of risk that the Group is prepared to accept to achieve its strategic and business objectives. The risk tolerance is reviewed and approved by the Board periodically but at least annually with reference to changing industry and market developments. An acceptable risk tolerance is adopted in managing and controlling risks in a prudent manner with a view to achieving steady growth and reasonable returns. Various ratios and risk limits are set with reference to the legal and regulatory requirements to limit and control the risk exposure under an acceptable risk tolerance level and commensurate with prudent liquidity risk management practices.

The Asset and Liability Committee has been delegated by the Board to manage the Group's liquidity risk strategy, policies and practices. The Committee membership consists of the chiefs of risk and control functions, and various business lines. Liquidity costs, benefits and risks are incorporated in the internal pricing, performance measurement and new product approval process for all significant activities, both on- and off-balance sheet.

The Group's liquidity is managed by the Treasury Division and monitored by management and the Asset and Liability Committee in accordance with the guidelines and procedures laid down in the liquidity risk management policy that has been approved by the Board.

Liquidity risk management

The Bank's operation is mainly funded by customer deposits and shareholders' funds. Diversified and stable funding sources are maintained by determining the appropriate mix of liabilities and building strong and lasting relationships with key fund providers in accordance with the liquidity risk management policy.

Liquidity is managed on a group basis, covering both the local and overseas operations as well as all related entities of the Bank. The formulation and management of the Group's funding strategy is centralised at the Treasury Division.

Adequate liquidity will be maintained at all times to meet obligations when they fall due in normal circumstances and an appropriate mix of additional stock of high quality liquid assets will be maintained to provide contingent liquidity in the event of a funding crisis. The normal borrowing capacity to obtain funds in the interbank market is estimated based on past experience and the wholesale funding needs for both local and foreign currencies is limited to an amount which is comfortably within that borrowing capacity.

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.

10 Liquidity risk (Continued)

(a) Qualitative disclosure related to liquidity risk management (Continued)

Stress testing

The stress-testing results form an important component in assisting the Risk Committee with reviewing and endorsing the Group's risk tolerance levels, which are defined by internal limits on various risk ratios, as well as assisting the Asset and Liability Committee in managing the overall liquidity of the Group and to make informed strategic business decisions.

Contingency funding plan

The Contingency Funding Plan is a component of the Group's Business Continuity Plan, and describes the Group's strategy for dealing with any liquidity problems, and the procedures for making up cash flow deficits in emergency situations.

(b) Quantitative disclosure

Customised measurement tools or metrics

A cash-flow approach is adopted to managing liquidity risk by ensuring that a net positive cash-flow position is maintained or otherwise sufficient cash can be generated from assets or funding sources to cover any funding shortfalls. The projections are forward-looking and covers liquidity risks stemming from on-balance sheet assets and liabilities and off-balance sheet positions. Cash-flow projections are made over daily time bands of up to 7 days ahead and wider time bands of up to 1 year ahead. Internal limits are set to control the size of the cumulative net mismatch positions for the shorter-term time bands. Cash-flow projections cover positions in HK dollar and in all currencies in aggregate. Separate cash-flow projections are also performed for individual foreign currencies in which there are significant positions, such as US dollar and the renminbi.

Concentration limits on collateral pools and sources of funding

Retail deposits account for an important part of the Group's funding base, and the composition and quality of such deposits are carefully monitored and managed. Core deposits are characterised by their stability and reliability and are identified based on internally defined criteria. An internal target is set for the proportion of core deposits against total deposits.

Liquidity exposures and funding needs at the level of individual legal entities, foreign branches and subsidiaries

The Group is not required to calculate the liquidity coverage ratio ("LCR") and net stable funding ratio ("NSFR") under the Banking (Liquidity) Rules. Instead, the Liquidity Maintenance Ratio ("LMR") and the Core Funding Ratio ("CFR") are used to measure respectively the short-term and long-term liquidity exposures of the Group against its funding needs. The LMR is the ratio of liquefiable assets to qualifying liabilities for the coming one month. Under the Banking Ordinance, the Group is subject to the statutory limit of the LMR, which is prescribed at 25%. The CFR is the ratio of the amount of available core funding to the amount of required core funding and measures the availability of funding from capital and liabilities to cover the amount of assets and off-balance sheet obligations that need to be funded. Under the Banking (Liquidity) Rules, the Group is under regulation to maintain a CFR of not less than 75% on average in each calendar month. Funding or liquidity support is provided to all branches outside of Hong Kong and such support is appropriately accounted for. The funding positions of the branches outside of Hong Kong are closely monitored and any regulatory or legal impediments to accessing liquidity will be addressed on a group basis. Other than branches outside of Hong Kong, the liquidity needs of other group companies are insignificant.

10 Liquidity risk (Continued)

(b) Quantitative disclosure (Continued)

Contractual maturity profile

	Next day	Within 1 month	> 1 month up to 3 months	> 3 months up to 1 year	> 1 year up to 5 years	Over 5 years	Balancing amount	Total
Currency notes and coins	762,738	–	–	–	–	–	–	762,738
Amount receivable arising from derivative contracts	228,911	905	1,789	10,415	9,658	–	–	251,678
Due from MA for a/c of Exchange Fund	2,601,976	–	–	–	–	–	–	2,601,976
Due from overseas central banks	4,753	–	–	–	–	–	177,526	182,279
Due from banks	16,784,621	13,859,007	3,138,646	3,952,016	–	–	–	37,734,290
Debt securities, prescribed instruments and structured financial instruments held (net of short positions)	55,720,566	199,446	356,976	6,461,807	5,617,582	2,798,136	2,874	71,157,387
Acceptances and bills of exchange held	43,805	121,556	184,965	22,728	–	–	–	373,054
Loans and advances to non-bank customers	5,601,824	5,360,532	10,398,603	22,449,876	36,171,872	18,321,800	1,598,873	99,903,380
Other assets	257,665	639,371	89,755	315,229	774,113	75,230	7,976,641	10,128,004
Total on-balance sheet assets	**82,006,859**	**20,180,817**	**14,170,734**	**33,212,071**	**42,573,225**	**21,195,166**	**9,755,914**	**223,094,786**
Total off-balance sheet claims	**–**	**781,054**	**183,347**	**61,318**	**–**	**–**	**633,531**	**1,659,250**
Deposits from non-bank customers	65,544,628	34,044,707	42,491,280	30,083,286	328,048	75,161	–	172,567,110
Amount payable arising from derivative contracts	236,420	905	1,789	10,415	9,658	–	–	259,187
Due to MA for a/c of Exchange Fund	–	–	389,218	–	–	–	–	389,218
Due to banks	2,616,927	4,690,635	3,585,042	813,482	–	–	–	11,706,086
Other liabilities	507,585	1,220,260	371,675	740,720	228,133	75,132	731,124	3,874,629
Capital and reserves	–	–	–	–	4,257,647	–	29,607,022	33,864,669
Total on-balance sheet liabilities	**68,905,560**	**39,956,507**	**46,839,004**	**31,647,903**	**4,823,486**	**150,293**	**30,338,146**	**222,660,899**
Total off-balance sheet obligations	**4,055,443**	**2,596,660**	**5,378,482**	**12,266,481**	**7,055,124**	**1,804,391**	**–**	**33,156,581**
Contractual Maturity Mismatch	**9,045,856**	**(21,591,296)**	**(37,863,405)**	**(10,640,995)**	**30,694,615**	**19,240,482**		
Cumulative Contractual Maturity Mismatch	**9,045,856**	**(5,735,598)**	**(50,408,845)**	**(120,615,644)**	**(124,105,562)**	**(11,114,743)**		

11 Interest rate risk in the banking book ("IRRBB")

Qualitative disclosure and quantitative disclosure are described in Note 3.2.4 of Notes to the Consolidated Financial Statements.

12 Non-bank Mainland exposures

The Bank	2019			2018		
Types of counterparties	On-balance sheet exposures	Off-balance sheet exposures	Total	On-balance sheet exposures	Off-balance sheet exposures	Total
1. Central government, central government-owned entities and their subsidiaries and joint ventures	8,709,448	–	8,709,448	6,292,131	2,208	6,294,339
2. Local governments, local government-owned entities and their subsidiaries and joint ventures	–	–	–	19,115	–	19,115
3. PRC nationals residing in Mainland China or other entities incorporated in Mainland China and their subsidiaries and joint ventures	6,654,865	1,344,663	7,999,528	7,298,028	1,372,484	8,670,512
4. Other entities of central government not reported in item 1 above	2,412,217	–	2,412,217	638,900	–	638,900
5. Other entities of local governments not reported in item 2 above	2,430,959	83,125	2,514,084	1,248,651	–	1,248,651
6. PRC nationals residing outside Mainland China or entities incorporated outside Mainland China where the credit is granted for use in Mainland China	7,201,890	633,321	7,835,211	7,056,484	1,113,220	8,169,704
7. Other counterparties where the exposures are considered by the reporting institution to be non-bank Mainland China exposures	922,241	501	922,742	600,757	519	601,276
Total	28,331,620	2,061,610	30,393,230	23,154,066	2,488,431	25,642,497
Total assets after provision	207,731,490			185,975,357		
On-balance sheet exposures as percentage of total assets	13.64%			12.45%		

13 Currency concentrations

Equivalent in Hong Kong dollars	2019 Spot assets	Spot liabilities	Forward purchases	Forward sales	Net options position	Net long/(short) position	Net structural position
US Dollars	89,701,000	(79,848,000)	34,007,000	(27,273,000)	–	16,587,000	584,000
Pound Sterling	7,448,000	(5,931,000)	2,208,000	(3,736,000)	–	(11,000)	50,000
Euro Dollars	1,226,000	(1,209,000)	89,000	(106,000)	–	–	–
Renminbi	20,021,000	(19,031,000)	4,623,000	(4,690,000)	–	923,000	6,104,000
Canadian Dollars	1,690,000	(1,692,000)	14,000	(12,000)	–	–	–
Australian Dollars	2,838,000	(2,894,000)	1,144,000	(1,079,000)	–	9,000	–
Other currencies and gold	2,345,000	(1,054,000)	1,984,000	(3,251,000)	–	24,000	–
	125,269,000	(111,659,000)	44,069,000	(40,147,000)	–	17,532,000	6,738,000

Equivalent in Hong Kong dollars	2018 Spot assets	Spot liabilities	Forward purchases	Forward sales	Net options position	Net long/(short) position	Net structural position
US Dollars	76,854,000	(67,708,000)	17,276,000	(19,360,000)	–	7,062,000	2,310,000
Pound Sterling	4,944,000	(4,923,000)	732,000	(757,000)	–	(4,000)	35,000
Euro Dollars	1,482,000	(1,479,000)	455,000	(456,000)	–	2,000	–
Renminbi	18,474,000	(17,488,000)	9,258,000	(9,423,000)	–	821,000	5,678,000
Canadian Dollars	1,260,000	(1,450,000)	218,000	(27,000)	–	1,000	–
Australian Dollars	3,512,000	(3,500,000)	875,000	(892,000)	–	(5,000)	–
Other currencies and gold	1,289,000	(1,081,000)	793,000	(982,000)	–	19,000	–
	107,815,000	(97,629,000)	29,607,000	(31,897,000)	–	7,896,000	8,023,000

Net structural position includes structural positions of the Bank's Hong Kong offices, overseas branches and subsidiaries. Structural assets and liabilities include:

- investments in properties and equipment, net of depreciation;
- capital, statutory reserves and unremitted profits of overseas branches; and
- investments in overseas subsidiaries and related company.

The net options position is calculated based on the delta-weighted positions of all foreign exchange option contracts.

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

14 Disclosure on Remuneration

GUIDING PRINCIPLES

The Bank aims to sustain long-term capital preservation and financial strength for the benefits of all stakeholders and is committed to promoting a sound corporate culture of prudent risk-taking at all levels of the Bank, with staff at all times conscientiously serving the Bank by adhering to the established values. The Remuneration Policy (the "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 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 (the "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. Johnson Mou Daid CHA. The other members are Dr. Richard LEE and Mr. Hung-ching YUNG.

The Committee reviews the Policy and the remuneration structure at least annually and the Policy will be submitted to the Board for approval. In 2019, the Committee held two meetings. The review covered the composition of the senior management and key personnel, the roles and responsibilities of the Committee, the Chief Executive, the Chief Risk Officer and Human Resources Division in relation to the remuneration system, the risk level and financial stability of the Bank, and the vesting of variable remuneration with reference to the risk appetite and the risk exposure of the Bank.

The Committee may at its discretion seek information and recommendations from relevant departments, committees or independent consultant as appropriate when conducting the review. In 2019, the Committee has not sought advice from external consultant on remuneration matters but has commissioned Internal Audit Department to conduct an independent review on the effectiveness of the Bank's remuneration system to ensure compliance with the principles set out in the Supervisory Policy Manual CG-5 "Guideline on a Sound Remuneration System" issued by the HKMA.

REMUNERATION OF DIRECTORS, SENIOR MANAGEMENT AND KEY PERSONNEL

The Committee is responsible for making recommendations to the Board on the formulation and review of the remuneration packages for Directors, the Chief Executive, senior management and key personnel, 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 associates shall be involved in deciding his/her own remuneration package.

14 Disclosure on Remuneration (Continued)

REMUNERATION STRUCTURE

The remuneration package is a combination of fixed and variable remuneration. Fixed remuneration consists of basic salary, allowances, double pay and provident fund contribution. Variable remuneration takes into account the overall performance of the Bank and individual business units, while individual performance is 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, which covers both financial and non-financial factors, would be differentiated into various levels, and be adequately and effectively evaluated. Final approval of the discretionary bonus which is all cash-based 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 established remuneration measures continued to apply in 2019. The timing and the portion of the performance-related bonus distribution are vested in the Committee and finally with the Board. The bonus (or part of it) may be withheld if the Bank's performance is not justified, or if the business objectives are not achieved, or when it is necessary to protect the financial soundness of the Bank.

DEFERRAL ARRANGEMENTS

In view of the Bank's existing business model and organization structure, a portion of the discretionary bonus payment of senior management and key personnel is subject to deferment arrangements as determined by the Committee and vesting by equal portions over a period of three years in order to align with the long-term value creation and time horizons of risk. In circumstances where it is later established that any performance measurement is proven to have been manifestly misstated, or it is later established that the employee concerned has committed fraud, malfeasance, or has violated material internal control policies or breached the relevant rules and regulations, all or part of the unvested deferred variable remuneration for a particular year shall be reduced.

14 Disclosure on Remuneration (Continued)

SENIOR MANAGEMENT AND KEY PERSONNEL REMUNERATION

Quantitative information on remuneration for the Bank's senior management and key personnel during the financial year of 2019, split into fixed and variable remuneration, is set out below:

Remuneration amount and quantitative information		Senior management	Key personnel
Fixed remuneration	Number of employees	12	7
	Total fixed remuneration	**40,266**	**9,919**
	Cash-based	40,266	9,919
	Of which: deferred	–	–
	Other forms	–	–
	Of which: deferred	–	–
Variable remuneration	Number of employees	11	7
	Total variable remuneration	**28,904**	**4,412**
	Cash-based	28,904	4,412
	Of which: deferred	5,772	636
	Other forms	–	–
	Of which: deferred	–	–
Total remuneration		**69,170**	**14,331**

Notes:

(i) Remuneration refers to all remuneration payable to employees during the year when being appointed as senior management or key personnel.

(ii) Senior management refers to the Chief Executive and division heads of major businesses and operations at the rank of Executive Vice President or above. Key personnel refers to employees whose duties or activities in the course of the employment involve the assumption of material risk or the taking on of material exposures on behalf of the Bank.

(iii) No senior management or key personnel has been awarded or paid sign-on award, guaranteed bonus or severance payment during the financial year of 2019.

Deferred and retained remuneration in 2019	Total amount of outstanding deferred remuneration	Of which: Total amount of outstanding deferred and retained remuneration exposed to ex post explicit and/or implicit adjustments	Total amount of amendment during the year of 2019 due to ex post explicit adjustments	Total amount of amendment during the year of 2019 due to ex post implicit adjustments	Total amount of deferred remuneration paid out in 2019
Senior management					
Cash	10,874	–	–	–	4,523
Other	–	–	–	–	–
Key personnel					
Cash	1,056	–	–	–	380
Other	–	–	–	–	–
Total	11,930	–	–	–	4,903

Note:

(i) The outstanding deferred remuneration in the financial year relates to the 2017, 2018 and 2019 variable remuneration.

BRANCHES AND SUBSIDIARIES

Management and Administration

Shanghai Commercial Bank Tower, 12 Queen's Road Central, Hong Kong
Telephone: (852) 2818 0282
Fax: (852) 2810 4623
SWIFT: SCBK HK HH
Web Site: www.shacombank.com.hk

Hong Kong Island Branches

Central Head Office	Lobby Floor, Shanghai Commercial Bank Tower, 12 Queen's Road Central
Aberdeen Branch	118 Aberdeen Main Road, Aberdeen
Causeway Bay Branch	18 Pennington Street, Causeway Bay
Connaught Road Branch	G/F & 1/F Southland Building, 48 Connaught Road Central, Central
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	G/F., 41-47 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	Shop 2, G/F, 57-61 Belcher's 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
Mody Road Branch	Units 101-103, 1/F., Wing On Plaza, 62 Mody Road, Tsimshatsui East
Mongkok Branch	666 Nathan Road, Mongkok

Kowloon Branches (Continued)

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 N117, 1/F., Temple Mall North, 136 Lung Cheung Road, Wong Tai Sin

New Territories and Outlying Island Branches

Kingswood Villa Branch	Shop G08, G/F., +WOO Phase 2, 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 4, G/F., Mee Tak Building, Nos. 27-31, 35-43 Kwong Fuk 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	Shops 1-3, G/F., Ming Wai Building, 4-26 Tuen Mun Heung Sze Wui Road, 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

BRANCHES AND SUBSIDIARIES (CONTINUED)

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 Branches

Shanghai Branch	Room 913, China Merchants Tower, 161 Lu Jia Zui Road (E), Pu Dong, Shanghai 200120, P.R.C.
Shanghai FTZ Sub-Branch	Room 03-05, 15/F, 55 Ji Long Rd, Pu Dong, Shanghai 200131, P.R.C.
Shenzhen Branch	Room 01-03, 20/F, Tower One, Kerry Plaza, No.1 Zhong Xin Si Road, Futian District, Shenzhen 518048, P.R.C.

Wholly-owned Subsidiaries

Glory Step Westpoint Investments Limited
Hai Kwang Property Management Company Limited
Infinite Financial Solutions Limited
KCC 23F Limited
KCC 25F Limited
KCC 26F 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 Westpoint Investments Limited

Subsidiaries

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