2009

集友銀行
Chiyu Banking Corporation Ltd.
中銀香港集團成員 A member of BOCHK Group

Annual Report

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Financial Highlights

	2009	2008	Change
For the year	**HK$'000**	HK$'000	+/(-)%
Net operating income before impairment allowances	**944,926**	1,145,044	-17.48
Operating profit	**491,537**	712,176	-30.98
Profit before taxation	**509,276**	714,267	-28.70
Profit for the year	**421,180**	591,183	-28.76
At year-end	**HK$'000**	HK$'000	+/(-)%
Capital and reserves	**4,090,125**	3,739,557	+9.37
Issued and fully paid share capital	**300,000**	300,000	-
Total assets	**39,944,869**	39,211,049	+1.87
Financial ratios	**%**	%	
Return on average capital and reserves[1]	**10.76**	14.73	-3.97
Return on average total assets[2]	**1.06**	1.51	-0.45
Cost to income ratio	**50.47**	36.66	+13.81
Loan to deposit ratio[3]	**54.10**	48.97	+5.13
Average liquidity ratio[4]	**44.20**	42.88	+1.32
Capital adequacy ratio[5]	**15.06**	15.37	-0.31

1. Return on average capital and reserves = $\dfrac{\text{Profit for the year}}{\text{Average of beginning and ending balance of capital and reserves}}$
2. Return on average total assets = $\dfrac{\text{Profit for the year}}{\text{Average of beginning and ending balance of total assets}}$
3. Loan to deposit ratio is calculated as at year end. Loan represents gross advances to customers. Deposit also includes structured deposits reported as "Financial liabilities designated at fair value through profit or loss".
4. Average liquidity ratio is calculated as the simple average of each calendar month's average liquidity ratio of local offices of Chiyu Banking Corporation Limited for the year.
5. Capital adequacy ratio is computed on the combined basis that comprises the positions of local offices and overseas branches of Chiyu Banking Corporation Limited specified by the Hong Kong Money Authority ("HKMA") for its regulatory purposes and in accordance with the Banking (Capital) Rules.

Five-Year Financial Summary

The financial information of the Group for the last five years commencing from 1 January 2005 is summarised below:

	2009	2008	2007	2006	2005
For the year	**HK$'000**	HK$'000	HK$'000	HK$'000	HK$'000
Net operating income before impairment allowances	**944,926**	1,145,044	1,177,834	931,491	766,592
Operating profit	**491,537**	712,176	930,983	668,074	577,103
Profit before taxation	**509,276**	714,267	942,273	675,018	590,793
Profit for the year	**421,180**	591,183	774,890	559,818	494,167
At year-end	**HK$'000**	HK$'000	HK$'000	HK$'000	HK$'000
Advances and other accounts	**18,582,368**	15,908,861	13,354,058	11,101,224	10,890,769
Total assets	**39,944,869**	39,211,049	39,039,964	33,985,794	31,233,146
Deposits from customer[1]	**33,817,255**	32,218,306	31,517,480	27,569,628	25,476,311
Total liabilities	**35,854,744**	35,471,492	34,754,823	30,042,341	27,441,970
Issued and fully paid share capital	**300,000**	300,000	300,000	300,000	300,000
Capital and reserves	**4,090,125**	3,739,557	4,285,141	3,943,453	3,791,176
Financial ratios	**%**	%	%	%	%
Return on average capital and reserves	**10.76**	14.73	18.83	14.48	13.62
Return on average total assets	**1.06**	1.51	2.12	1.72	1.59
Cost to income ratio	**50.47**	36.66	22.93	24.74	28.61
Loan to deposit ratio[1]	**54.10**	48.97	41.70	40.09	39.86

1. Deposits from customers also include structured deposits reported as "Financial liabilities designated at fair value through profit or loss".

Board of Management

Board of Management

Chief Executive

NG Man Kung

Deputy General Manager

CHAN Yiu Fai

ZHANG Yu Dong

Assistant General Manager

CHENG Pik Chuen

CHAN Kin Hing

LAW King Chee

The Consultant of Board of Directors

TAN Khek Seng

Management Discussion and Analysis

Business Review

The financial turmoil was still exerting its influence on the global economy in the first half of 2009. The combination of notable downturn in local GDP and decrease in foreign trade led to a weak demand in corporate lending. As the investment market remained uncertain, transactions of fund and bond related products suffered a sharp drop. Net interest margin was significantly narrowed under the low interest rate environment and the revenue of the banking sector was under pressure. Nevertheless, the sustained and rapid economic development in Mainland China has boosted the growth of Hong Kong's tourism-related businesses and domestic spending. Together with the rescue measures imposed by governments worldwide, the economy began to rebound in the second half of the year. With excessive capital inflows to Hong Kong, the stock and property markets regain their growth momentum and the banking industry is again fueled with vitality amid the tough operating environment.

Responding to opportunities and challenges in the markets, the Group takes positive yet prudent strategies and fully utilizes its competitive edge to expand traditional core businesses. On the one hand, through the participation of Hong Kong Special Administrative Region ("HKSAR")'s "SME Loan Guarantee Scheme", we dedicate to provide our Small and Medium Enterprises ("SME") clients financing services, as well as a full range of cross-border business solutions as the Group strives to establish its position as the ideal business partner of our clients who expand their businesses into Mainland China. On the other hand, through upgrading the electronic banking service, we move a step forward to provide a more convenient and cost-effective channel for our customers to execute banking transactions at anytime and anywhere, as well as to obtain real-time market information. The Group offers competitive mortgage schemes and efficient stock-related trading services to fulfill our customers' capital appreciation needs. To cope with market and credit risk under the unstable economic environment, the Group has put efforts to strengthen its credit risk control procedures; to enhance the analysis and selection of our investments in treasury products; to maintain high level of asset liquidity as well as quality; and to improve cost management for a better utilization of resources.

The Group's core businesses are to provide personal and corporate banking and other related financial services. With an all-rounded Commercial Banking Centre and 24 branches in Hong Kong, together with 2 branches and 1 sub-branch (launched in Xiamen Jimei in March 2009) in Mainland China, the Group has further enhanced its branch network to provide more efficient cross-border financial services to our customers. In line with the Renminbi business agreement between Mainland China and Hong Kong, we devote to provide personal and trade-related Reminibi services to our customers. Our Product Team strikes to develop and up-grade our products to meet the quick changing needs. We emphasize on improving our Customer Relationship Team's image and their professionalism, so that they can provide tailored-made flexible solutions to satisfy our customers' needs in a timely manner.

Management's Discussion and Analysis (continued)

Financial Review

For 2009, the Group recorded a profit attributable to shareholders of HK$421,180,000, dropped by 28.76% from last year, mainly due to the decrease of net interest income as a result of low market interest rate. The return on average shareholders' funds and the return on average total assets were 10.76% and 1.06%, respectively decreased by 3.97% and 0.45% against 2008.

Net interest income was HK$647,101,000, decreased by 21.78% as compared with 2008. Net interest margin was 1.70% or 55 basis points lower than last year. Non-interest income was HK$297,825,000, dropped by 6.28% from last year. Operating expenses rose by 13.62% to HK$476,935,000, which included a provision of HK$174,636,000 in relation to Lehman Brothers related products, representing an increase of 29.05% against last year. Should the effect of the expenses be excluded, the Group's operating expenses would have only increased by 6.27% while the cost-to-income ratio would have risen by 7.15% to 31.99% in 2009.

The Group has continued to apply vigilant credit risk management, the classified loans ratio maintained at a relatively low level of 0.12%. In 2009, net reversal of loan impairment allowances was HK$21,958,000, as compared with net charge of loan impairment allowances of HK$11,332,000 last year.

As at 31 December 2009, the Group recorded an increase in the total consolidated assets by 1.87% to HK$39,944,869,000. Loans and advances to customers rose by 15.97% to HK$18,296,796,000. Customer deposits also recorded an increase of 4.96% to HK$33,817,255,000.

Prospect

In 2010, the Group is of the view that the global economy will continue to revive from the Financial Tsunami while instability still exists. With the impact of Financial Tsunami gradually weakening, there will be more business opportunities in the banking sector in Hong Kong, but the operating environment is still filled with uncertainties and challenges.

According to the Group's business strategy "Base in Hong Kong; Penetrate into Mainland China; Tie with Overseas Chinese", we are devoted to provide flexible, efficient and tailor-made financial services to SME and comprehensive wealth management services to personal customers. We will fully utilize our competitive advantages on traditional banking services and provide services differentiation in order to further expand our scope of services to target customers. The Group will continue to develop its one-stop service platform in Mainland China for better capturing of business opportunities in the region. At the same time, we are committed to maintaining good corporate governance by allocating adequate resources to the aspects of risk management and internal control, as well as improving operational efficiency and resources utilization.

The Group's foundation remains solid and is ready for any challenges ahead. We would like to express our immense gratitude to the shareholders and the Board of Directors for their guidance and support. To reciprocate our customers' loyalty, we are devoted to provide them with excellent and efficient services. Last but not least, we would like to show our appreciation to all of our employees for their hard work and effort.

Management's Discussion and Analysis (continued)

Risk Management

Overview

The Group believes that sound risk management is a key success factor for any organisation. In its daily operation, the Group attaches a high degree of importance to risk management and emphasises that a balance must be struck between risk control and business growth and development. The principal types of risk inherent in the Group's businesses are reputation risk, legal and compliance risk, strategic risk, credit risk, market risk, interest rate risk, liquidity risk and operational risk. The Group's risk management objective is to enhance shareholder value by maintaining risk exposures within acceptable limits.

Risk Management Governance Structure

The Group's risk management governance structure is designed to cover the whole process of all businesses and ensure various risks are properly managed and controlled in the course of conducting business. The Group has a sound risk management organisational structure as well as comprehensive policies and procedures to identify measure, monitor and control various risks that may arise for the organisation. These risk management policies and procedures are regularly reviewed and modified to reflect changes in markets and business strategies. Various groups of risk takers assume their respective responsibilities for risk management.

The Board of Directors, representing the interests of shareholders, is the highest decision making authority of the Bank and has the ultimate responsibility for risk management. The Board, with the assistance of its committees, has the primary responsibility for the determination of risk management strategies and for ensuring that the Group has an effective risk management system to implement these risk management strategies. Risk Management Committee ("RC"), a standing committee established by the Board of Directors, is responsible for overseeing the Group's various types of risks, reviewing and approving high level risk related policies and overseeing their implementation, reviewing significant or high risk exposures or transactions and exercising its power of veto if it believes that the transaction shall not proceed. Audit Committee ("AC") assists the Board in fulfilling its role on overseeing internal control system.

To achieve the Group's risk management goals, the Group has established a centralised risk management structure that involves the following elements:

- a corporate governance structure to provide active oversight and participation by the Board of Directors, committees and senior management;
- reporting lines that are independent of the Group's Business Units;
- uniform risk management policies, procedures and limits by which the Group identifies, measures, monitors and controls inherent risks;
- improved risk measurement, monitoring and management information systems to support business activities and risk management; and
- clearly defined risk management responsibilities and accountability.

The Group faces the same types of inherent business risks and adopts consistent risk management strategies and policies as its immediate holding company, Bank of China (Hong Kong) Limited ("BOCHK"). The Group executes its risk management strategy independently and functionally reports to BOCHK on a regular basis.

Management's Discussion and Analysis (continued)

Risk Management (continued)

Reputation Risk Management

Reputation risk is the risk that negative publicity regarding the Group's business practices, whether genuine or not, will cause a potential decline in the customer base or lead to costly litigation or revenue erosion. Reputation risk is inherent in every aspect of business operation and covers a wide spectrum of issues.

In order to mitigate reputation risk, the Group has formulated and duly followed its Reputation Risk Management Policy. The policy aims to prevent and manage reputation risk proactively at an early stage when an incident occurs. The system entails continuous monitoring of external reputation risk incidents and published failures of risk incidents in the financial industry.

Legal and Compliance Risk Management

Legal risk is the risk that unenforceable contracts, lawsuits or adverse judgments may disrupt or otherwise negatively affect the operation or financial condition of the Group. Compliance risk is the risk of penalty arising from any failure to comply with relevant regulations governing the conduct of businesses in specific countries. By establishing and maintaining appropriate policies and procedures, the Compliance Section is responsible for proactively identifying and managing these risks.

Strategic Risk Management

Strategic risk generally refers to the risks that may induce immediate or future negative impact on the financial and market positions of the Group because of poor strategic decisions, improper implementation of strategies and lack of response to the market. The Group has developed a Strategic Risk Management Policy that clearly defines the management and oversight of such risks.

Management’s Discussion and Analysis (continued)

Risk Management (continued)

Credit Risk Management

Credit risk is the risk that a customer or counterparty will be unable to or unwilling to meet a commitment it has entered into. Credit Risk Management Division (“CMD”) provides centralised management of credit risk within the Group. Different credit approval and control procedures are adopted according to the level of risk associated with the customer or transaction. Corporate credit applications and retail credit transactions, including residential mortgage loans and personal loans are independently reviewed and objectively assessed by risk management units.

The Group’s internal loan grading system divides loans into 5 categories with reference to HKMA’s guidelines. CMD provides regular credit management information reports and ad hoc reports to members of Executive Committee (“EC”), RC, AC and Board of Directors.

Market Risk Management

Market risk is the risk of loss that results form movements in the market rates and prices. The Group’s market risk arises from customer-related business. The Group’s market risk in trading book arises from customer-related business. The risk includes potential losses arising from changes in foreign exchange and interest rates as well as equities and commodities prices. On the other hand, the major market risk in banking book arises from the group’s investment portfolio. The risk includes potential losses arising from changes in market parameters such as credit, liquidity, and interest rate risk. These positions are subject to monthly mark-to-market valuation.

Market risk is managed within the risk limits approved by the RC. The overall risk limits are divided into sub-limits by reference to different risk factors, including interest rate, foreign exchange rate, commodity price and equity price. CMD, Finance Division and Settlement Section are responsible for the regularly oversight of the Group’s market risk to ensure that overall and individual market risks are within the Group’s risk tolerance. Risk exposures are monitored on a regular basis to ensure that they are within established risk limits.

The Group has met the “de minimis” criteria set out in the Maintenance of Adequate Capital Against Market Risk guideline issued by the HKMA. As a result, the Group considers that the market risk arising from its trading book is not material and no further qualitative or quantitative disclosure is made of market risk in these accounts.

Management's Discussion and Analysis (continued)

Risk Management (continued)

Interest Rate Risk Management

The Group's interest rate risk exposures are mainly structural. The major types of interest rate risk from structural positions are:

repricing risk	–	mismatches in the maturity or repricing periods of assets and liabilities
basis risk	–	different pricing basis for different transactions so that yield on assets and cost of liabilities may change by different amounts within the same repricing period

The Group's Asset and Liability Management Committee ("ALCO") maintains oversight of interest rate risk and RC sanctions the interest rate risk management policies formulated by ALCO. The interest rate risk is identified and measured on a regular basis. The Treasury Division manages the interest rate risk according to the established policies. The Finance Division closely monitors the related risks and the results are reported to RC and ALCO regularly.

Gap analysis is one of the tools used to measure the Group's exposure to repricing risk. This provides the Group with a static view of the maturity and repricing characteristics of its balance sheet positions. The Group uses interest rate derivatives to hedge its interest rate exposures and in most cases, plain vanilla interest rate swaps are used.

Sensitivities of earnings and economic value to interest rate changes (Earnings at Risk and Economic Value at Risk) are assessed through hypothetical interest rate shock of 200 basis points across the yield curve on both sides. Earnings at Risk and Economic Value at Risk are controlled respectively within an approved percentage of the projected net interest income for the year and the latest capital base as sanctioned by RC. The results are reported to ALCO and RC on a regular basis.

The impact of basis risk is gauged by the projected change in net interest income under scenarios of imperfect correlation in the adjustment of the rates earned and paid on different instruments. Ratios of assets to liabilities with similar pricing basis are established to monitor such risk.

Management's Discussion and Analysis (continued)

Risk Management (continued)

Liquidity Risk Management

The aim of liquidity management is to enable the Group, even under adverse market conditions, to meet all its maturing repayment obligations on time and to fund all of its asset growth and strategic opportunities without forced liquidation of its assets at short notice.

The Group funds its operations principally by accepting deposits from retail and corporate depositors. In addition, the Group may issue certificates of deposit to secure long-term funds. Funding may also be secured through adjusting the asset mix in the Group's investment portfolio. The Group uses the majority of funds raised to extend loans, to purchase debt securities or to conduct interbank placements.

The Group monitors the liquidity risks using cash flow analysis and by examining deposit stability, concentration risk, mismatch ratios, loan-to-deposit ratio and liquidity profile of the investment portfolio. The primary objective of the Group's asset and liability management strategy is to achieve optimal return while ensuring adequate levels of liquidity and capital within an effective risk control framework and ALCO is responsible for establishing these policy directives (including the liquidity contingency plan), and RC sanctions the liquidity management policies. The Treasury Department manages the liquidity risk according to the established policies. The Finance Division monitors the Group's liquidity risks and reports to the management and ALCO regularly.

Operational Risk Management

Operational risk relates to the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. Strategic Planning and Control Department ("SCD") oversees the entire operational risk management framework of the Group.

The Group has put in place an effective internal control process which requires the establishment of detailed policies and control procedures for all the key activities. Proper segregation of duties and independent authorisation are the fundamental principles followed by the Group. Business line management is responsible for managing and reporting operational risks specific to their business units by identifying, assessing and controlling the risks inherent in their business processes, activities and products. These are followed by periodic monitoring and ongoing review of changes by SCD. SCD formulates corporate-level policies and procedures concerning operational risk management which are approved by RC. SCD evaluates the operational risk profile, records operational risk data and reports operational risk issues to RC and senior management.

Business continuity plans are in place to support business operations in the event of emergency or disaster. Adequate backup facilities are maintained and periodic drills are conducted. The Group also arranges insurance cover to reduce potential losses in respect of operational risk.

Management's Discussion and Analysis (continued)

Risk Management (continued)

Capital Management

The major objective of capital management is to maximise total shareholders' return while maintaining a capital adequacy position commensurate with the Group's overall risk profile. The Group periodically reviews its capital structure and adjusts the capital mix where appropriate to achieve the targeted weighted average cost of capital. ALCO monitors the Group's capital adequacy. The Group has complied with all the statutory capital standards for all the periods.

To comply with HKMA's requirements as stated in the Supervisory Policy Manual "Supervisory Review Process", the Group has implemented its internal capital adequacy assessment process ("ICAAP"). Using the statutory minimum capital adequacy ratio ("CAR"), 8%, as a starting point, extra capital (capital add-on) needed to cover the risks not captured under Pillar I was assessed. Scorecard methodology has been used to evaluate the Group's risk profile in order to assess the capital add-on and determine the minimum CAR. An Operating CAR Range has also been established which incorporates the need for future business growth and efficiency of capital utilisation.

Stress Testing

The Group supplements the analysis of various types of risks with stress testing. Stress testing is a risk management tool for estimating the Group's risk exposures under stressed conditions arising from extreme but plausible market or macroeconomic movements. These tests are conducted on a regular basis and ALCO monitors the results against limits approved by RC. Stress test results are also reported to the Board and RC regularly.

Report of the Directors

The Directors are pleased to present their report together with the audited consolidated financial statements of Chiyu Banking Corporation Limited (hereinafter referred to as the "Bank") and its subsidiaries (together with the Bank hereinafter referred to as the "Group") for the year ended 31 December 2009.

Principal Activities

The principal activities of the Group are the provision of banking and related financial services. An analysis of the Group's performance for the year by business segments is set out in Note 41 to the financial statements.

Results and Appropriations

The results of the Group for the year are set out in the consolidated income statement on page 20.

The Board declared a first interim dividend of HK$48.50 per ordinary share, totaling HK$145,500,000 on 31 December 2009.

Reserves

Details of movements in the reserves of the Group and the Bank are set out in the consolidated statement of changes in equity and statement of changes in equity on page 25 and 26 respectively.

Properties, Plant and Equipment

Details of movements in properties, plant and equipment of the Group and the Bank are set out in Note 28 to the financial statements.

Share Capital

Details of the share capital of the Group and the Bank are set out in the Note 34 to the financial statements.

Report of the Directors (continued)

Directors

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

Chairman	He Guangbei #
Vice Chairman	Ng Leung Sing #
	Ng Man Kung
Directors	Chan Yiu Fai
	Chen Zhong Xin #
	Cheung Wai Hing *
	Chiu Ming Wah #
	Liu Yanfen #
	Mao Xiaowei #
	Ouyang Jian#
	Tan Wan Chye #
	To Chi Wing #
	Woo Chia Wei *
	Yu Kwok Chun *

Non-executive Directors

* Independent non-executive Directors

In accordance with Article 99 of the Bank's Articles of Association, Mr. Chiu Ming Wah and Mr. Tan Wan Chye retire at the forthcoming annual general meeting and, being eligible, offer themselves for re-election.

Directors' Interests

Pursuant to written resolutions of all the shareholders of the Bank's intermediate holding company, BOC Hong Kong (Holdings) Limited ("BOCHKHL"), passed on 10 July 2002, BOCHKHL has approved and adopted two share option schemes, namely, the Share Option Scheme and the Sharesave Plan. No options have been granted by BOCHKHL pursuant to the Share Option Scheme or the Sharesave Plan during the year.

On 5 July 2002, Mr. He Guangbei, Mr. Ng Leung Sing, Mr. Ng Man Kung, Mr. Chiu Ming Wah, Mr. Mao Xiaowei, Mr. Chan Yiu Fai and Mr. To Chi Wing were granted option by BOC Hong Kong (BVI) Limited ("BOC (BVI)"), the immediate holding company of BOCHKHL, pursuant to a Pre-listing Share Option Scheme to purchase from BOC (BVI) existing issued shares of BOCHKHL at a price of HK$8.5 per share. These options have a vesting period of four years from 25 July 2002 with a valid exercise period of ten years. Messrs. Ng Man Kung and Chan Yiu Fai exercised the options to purchase an aggregate of 723,000 shares of BOCHKHL during the year.

Report of the Directors (continued)

Directors' Interests (continued)

Save as disclosed above, at no time during the year was the Bank, its subsidiaries, its fellow subsidiaries or its holding company a party to any arrangements to enable the directors to acquire benefits by means of the acquisition of shares in, or debentures of the Bank or at any other body corporate.

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

Management Contracts

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

Compliance with the Banking (Disclosure) Rules

The financial statements for the year ended 31 December 2009 comply with the requirements set out in the Banking (Disclosure) Rules under the Banking Ordinance.

Auditor

The financial statements have been audited by PricewaterhouseCoopers. A resolution for their re-appointment as auditor for the ensuing year will be proposed at the forthcoming annual general meeting.

On behalf of the Board

HE Guangbei

Chairman

Hong Kong, 10 March 2010

Corporate Governance

The Group has complied with the HKMA's guidelines set out in the Supervisory Policy Manual CG-1 "Corporate Governance of Locally Incorporated Authorised Institutions".

In order to focus on the strategic and material issues that have significant impact on the Group's operation, financial performance, risk management and long-term development, three committees have been established under the Board of Directors to oversee the major areas of the Group. The details of the committees are given below.

Executive Committee ("EC")

The EC has been delegated with authorities from the Board to handle matters which require the Board's review, but arise between board meetings. Its responsibilities include:

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

The members of EC are Mr. Ng Man Kung (Chairman), Mr. Chan Yiu Fai and Mr. To Chi Wing. All are Directors of the Bank.

Audit Committee ("AC")

The AC assists the Board in overseeing the auditing activities of the Group and monitoring compliance with approved policies and procedures, so that the effectiveness of financial reporting process and internal control systems of the Group can be assured. Its responsibilities include:

- reviewing and monitoring the effectiveness of the internal control systems, the controls over financial risks and the procedures of financial reporting and auditing;
- assessing independently the effectiveness and efficiency of financial reporting system and its controlling mechanism, and the sufficiency of operating policies and system; and
- monitoring the operation of the Group to ensure the Group is running in compliance with the relevant rules and regulations.

The members of AC are Mr. Chiu Ming Wah (Chairman), Mr. Cheung Wai Hing , Ms. Liu Yanfen, Mr. Tan Wan Chye and Mr. Woo Chia Wei. All are non-executive Directors of the Bank.

Risk Management Committee ("RC")

The RC assists the Board in overseeing the risk management of the Group, formulating the Group's risk management strategies, policies and procedures, and monitoring the implementation of those strategies, policies and procedures. Its responsibilities include:

- assisting the Board to measure and monitor the risk exposures of the Group;
- recommending appropriate risk management strategies to the Board; and
- formulating risk management related policies such as risk management policies and authorities and duties delegation policies in accordance with the requirements set by the Board.

The members of the RC are Mr. Mao Xiaowei (Chairman), Mr. Ng Leung Sing, Mr. Ng Man Kung, Mr. To Chi Wing and Mr. Yu Kwok Chun. All are Directors of the Bank.

Independent Auditor's Report
To the shareholders of Chiyu Banking Corporation Limited

(incorporated in Hong Kong with limited liability)

We have audited the consolidated financial statements of Chiyu Banking Corporation Limited (the "Bank") and its subsidiaries (together, the "Group") set out on pages 20 to 151, which comprise the consolidated and company balance sheets as at 31 December 2009, and the consolidated income statement, the consolidated and company statements of comprehensive income, the consolidated and company statements of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility for the financial statements

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

Auditor's responsibility

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

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

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

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

Independent Auditor's Report (continued)

Opinion

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

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 10 March 2010

Consolidated Income Statement

For the year ended 31 December	Notes	2009	2008
		HK$'000	HK$'000
Interest income		**776,104**	1,316,490
Interest expense		**(129,003)**	(489,219)
Net interest income	5	**647,101**	827,271
Fees and commission income		**303,012**	293,317
Fees and commission expenses		**(44,274)**	(47,692)
Net fees and commission income	6	**258,738**	245,625
Net trading income	7	**35,913**	55,158
Net (loss)/gain on financial instruments designated at fair value through profit or loss		**(5,098)**	9,031
Net gain on investments in securities	8	**-**	131
Other operating income	9	**8,272**	7,828
Net operating income before impairment allowances		**944,926**	1,145,044
Net reversal/(charge) of impairment allowances	10	**23,546**	(13,088)
Net operating income		**968,472**	1,131,956
Operating expenses	11	**(476,935)**	(419,780)
Operating profit		**491,537**	712,176
Net gain from disposal of/fair value adjustments on investment properties	12	**17,740**	2,100
Net loss from disposal of properties, plant and equipment	13	**(1)**	(9)
Profit before taxation		**509,276**	714,267
Taxation	14	**(88,096)**	(123,084)
Profit for the year		**421,180**	591,183
Dividends	16	**145,500**	1,179,000

The notes on pages 28 to 151 are an integral part of these financial statements.

Consolidated Statement of Comprehensive Income

	Notes	**2009**	2008
		HK$'000	HK$'000
Profit for the year		**421,180**	591,183
Net change in fair value of available-for-sale securities		**2,053**	12,187
Revaluation of premises		**82,199**	30,741
Currency translation difference		**386**	1,888
Net deferred tax on items taken directly to equity		**(9,750)**	(2,583)
Other comprehensive income for the year, net of tax		**74,888**	42,233
Total comprehensive income for the year		**496,068**	633,416
Total comprehensive income attributable to:			
Equity holders of the Bank		**496,068**	633,416

The notes on pages 28 to 151 are an integral part of these financial statements.

Statement of Comprehensive Income

	Notes	**2009**	2008
		HK$'000	HK$'000
Profit for the year		**418,553**	587,198
Net change in fair value of available-for-sale securities		**(1,954)**	1,679
Revaluation of premises		**81,848**	29,391
Currency translation difference		**386**	1,888
Net deferred tax on items taken directly to equity		**(9,698)**	(3,668)
Other comprehensive income for the year, net of tax		**70,582**	29,290
Total comprehensive income for the year		**489,135**	616,488

The notes on pages 28 to 151 are an integral part of these financial statements.

Consolidated Balance Sheet

As at 31 December	Notes	**2009**	2008
		HK$'000	HK$'000
ASSETS			
Cash and balances with banks and other financial institutions	20	**7,987,577**	8,585,754
Placements with banks and other financial institutions maturing between one and twelve months		**5,525,376**	8,721,608
Financial assets designated at fair value through profit or loss	21	**793,116**	369,757
Derivative financial instruments	22	**349,936**	385,945
Advances and other accounts	23	**18,582,368**	15,908,861
Investment in securities	25	**5,064,237**	3,933,003
Investment properties	27	**78,800**	80,050
Properties, plant and equipment	28	**657,463**	584,477
Other assets	29	**905,996**	641,594
Total assets		**39,944,869**	39,211,049
LIABILITIES			
Deposits from and balances with banks and other financial institutions		**468,726**	1,072,082
Financial liabilities designated at fair value through profit or loss	30	**-**	768,509
Derivative financial instruments	22	**164,386**	208,845
Deposits from customers	31	**33,817,255**	31,449,797
Other accounts and provisions	32	**1,321,136**	1,896,809
Current tax liabilities		**4,926**	22,067
Deferred tax liabilities	33	**78,315**	53,383
Total liabilities		**35,854,744**	35,471,492
EQUITY			
Share capital	34	**300,000**	300,000
Reserves	35	**3,790,125**	3,439,557
Total equity		**4,090,125**	3,739,557
Total liabilities and equity		**39,944,869**	39,211,049

The notes on pages 28 to 151 are an integral part of these financial statements.

Approved by the Board of Directors on 10 March 2010 and signed on behalf of the Board by:

HE Guangbei

Director

NG Man Kung

Director

Balance Sheet

As at 31 December	Notes	2009	2008
		HK$'000	HK$'000
ASSETS			
Cash and balances with banks and other financial institutions	20	**7,987,577**	8,585,754
Placements with banks and other financial institutions maturing between one and twelve months		**5,525,376**	8,721,608
Financial assets designated at fair value through profit or loss	21	**793,116**	369,757
Derivative financial instruments	22	**349,936**	385,945
Advances and other accounts	23	**18,582,368**	15,908,861
Investment in securities	25	**5,021,059**	3,893,832
Investment in subsidiaries	26	**3,913**	3,913
Amount due from subsidiaries	26	**20,351**	20,340
Investment properties	27	**78,800**	80,050
Properties, plant and equipment	28	**651,063**	578,277
Other assets	29	**905,996**	641,594
Total assets		**39,919,555**	39,189,931
LIABILITIES			
Deposits and balances of banks and other financial institutions		**468,726**	1,072,082
Financial liabilities designated at fair value through profit or loss	30	**-**	768,509
Derivative financial instruments	22	**164,386**	208,845
Deposits from customers	31	**33,851,546**	31,483,825
Amount due to subsidiaries	26	**33,197**	30,888
Other accounts and provisions	32	**1,320,863**	1,896,335
Current tax liabilities		**4,926**	22,067
Deferred tax liabilities	33	**77,894**	52,998
Total liabilities		**35,921,538**	35,535,549
EQUITY			
Share capital	34	**300,000**	300,000
Reserves	35	**3,698,017**	3,354,382
Total equity		**3,998,017**	3,654,382
Total liabilities and equity		**39,919,555**	39,189,931

The notes on pages 28 to 151 are an integral part of these financial statements.

Approved by the Board of Directors on 10 March 2010 and signed on behalf of the Board by:

HE Guangbei

Director

NG Man Kung

Director

Consolidated Statement of Changes in Equity

	Attributable to equity holders of the Group						
	Share capital	Premises revaluation reserve	Reserve for fair value changes of available-for-sale securities	Regulatory reserve*	Translation reserve	Retained earnings	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
At 1 January 2008	300,000	317,579	8,157	172,274	-	3,487,131	4,285,141
Comprehensive income	-	26,880	13,465	-	1,888	591,183	633,416
2008 first interim dividend paid	-	-	-	-	-	(678,000)	(678,000)
2008 second interim dividend declared	-	-	-	-	-	(501,000)	(501,000)
Transfer from retained earnings	-	-	-	19,221	-	(19,221)	-
At 31 December 2008	300,000	344,459	21,622	191,495	1,888	2,880,093	3,739,557

	Attributable to equity holders of the Group						
	Share capital	Premises revaluation reserve	Reserve for fair value changes of available-for-sale securities	Regulatory reserve*	Translation reserve	Retained earnings	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
At 1 January 2009	**300,000**	**344,459**	**21,622**	**191,495**	**1,888**	**2,880,093**	**3,739,557**
Comprehensive income	**-**	**72,120**	**2,382**	**-**	**386**	**421,180**	**496,068**
Release upon disposal of premises	**-**	**(8,810)**	**-**	**-**	**-**	**8,810**	**-**
2009 first interim dividend declared	**-**	**-**	**-**	**-**	**-**	**(145,500)**	**(145,500)**
Transfer to retained earnings	**-**	**-**	**-**	**(42,238)**	**-**	**42,238**	**-**
At 31 December 2009	**300,000**	**407,769**	**24,004**	**149,257**	**2,274**	**3,206,821**	**4,090,125**

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

The notes on pages 28 to 151 are an integral part of these financial statements.

Statement of Changes in Equity

	Attributable to equity holders of the Bank						
	Share capital	Premises revaluation reserve	Reserve for fair value changes of available-for-sale securities	Regulatory reserve*	Translation reserve	Retained earnings	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
At 1 January 2008	300,000	315,828	1,030	172,274	-	3,427,762	4,216,894
Comprehensive income	-	25,732	1,670	-	1,888	587,198	616,488
2008 first interim dividend paid	-	-	-	-	-	(678,000)	(678,000)
2008 second interim dividend delcared	-	-	-	-	-	(501,000)	(501,000)
Transfer from retained earnings	-	-	-	19,221	-	(19,221)	-
At 31 December 2008	300,000	341,560	2,700	191,495	1,888	2,816,739	3,654,382

	Attributable to equity holders of the Bank						
	Share capital	Premises revaluation reserve	Reserve for fair value changes of available-for-sale securities	Regulatory reserve*	Translation reserve	Retained earnings	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
At 1 January 2009	**300,000**	**341,560**	**2,700**	**191,495**	**1,888**	**2,816,739**	**3,654,382**
Comprehensive income	**-**	**71,821**	**(1,625)**	**-**	**386**	**418,553**	**489,135**
Release upon disposal of premises	**-**	**(8,810)**	**-**	**-**	**-**	**8,810**	**-**
2009 first interim dividend declared	**-**	**-**	**-**	**-**	**-**	**(145,500)**	**(145,500)**
Transfer to retained earnings	**-**	**-**	**-**	**(42,238)**	**-**	**42,238**	**-**
At 31 December 2009	**300,000**	**404,571**	**1,075**	**149,257**	**2,274**	**3,140,840**	**3,998,017**

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

The notes on pages 28 to 151 are an integral part of these financial statements.

Consolidated Cash Flow Statement

For the year ended 31 December	Notes	2009	2008
		HK$'000	HK$'000
Cash flows from operating activities			
Operating cash (outflow)/ inflow before taxation	36(a)	**(3,824,855)**	3,349,114
Hong Kong profits tax paid		**(100,787)**	(170,458)
Overseas profits tax paid		**(20,677)**	(25,576)
Net cash (outflow)/inflow from operating activities		**(3,946,319)**	3,153,080
Cash flows from investing activities			
Purchase of properties, plant and equipment		**(4,919)**	(9,600)
Proceeds from disposal of investment properties		**18,990**	-
Proceeds from disposal of other assets		**49**	-
Net cash inflow/(outflow) from investing activities		**14,120**	(9,600)
Cash flows from financing activities			
Dividends paid to equity holders of the Bank		**(501,000)**	(948,000)
Net cash outflow from financing activities		**(501,000)**	(948,000)
(Decrease)/increase in cash and cash equivalents		**(4,433,199)**	2,195,480
Cash and cash equivalents at 1 January		**14,845,037**	12,649,557
Cash and cash equivalents at 31 December	36(b)	**10,411,838**	14,845,037

The notes on pages 28 to 151 are an integral part of these financial statements.

Notes to the Financial Statements

1. Principal activities

The Group is principally engaged in the provision of banking and related financial services in Hong Kong.

The Bank is a limited liability company incorporated in Hong Kong. The address of its registered office is No.78 Des Vouex Road, Central, Hong Kong.

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 Hong Kong Financial Reporting Standards (HKFRSs is a collective term which includes all applicable individual Hong Kong Financial Reporting Standards, HKASs and Interpretations) issued by the HKICPA and the requirements of the Hong Kong Companies Ordinance.

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

The preparation of financial statements in conformity with HKFRSs requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group’s accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 3.

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.1 Basis of preparation (continued)

(a) Standards, amendments and interpretations already effective for accounting periods beginning on 1 January 2009

Standard/ Interpretation	Content	Applicable for financial years beginning on/ after	Relevant to the Group
HKAS 1 (Revised)	Presentation of Financial Statements	1 January 2009	Yes
HKAS 23 (Revised)	Borrowing Costs	1 January 2009	No
HKAS 32 and HKAS 1 (Amendments)	Puttable Financial Instruments and Obligations Arising on Liquidation	1 January 2009	No
HKFRS 1 and HKAS 27 (Amendments)	Cost of an investment in a Subsidiary, Jointly Controlled Entity or Associate	1 January 2009	No
HKFRS 2 (Amendment)	Share based payments - Vesting Conditions and Cancellations	1 January 2009	No
HKFRS 7 (Amendment)	Improving Disclosures about Financial Instruments	1 January 2009	Yes
HKFRS 8	Operating Segments	1 January 2009	Yes
HK(IFRIC)-Int 13	Customer Loyalty Programmes	1 July 2008	Yes
HK(IFRIC)-Int 15	Agreements for the Construction of Real Estate	1 January 2009	No
HK(IFRIC)-Int 16	Hedges of a Net Investment in a Foreign Operation	1 October 2008	No

- HKAS 1 Presentation of Financial Statements (Revised)

The revised standard prohibits the presentation of items of income and expenses (that is 'non-owner changes in equity') in the statement of changes in equity, requiring 'non-owner changes in equity' to be presented separately from owner changes in equity. All 'non-owner changes in equity' are required to be shown in a performance statement.

The Group has elected to present its performance in two separate statements: an income statement and a statement of comprehensive income. The financial information has been prepared under the revised presentation requirements. The adoption of this revised standard affects the presentation of the Group's financial statements.

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.1 Basis of preparation (continued)

(a) Standards, amendments and interpretations already effective for accounting periods beginning on 1 January 2009 (continued)

- HKFRS 7 Financial Instruments: Disclosures (Amendment)

The amendment increases the disclosure requirements about fair value measurement and reinforces existing principles for disclosure about liquidity risk. The amendment introduces a three-level hierarchy for fair value measurement disclosures and requires some specific quantitative disclosures for financial instruments on the lowest level in the hierarchy. It is not required to provide comparative disclosures in the first year of application. The adoption of the amendment does not have an impact on the financial position or the comprehensive income of the Group.

- HKFRS 8 Operating Segments

HKFRS 8 replaces HKAS 14 'Segment Reporting'. It requires a 'management approach' under which segment information, that reflects the operating result of segments reviewed regularly by the management for operation decisions making, resources allocation and performance assessment, is presented on the same basis and in the same manner as that used for internal reporting to the management. The adoption of HKFRS 8 makes no change in the number of reportable segments presented.

- HK(IFRIC)-Int 13 Customer Loyalty Programmes

HK(IFRIC)-Int 13 clarifies that when an entity provides customers with incentives to buy goods or services under a customer loyalty programme (for example, customers accumulate loyalty points to redeem free or discounted products or service), the fair value of the consideration received or receivable in respect of the initial sale shall be allocated between the award credits and the other components of the sale or service. As the interpretation does not have a significant impact on the Group's results of operations and financial position, no restatement of prior year figure has been made.

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards, amendments and interpretations issued that are not yet effective and have not been early adopted by the Group in 2009

The following standards, amendments and interpretations have been issued and are mandatory for accounting periods beginning on or after 1 July 2009:

Standard/ Interpretation	Content	Applicable for financial years beginning on/ after	Relevant to the Group
HKAS 27 (Revised)	Consolidated and Separate Financial Statements	1 July 2009	Yes
HKAS 32 (Amendment)	Classification of Rights Issues	1 February 2010	No
HKAS 39 (Amendment)	Financial Instruments: Recognition and Measurement - Eligible Hedged Items	1 July 2009	No
HKFRS 1 (Revised)	First-time Adoption of HKFRS	1 July 2009	No
HKFRS 2 (Amendment)	Group Cash-settled Share-based Payment Transactions	1 January 2010	No
HKFRS 3 (Revised)	Business Combinations	1 July 2009	Yes
HKFRS 9	Financial Instruments Part 1: Classification and Measurement	1 January 2013	Yes
HK(IFRIC)-Int 17	Distributions of Non-cash Assets to Owners	1 July 2009	No
HK(IFRIC)-Int 18	Transfers of assets from customers	1 July 2009	No
HK(IFRIC)-Int 19	Extinguishing Financial Liabilities with Equity Instruments	1 July 2010	No

- HKAS 27 Consolidated and Separate Financial Statements (Revised)

  The revised standard requires changes in a parent's ownership interest in a subsidiary that do not result in the loss of control are accounted for within other comprehensive income. The standard also specifies the accounting when control is lost. Any remaining interest in the entity is re-measured to fair value and a gain or loss is recognised in income statement. The Group will apply HKAS 27 (Revised) prospectively from 1 January 2010.

- HKFRS 3 Business Combinations (Revised)

  The revised standard continues to apply the acquisition method to business combinations, with some significant changes. For example, all payments to purchase a business are to be recorded at fair value at the acquisition date, with contingent payments classified as debt subsequently re-measured through the consolidated income statement. All acquisition-related costs should be expensed. The Group will apply HKFRS 3 (Revised) prospectively to all business combinations (other than common control combination) acquired on or after 1 January 2010.

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards, amendments and interpretations issued that are not yet effective and have not been early adopted by the Group in 2009 (continued)

- HKFRS 9 Financial Instruments Part 1: Classification and Measurement

  HKFRS 9 was issued in November 2009 and replaces those parts of HKAS 39 relating to the classification and measurement of financial assets. Key features are as follows:

  Financial assets are required to be classified into one of the below two measurement categories: those to be measured subsequently at fair value or those to be measured subsequently at amortised cost. Classification is to be made on transition, and subsequently on initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument.

  A financial instrument is subsequently measured at amortised cost only if it is a debt instrument and both the objective of the entity's business model is to hold the asset to collect the contractual cash flows, and the asset's contractual cash flows represent only unleveraged payments of principal and interest are met. All other debt instruments are to be measured at fair value through profit or loss.

  All equity instruments are to be measured subsequently at fair value. Equity instrument that are held for trading will be measured at fair value through profit or loss. For all other equity investments, an irrevocable election can be made on a share-by-share basis at initial recognition, to recognise unrealised and realised fair value gains and losses through other comprehensive income rather than income statement. Once elected to be recognized through other comprehensive income, there will be no recycling of fair value gains and losses to income statement. Dividends are to be presented in income statement, as long as they represent a return on investment.

  While adoption of HKFRS 9 is mandatory from 1 January 2013, earlier adoption is permitted. The Group is considering the impact of the standard on the consolidated financial statements and the timing of its application.

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.1 Basis of preparation (continued)

(c) Improvements to HKFRS

'Improvements to HKFRS' contains numerous amendments to HKFRS which the HKICPA consider non-urgent but necessary. It comprises amendments that result in accounting changes for presentation, recognition or measurement purpose as well as terminology or editorial amendments related to a variety of individual HKFRS. Most of the amendments are effective for annual periods beginning on or after 1 January 2009 or 1 January 2010 respectively, with earlier application permitted. No material changes to accounting policies are expected as a result of these amendments.

(d) Standard issued that is not yet effective but has been early adopted by the Group in 2009

The following revised standard has been early partially adopted by the Group retrospectively.

Standard/ Interpretation	Content	Applicable for Financial years beginning on/ after	Relevant to the Group
HKAS 24 (Revised)	Related Party Disclosures	1 January 2011	Yes

- HKAS 24 Related Party Disclosures (Revised)

  The revised standard was issued in November 2009. In 2009, the Group partially adopted the revised HKAS 24 –Related Party Disclosures as permitted in its transition provisions. The Group applied the partial exemption in HKAS 24 (Revised) regarding disclosure requirements for government-related entities. According to the previous version of HKAS 24, the Group was required to disclose transactions with the government and other government related-entities. The amendment introduces an exemption from certain disclosure requirements of HKAS 24 for transactions between government-related entities and the government, and all other government-related entities. The Group has early adopted the partial exemption and has applied this retrospectively. The early application does not have any effect on the Group's operating results, financial position or comprehensive income but has an impact on disclosure. The related party disclosures have been changed accordingly.

  The remainder of the revised standard amending the definition of related parties will be applied in the annual period beginning 1 January 2011 and will not have any impact on the Group.

Except for the early partial adoption of HKAS24 (Revised), the Group has not early adopted other new or amended accounting standards or interpretations in 2009.

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.2 Consolidation

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

Subsidiaries

Subsidiaries are all entities (including special purpose entities) over which the Group controls the composition of the Board of Directors, controls more than half of the voting power, holds more than half of the issued capital or by any other means that entitle the Group to govern the financial and operating policies of the entities. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group not under common control. The cost of such an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed as of the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets (including intangible assets) acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values as of the acquisition date, irrespective of the extent of any non-controlling interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the Group's share of the identifiable net assets of the subsidiary acquired, the difference is recognised directly in the consolidated income statement.

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

In the Bank's balance sheet the investments in subsidiaries are stated at cost less allowance for impairment losses. The results of subsidiaries are accounted for by the Bank on the basis of dividends received and receivable.

The gain or loss on the disposal of a subsidiary represents the difference between: (a) the proceeds of the sale and, (b) the Group's share of its net assets including goodwill on acquisition net of any accumulated impairment loss and any related accumulated foreign currency translation difference.

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.3 Segmental reporting

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

2.4 Foreign currency translation

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

Foreign exchange gains and losses resulting from the settlement of foreign currency transactions using the exchange rates prevailing at the dates of the transactions and monetary assets and liabilities denominated in foreign currencies translated at the rate of exchange at the balance sheet date are recognised directly in the income statement.

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

Translation differences on non-monetary items, such as equities held at fair value through profit or loss, are reported as part of the fair value gain or loss. Translation differences on non-monetary financial assets such as equities classified as available-for-sale are included in the available-for-sale reserve in equity.

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.4 Foreign currency translation (continued)

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

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

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

2.5 Derivative financial instruments

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

The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e., the fair value of the consideration given or received).

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

Derivatives are categorised as held for trading and changes in their fair value are recognised immediately in the income statement unless they are designated as hedges and are effective hedging instruments, then they are subject to measurement under the hedge accounting requirements.

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.6 Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

2.7 Interest income and expense and fees and commission income and expense

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

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

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.7 Interest income and expense and fees and commission income and expense (continued)

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

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

2.8 Financial assets

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

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

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

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

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.8 Financial assets (continued)

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

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

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

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

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

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

Gains and losses from changes in the fair value of such assets (excluding the interest component) are reported in net trading income or net gain/loss on financial instruments designated at fair value through profit or loss. The interest component is reported as part of interest income. Dividends on equity instruments of this category are recognised in the consolidated income statement when the Group's right to receive payment is established.

(2) Loans and receivables

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

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.8 Financial assets (continued)

(3) Held-to-maturity

Financial assets classified as held-to-maturity are those traded in active markets, with fixed or determinable payments and fixed maturities that the Group's management has both the positive intention and the ability to hold to maturity. Were the Group to sell other than an insignificant amount of held-to-maturity assets, the entire category would be tainted and reclassified as available-for-sale. They are initially recorded at fair value plus any directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest method less allowances for impairment losses.

(4) Available-for-sale

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

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

2.9 Financial liabilities

The Group classifies its financial liabilities under the following categories: trading liabilities, financial liabilities designated at fair value through profit or loss, deposits, debt securities in issue, subordinated liabilities, and other liabilities. All financial liabilities are classified at inception and recognised initially at fair value.

(1) Trading liabilities

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

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.9 Financial liabilities (continued)

(2) Financial liabilities designated at fair value through profit or loss

A financial liability can be designated at fair value through profit or loss if it is so designated at inception. Financial liabilities so designated include certain certificates of deposit issued and certain deposits received from customers that are embedded with derivatives. A financial liability is typically so designated if it meets the following criteria:

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

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

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

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

(3) Deposits and other liabilities

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

2.10 Recognition and de-recognition of financial instruments

Purchases and sales of financial assets at fair value through profit or loss, available-for-sale and held-to-maturity are recognised on the trade date, the date on which the Group purchases or sells the assets. Loans and receivables (except investment securities without an active market) are recognised when cash is advanced to the borrowers. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership.

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.10 Recognition and de-recognition of financial instruments (continued)

Trading liabilities, financial liabilities designated at fair value through profit or loss and debt securities in issue are recognised on the trade date. Deposits other than trading liabilities are recognised when money is received from customers, other liabilities are recognised when such obligations arise. Financial liabilities are de-recognised from the balance sheet when and only when the obligation specified in the contract is discharged, cancelled or expired. If the Group purchases its own debt, it is removed from the balance sheet, and the difference between the carrying amount of a liability and the consideration paid is included in net trading income.

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

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

2.11 Determination of fair value of financial instruments

The fair values of financial assets and financial liabilities that are quoted in active markets are based on current bid prices and current ask prices respectively. If the market for financial assets and financial liabilities is not active (such as unlisted securities), the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.12 Impairment of financial assets

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

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

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

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

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

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

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

- adverse changes in the payment status of borrowers in the group; or
- national or local economic conditions that correlate with defaults on the assets in the group.

(1) Assets carried at amortised cost

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

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.12 Impairment of financial assets (continued)

(1) Assets carried at amortised cost (continued)

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

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

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

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

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

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.12 Impairment of financial assets (continued)

(1) Assets carried at amortised cost (continued)

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

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

(2) Assets classified as available-for-sale

If evidence of impairment exists for available-for-sale financial assets, the cumulative losses, measured as the difference between the acquisition cost or amortised cost and the current fair value, less any impairment loss on that financial asset previously recognised in the income statement, is removed from equity and recognised in the income statement. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed through the income statement. With respect to equity instruments, further fair value changes are recognised in the reserve for fair value change of available-for-sale securities through other comprehensive income.

2.13 Impairment of investment in subsidiaries and non-financial assets

Assets that have an indefinite useful life or are not yet available for use are not subject to amortisation, but are tested annually for impairment. 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 impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units). Assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.14 Financial guarantee contracts

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

Financial guarantees are initially recognised as financial liabilities and reported under “Other accounts and provisions” in the financial statements at fair value on the date the guarantee was given. Subsequent to initial recognition, the Group’s liabilities under such guarantees are measured at the higher of (i) the amount determined in accordance with HKAS 37 Provisions, Contingent Liabilities and Contingent Assets and (ii) the amount initially recognised less, where appropriate, cumulative amortisation recognised over the life of the guarantee on a straight-line basis. Any changes in the liability relating to financial guarantees are taken to the income statement.

2.15 Premises, equipment, fixtures and fittings

Premises comprise primarily branches and offices. Premises are shown at fair value based on periodic, but at least annually, valuations by external independent valuers less subsequent depreciation. Any accumulated depreciation at the date of revaluation is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. In the intervening periods, the directors review the carrying amount of premises, by reference to the open market value of similar properties, and adjustments are made when there has been a material change. All equipment, fixtures and fittings are stated at historical cost less accumulated depreciation and impairment. Historical cost includes expenditures that are directly attributable to the acquisition and installation of the items.

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

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.15 Premises, equipment, fixtures and fittings (continued)

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

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

• Premises	Over the remaining period of lease
• Equipment, fixtures and fittings	3-15 years

The useful lives of assets are reviewed, and adjusted if appropriate, as of each balance sheet date.

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

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

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.16 Investment properties

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

Investment properties are recognised initially at cost, including related transaction costs. After initial recognition, investment properties are measured at fair value assessed by professional valuers on the basis of open market value. If this information is not available, alternative valuation methods are used such as recent prices on less active markets or discounted cash flow projections. These valuations are performed in accordance with the guidance issued by the International Valuation Standards Committee.

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

Any changes in fair value are reported directly in the income statement. Deferred income tax is provided on revaluation surpluses of investment properties in accordance with HK(SIC)-Int 21 "Income Taxes – Recovery of Revalued Non-Depreciable Assets" on HKAS 12 "Income Taxes".

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

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.17 Leases

(1) Operating leases

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

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

Where the Group is a lessor, the land and buildings subject to the operating lease are accounted for as investment properties. Rental income from operating leases is recognised on a straight-line basis over the lease term.

(2) Finance leases on properties

Where the land and buildings elements of leasehold properties held for own use can be split reliably at inception of the lease, leasehold land and land use rights are recognised as operating leases if they have indefinite economic lives. The up-front prepayments made or other costs incurred for acquiring the leasehold land and land use rights are expensed in the income statement on a straight-line basis over the period of the lease. Where there is impairment of the up-front prepayments, the impairment is expensed in the income statement immediately. Where the land and buildings cannot be split reliably at inception of the lease, the land and buildings elements will continue to be treated as finance leases and measured at fair value.

Separate measurements of the land and buildings elements are not required when the Group's interest in both land and buildings is classified as investment properties as if they are finance leases and are measured at fair value.

2.18 Cash and cash equivalents

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

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.19 Provisions

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

2.20 Employee benefits

(1) Retirement benefit costs

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

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

(2) Leave entitlements

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

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

(3) Bonus plans

The expected cost of bonus payments are recognised as a liability when the Group has a present legal or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made. Liabilities for bonus plans are expected to be settled within twelve months and are measured at the amounts expected to be paid when they are settled.

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.21 Current and deferred income taxes

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

Income tax payable on profits, based on the applicable tax law enacted or substantially enacted at the balance sheet date in each jurisdiction where the Company and the subsidiaries and associates operate and generate taxable income, is recognised as a current income tax expense in the period in which profits arise.

Deferred income tax is provided in full, using the balance sheet liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates and laws that have been enacted or substantially enacted by the balance sheet 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 asset impairment provisions, depreciation of property and equipment, revaluation of certain assets including available-for-sale securities and properties, and tax losses carried forward. However, the deferred income tax is not recognised if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss.

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

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

Notes to the Financial Statements (continued)

2. Summary of significant accounting policies (continued)

2.22 Repossessed assets

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

2.23 Fiduciary activities

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

2.24 Contingent liabilities and contingent assets

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

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

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

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

2.25 Related parties

For the purposes of these financial statements, a party is considered to be related to the Group if the Group has the ability, directly and indirectly through one or more intermediaries, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control. Related parties may be individuals or entities.

Notes to the Financial Statements (continued)

3. Critical accounting estimates and judgements in applying accounting policies

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 that are believed to be reasonable under the circumstances. Areas susceptible to changes in essential estimates and judgements, which affect the carrying amount of assets and liabilities, are set out below. The effect of changes to either the key assumptions or other estimation uncertainties will be presented below if it is practicable to determine. It is possible that actual results may require material adjustments to the estimates referred to below.

3.1 Impairment allowances on loans and advances

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

3.2 Impairment of held-to-maturity and available-for-sale investments

The Group reviews its held-to-maturity and available-for-sale investment portfolios to assess impairment at l east on a quarterly basis. In determining whether any of these investments is impaired, risk characteristics and performance such as external credit rating, market price etc will be assessed. The Group makes estimates on the default rate and loss severity of each investment with reference to market performance of the portfolios, current payment status of the issuers or performance of the underlying assets, or economic conditions that correlate with defaults on the collateralised assets.

Notes to the Financial Statements (continued)

3. Critical accounting estimates and judgements in applying accounting policies (continued)

3.3 Fair values of derivatives financial instruments

The fair values of derivatives financial instruments that are not quoted in active markets are determined by using valuation techniques. Valuation techniques used include discounted cash flows analysis and models with built-in functions available in externally acquired financial analysis or risk management systems widely used by the industry. To the extent practical, the models use only observable data.

3.4 Held-to-maturity investments

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

3.5 Provision

The Group uses judgement to assess whether the Group has a present legal or constructive obligation as a result of past events at each balance sheet date, and judgement is used to determine if it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and to determine a reliable estimate of the amount of the obligation.

On 22 July 2009, the Group agreed with the Securities and Futures Commission, the HKMA and fifteen other distributing banks to make an offer to eligible customers to repurchase their holdings in all outstanding Lehman Brothers minibonds ("Minibonds") subscribed through the Group ("the Repurchase Scheme").

In determining the Group's charge to the income statement in respect of the Minibonds, the Group took into account the estimated aggregate amount paid and payable under the Repurchase Scheme and the voluntary offer, the provision made prior to the date of the Repurchase Scheme and the amount recoverable from the Minibonds.

The amount recoverable from the Minibonds is uncertain and dependent on a number of factors including resolution of certain legal matters, which may result in a wide range of recovery outcomes. The Group has made an assessment of the amount recoverable taking into account such uncertainties. The final amount recovered by the Group could be different from the assessment and may result in a significant credit being recognised in the income statement in the period when it is realised.

Notes to the Financial Statements (continued)

4. Financial risk management

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

Financial risk management framework

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

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

The RC, a standing committee established by the Board of Directors, is responsible for overseeing the Group's various types of risks, reviewing and approving high-level risk-related policies and overseeing their implementation, reviewing significant or high risk exposures or transactions and exercising its power of veto if it considers that any transaction should not proceed.

The Chief Executive ("CE") is responsible for managing the Group's various types of risks, approving detailed risk management policies, and approving material risk exposures or transactions within his authority delegated by the Board of Directors. The Head of Strategic Planning and Control Department ("SCD") assists the CE in fulfilling his responsibilities for the day-to-day management of risks. The Head of SCD is responsible for initiating new risk management strategies, projects and measures that will enable the Group to better monitor and manage new risk issues or areas that may arise from time to time from new businesses, products and changes in the operating environment. He may also take appropriate initiatives in response to regulatory changes. The Head of SCD is also responsible for reviewing material risk exposures or transactions within his delegated authority and exercising his power of veto if he believes that any transaction should not proceed.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

Financial risk management framework (continued)

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

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

Product development

To ensure effective risk assessment and monitoring, the Group developed a comprehensive product development and management framework, which clearly defines the roles and responsibilities of all related units, and the proper risk assessment procedures for the product development process.

In accordance with the strategic objectives set by the Management, the respective product management units are responsible for formulating business and product development plans which are aligned with the Group's overall strategies. Credit Risk Management Division ("CMD"), Compliance Section, Audit Division and Finance Division etc. are accountable for risk assessment and review.

Apart from product development, the respective business units shall work closely with relevant risk evaluating departments to identify and assess all the related risks. Based on the consideration of segregation of duties, risk evaluating departments shall conduct independent review on risk management procedures and assessment results. Products can only be launched after the risk management procedures are fulfilled and endorsed by all risk evaluating departments.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk

Credit risk is the risk that a customer or counterparty will be unable to or unwilling to meet its obligation under a contract. It arises principally from lending, trade finance, treasury business, and covers inter-bank transactions, foreign exchange and derivative transactions as well as investments in bonds and securities.

Credit risk management framework

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

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

The Head of SCD is responsible for the management of credit risk and for the formulation of all credit policies and procedures. Various units of the Group have their respective credit risk management responsibilities. Business units act as the first line of defense while risk management units, which are independent from the business units, are responsible for the day-to-day management of credit risks. CMD has the primary responsibility for drafting, reviewing and updating credit risk management policies and procedures.

The Board of Directors delegates credit approval authority to the CE. The CE can further delegate to the subordinates within his limit authorised by the Board of Directors. The Group sets the limits of credit approval authority according to the transactions' nature, customers'/counterparties' creditworthiness, the level of transaction risk, and the size of the credit exposure.

Credit risk measurement and control

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

<u>Loans and advances</u>

Different credit approval and control procedures are adopted according to the level of risk associated with the customer, counterparty or transaction. Corporate and financial institution credit applications are independently reviewed, objectively assessed and monitored by risk management units and credit rating models/scorecards are used in the process of credit approval whenever they are applicable. A credit scoring system is used to process retail credit transactions, including residential mortgage loans and personal loans.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Credit risk measurement and control (continued)

Loans and advances (continued)

CMD provides regular credit management information reports and ad hoc reports to the Board of Management, RC and Board of Directors to facilitate their continuous monitoring of credit risk.

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

The Group's internal loan grading system divides loans into 5 categories with reference to HKMA's guidelines.

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

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

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

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

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

Debt securities and derivatives

For investment in debt securities, the external credit rating and assessment on credit quality of the underlying assets are used for managing the credit risk involved. Credit limits are established on a customer and security issuer basis. For derivatives, the Group sets customer limits to manage the credit risk involved and follows the same approval and control processes as loans and advances. On-going monitoring procedures are established.

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

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Collateral held as security and other credit enhancements

The valuation and management of collateral have been documented in the policy covering acceptance criteria, validity of collateral, loan-to-value ratio, haircut ratio, valuation and insurance, etc. The collateral is revalued on a regular basis, though the frequency and the method used varies with the type of collateral involved and the nature and the risk of the underlying credit. The Group has established a mechanism to update the value of its main type of collateral, real properties, with the use of public indices on a portfolio basis. Collateral is insured with the Group as the beneficiary. In the personal sector, the main types of collateral are real properties, cash deposits, securities and investment funds. In the commercial and industrial sector, the main types of collateral are real properties, securities, receivables, cash deposits and machinery.

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

As at 31 December 2009 and 2008, the Group did not hold any collateral permitted to sell or re-pledge in the absence of default by the borrower.

Credit exposures

Maximum exposures to credit risk before collateral held or other credit enhancements of the Group are summarised as follows:

	2009	2008
	HK$'000	HK$'000
Credit risk exposures relating to on-balance sheet assets are as follows:		
Balances with banks and other financial institutions	**7,987,577**	8,585,754
Placements with banks and other financial institutions maturing between 1 and 12 months	**5,525,376**	8,721,608
Financial assets designated at fair value through profit or loss		
- debt securities	**793,116**	369,757
Derivative financial instruments	**349,936**	385,945
Advances and other accounts	**18,582,368**	15,908,861
Investment in securities		
- debt securities - available-for-sale	**1,088,402**	287,385
- debt securities - held-to-maturity	**3,930,474**	3,526,676
- debt securities - loans and receivables	**9**	77,645
Other assets	**905,996**	641,594
Credit risk exposures relating to off-balance sheet items are as follows:		
Letters of guarantee issued	**1,487,757**	925,729
Loan commitment and other credit related liabilities	**3,697,393**	3,763,460
	44,348,404	43,194,414

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Credit exposures (continued)

The above tables represent a worst case scenario of credit risk exposure to the Group at 31 December 2009 and 2008, without taking account of any collateral held, master netting agreements or other credit enhancements attached. For on-balance sheet assets, the exposures set out above are based on net carrying amounts. For letters of guarantee issued, the maximum exposure to credit risk is the maximum amount that the Group could be required to pay if the guarantees are called upon. For loan commitment and other credit related liabilities that are irrevocable over the life of the respective facilities or revocable in the event of a significant adverse change, the maximum exposure to credit risk is disclosed as the full amount of the committed facilities.

Gross loans and advances

Gross loans and advances before loan impairment allowances are summarised by product type as follows:

	2009	2008
	HK$'000	HK$'000
Advances to customers		
Personal		
- Mortgages	**3,166,469**	2,763,231
- Others	**1,608,619**	1,487,617
Corporate		
- Commercial loans	**12,642,436**	10,702,963
- Trade finance	**879,272**	823,293
	18,296,796	15,777,104
Trade bills	**338,534**	203,238
Total	**18,635,330**	15,980,342

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

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

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

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Gross loans and advances (continued)

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

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

(a) Advances neither overdue nor impaired

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

	2009			
	Pass	**Special mention**	**Sub-Standard or below**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Advances to customers				
Personal				
- Mortgages	**3,120,875**	**20,707**	**4,280**	**3,145,862**
- Others	**1,547,825**	**54,857**	**395**	**1,603,077**
Corporate				
- Commercial loans	**12,226,482**	**287,719**	**1,574**	**12,515,775**
- Trade finance	**781,027**	**93,083**	**-**	**874,110**
	17,676,209	**456,366**	**6,249**	**18,138,824**
Trade bills	**321,955**	**16,579**	**-**	**338,534**
Total	**17,998,164**	**472,945**	**6,249**	**18,477,358**

	2008			
	Pass	Special mention	Sub-Standard or below	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Advances to customers				
Personal				
- Mortgages	2,715,581	14,170	2,809	2,732,560
- Others	1,424,976	37,651	12	1,462,639
Corporate				
- Commercial loans	10,044,260	571,424	-	10,615,684
- Trade finance	755,058	48,600	-	803,658
	14,939,875	671,845	2,821	15,614,541
Trade bills	137,793	65,445	-	203,238
Total	15,077,668	737,290	2,821	15,817,779

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Gross loans and advances (continued)

(a) Advances neither overdue nor impaired (continued)

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

(b) Advances overdue but not impaired

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

	2009					
	Overdue for 3 months or less	**Overdue for 6 months or less but over 3 months**	**Overdue for 1 year or less but over 6 months**	**Overdue for over 1 year**	**Total**	**Market value of collateral**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
Advances to customers						
Personal						
- Mortgages	**20,601**		**-**	**5**	**20,606**	**63,060**
- Others	**5,461**	**-**	**-**	**-**	**5,461**	**24,894**
Corporate						
- Commercial loans	**113,619**	**-**	**-**	**3,700**	**117,319**	**182,539**
- Trade finance	**3,529**	**-**	**-**	**-**	**3,529**	**-**
Total	**143,210**	**-**	**-**	**3,705**	**146,915**	**270,493**

	2008					
	Overdue for 3 months or less	Overdue for 6 months or less but over 3 months	Overdue for 1 year or less but over 6 months	Overdue for over 1 year	Total	Market value of collateral
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Advances to customers						
Personal						
- Mortgages	28,591	369	-	249	29,209	58,507
- Others	24,495	-	-	88	24,583	46,378
Corporate						
- Commercial loans	57,281	-	-	1,254	58,535	69,047
- Trade finance	3,941	-	-	-	3,941	5,028
Total	114,308	369	-	1,591	116,268	178,960

	2009	2008
	HK$'000	HK$'000
Current market value of collateral held against the covered portion of advances to customers	**270,493**	178,960
Covered portion of advances to customers	**138,545**	92,074
Uncovered portion of advances to customers	**8,370**	24,194

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Gross loans and advances (continued)

(c) Impaired advances

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

	2009		2008	
	Gross advances HK$'000	**Market value of collateral HK$'000**	Gross advances HK$'000	Market value of collateral HK$'000
Advances to customers				
Personal				
- Mortgages	**-**	**-**	1,462	1,500
- Others	**81**	**-**	395	503
Corporate				
- Commercial loans	**9,343**	**6,095**	28,744	21,337
- Trade finance	**1,633**	**-**	15,694	10,386
Total	**11,057**	**6,095**	46,295	33,726
Loan impairment allowances made in respect of such advances	**6,396**		20,059	

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

	2009 HK$'000	2008 HK$'000
Current market value of collateral held against the covered portion of advances to customers	**6,095**	33,726
Covered portion of advances to customers	**5,894**	28,561
Uncovered portion of advances to customers	**5,163**	17,734

Classified or impaired advances to customers are analysed as follows:

	2009 HK$'000	2008 HK$'000
Gross classified or impaired advances to customers	**21,585**	54,608
Gross classified or impaired advances to customers as a percentage of gross advances to customers	**0.12%**	0.35%
Individually assessed loan impairment allowances made in respect of such advances	**6,396**	20,059

Classified or impaired advances to customers follow the definitions set out in the Banking (Disclosure) Rules and represent advances which are either classified as "substandard", "doubtful" or "loss" under the Group's classification of loan quality, or individually assessed to be impaired.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Gross loans and advances (continued)

(d) Advances overdue for more than 3 months

The gross amount of advances overdue for more than 3 months of the Group is analysed as follows:

	2009		2008	
	Amount	**% of gross advances to customers**	Amount	% of gross advances to customers
	HK$'000		HK$'000	
Gross advances to customers which have been overdue for:				
- six months or less but over three months	**33**	**0.00%**	743	0.00%
- one year or less but over six months	**1,640**	**0.01%**	2,402	0.02%
- over one year	**12,237**	**0.07%**	14,817	0.09%
Advances overdue for over three months	**13,910**	**0.08%**	17,962	0.11%
Individually assessed loan impairment allowances made in respect of such advances	**5,970**		7,742	

	2009	2008
	HK$'000	HK$'000
Current market value of collateral held against the covered portion of advances to customers	**13,146**	27,472
Covered portion of advances to customers	**9,078**	9,791
Uncovered portion of advances to customers	**4,832**	8,171

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

As at 31 December 2009 and 2008 there were no advances to banks and other financial institutions overdue for more than three months.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Gross loans and advances (continued)

(e) Rescheduled advances

	2009		2008	
	Amount	**% of gross advances to customers**	Amount	% of gross advances to customers
	HK$'000		HK$'000	
Rescheduled advances to customers net of amounts included in advances overdue for more than 3 months	**1,574**	**0.01%**	4,280	0.03%

As at 31 December 2009, the total rescheduled advances to customers during the year amounted to HK$1,573,838 (2008: HK$5,488,000).

As at 31 December 2009 and 2008, there were no rescheduled advances to banks and other financial institutions for the Group.

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

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Gross loans and advances (continued)

(f) Concentration of advances to customers

(i) Sectoral analysis of gross advances to customers

The information concerning gross advances to customers of the Group has been analysed into loans used inside or outside Hong Kong by industry sectors of the borrowers as follows:

	2009					
	Gross advances HK$'000	% Covered by collateral or other security	Classified or impaired HK$'000	Overdue* HK$'000	Individually assessed impairment allowances HK$'000	Collectively assessed impairment allowances HK$'000
Loans for use in Hong Kong						
Industrial, commercial and financial						
- Property development	988,140	18.51%	-	-	-	2,456
- Property investment	3,559,498	99.79%	-	100,479	-	12,545
- Financial concerns	352,747	16.29%	-	772	-	649
- Stockbrokers	-	-	-	-	-	-
- Wholesale and retail trade	647,674	79.50%	1,607	4,066	33	1,903
- Manufacturing	1,126,072	47.64%	1,755	4,391	1,329	4,012
- Transport and transport equipment	483,255	64.27%	-	2,010	-	1,554
- Recreational activities	444	100.00%	-	-	-	2
- Information technology	506,888	1.33%	-	-	-	884
- Others	469,750	54.72%	-	2,599	-	1,749
Individuals						
- Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	109,058	99.86%	694	1,291	-	82
- Loans for purchase of other residential properties	2,882,192	99.98%	3,591	19,316	-	1,677
- Others	1,295,879	97.29%	477	5,538	81	981
Total loans for use in Hong Kong	12,421,597	77.85%	8,124	140,462	1,443	28,494
Trade finance	879,279	36.33%	1,640	5,169	1,644	3,161
Loans for use outside Hong Kong	4,995,920	71.44%	11,821	12,337	3,309	14,911
Gross advances to customers	18,296,796	74.10%	21,585	157,968	6,396	46,566

*Advances with a specific repayment date are classified as overdue when the principal or interest is past due and remains unpaid.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Gross loans and advances (continued)

(f) Concentration of advances to customers (continued)

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

	2008					
	Gross advances	% Covered by collateral or other security	Classified or impaired	Overdue*	Individually assessed impairment allowances	Collectively assessed impairment allowances
	HK$'000		HK$'000	HK$'000	HK$'000	HK$'000
Loans for use in Hong Kong						
Industrial, commercial and financial						
- Property development	815,035	20.70%	-	-	-	2,268
- Property investment	3,162,324	97.69%	-	11,542	-	13,399
- Financial concerns	376,451	22.91%	-	-	-	710
- Stockbrokers	-	-	-	-	-	-
- Wholesale and retail trade	640,119	74.82%	-	20,810	-	3,228
- Manufacturing	922,329	43.73%	10,674	8,147	6,173	3,848
- Transport and transport equipment	320,212	78.06%	-	2,007	-	2,077
- Recreational activities	793	100.00%	-	-	-	3
- Information technology	202,238	4.04%	-	1,300	-	356
- Others	587,963	58.95%	1,208	4,982	-	2,256
Individuals						
- Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	113,231	99.88%	710	2,130	169	85
- Loans for purchase of other residential properties	2,467,290	99.92%	3,584	27,607	24	1,552
- Others	1,282,300	92.94%	496	24,264	11	957
Total loans for use in Hong Kong	10,890,285	78.99%	16,672	102,789	6,377	30,739
Trade finance	823,292	58.33%	15,694	11,425	6,168	3,712
Loans for use outside Hong Kong	4,063,527	66.30%	22,242	34,825	7,514	16,971
Gross advances to customers	15,777,104	74.64%	54,608	149,039	20,059	51,422

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Gross loans and advances (continued)

(f) Concentration of advances to customers (continued)

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

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

	2009		2008	
	New impairment allowances	**Classified or impaired loans written off**	New impairment allowances	Classified or impaired loans written off
	HK$'000	**HK$'000**	HK$'000	HK$'000
Loans for use in Hong Kong				
Industrial, commercial and financial				
- Property development	**-**	**-**	408	-
- Property investment	**-**	**-**	2,410	-
- Financial concerns	**-**	**-**	128	-
- Wholesale and retail trade	**3,955**	**3,921**	625	1,027
- Manufacturing	**550**	**1,785**	6,582	1,770
- Transport and transport equipment	**-**	**-**	374	-
- Recreational activities	**-**	**-**	1	-
- Information technology	**-**	**-**	64	-
- Others	**1,164**	**1,164**	405	-
Individuals				
- Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	**3**	**-**	185	-
- Loans for purchase of other residential properties	**56**	**-**	312	-
- Others	**112**	**-**	172	-
Total loans for use in Hong Kong	**5,840**	**6,870**	11,666	2,797
Trade finance	**544**	**-**	6,067	-
Loans for use outside Hong Kong	**295**	**1,796**	6,407	628
Gross advances to customers	**6,679**	**8,666**	24,140	3,425

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Gross loans and advances (continued)

(f) Concentration of advances to customers (continued)

(ii) Geographical analysis of gross advances to customers and overdue advances

The following geographical analysis of gross advances to customers and overdue advances is based on the location of the counterparties, after taking into account the transfer of risk in respect of such advances where appropriate.

Gross advances to customers

	2009	2008
	HK$'000	HK$'000
Hong Kong	**14,990,345**	13,098,916
Mainland China	**3,306,451**	2,678,188
	18,296,796	15,777,104
Collectively assessed loan impairment allowances in respect of the gross advances to customers		
Hong Kong	**36,432**	42,122
Mainland China	**10,134**	9,300
	46,566	51,422

Overdue advances

	2009	2008
	HK$'000	HK$'000
Hong Kong	**153,004**	140,424
Mainland China	**4,964**	8,615
	157,968	149,039
Individually assessed loan impairment allowances in respect of the overdue advances		
Hong Kong	**5,993**	8,892
Mainland China	**398**	2,837
	6,391	11,729
Collectively assessed loan impairment allowances in respect of the overdue advances		
Hong Kong	**632**	796
Mainland China	**13**	6
	645	802

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Gross loans and advances (continued)

(f) Concentration of advances to customers (continued)

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

Classified or impaired advances

	2009	2008
	HK$'000	HK$'000
Hong Kong	**16,621**	46,651
Mainland China	**4,964**	7,957
	21,585	54,608
Individually assessed loan impairment allowances in respect of the classified or impaired advances		
Hong Kong	**5,998**	17,222
Mainland China	**398**	2,837
	6,396	20,059
Collectively assessed loan impairment allowances in respect of the classified or impaired advances		
Hong Kong	**8**	58
Mainland China	**13**	-
	21	58

Repossessed assets

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

	Carrying value	
	2009	2008
	HK$'000	HK$'000
Commercial properties	**-**	7,190
Residential properties	**-**	-
	-	7,190

The estimated market value of repossessed assets held by the Group as at 31 December 2009 amounted to HK$ Nil (2008: HK$8,000,000). They comprise properties in respect of which the Group has acquired access or control (e.g. through court proceedings or voluntary actions by the borrowers concerned) for release in full or in part of the obligations of the borrowers.

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

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

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Balances and placements with banks and other financial institutions

The following table presents an analysis of balances and placements with banks and other financial institutions that are neither overdue nor impaired as at 31 December by rating agency designation, based on Moody's ratings or their equivalent.

	2009			
	Aaa to A3	**Lower than A3**	**Unrated**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Central banks	**665,308**	**-**	**-**	**665,308**
Banks and other financial institutions	**12,405,182**	**243,477**	**56,848**	**12,705,507**
	13,070,490	**243,477**	**56,848**	**13,370,815**

	2008			
	Aaa to A3	Lower than A3	Unrated	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Central banks	258,957	-	-	258,957
Banks and other financial institutions	16,115,993	1,494	780,257	16,897,744
	16,374,950	1,494	780,257	17,156,701

As at 31 December 2009 and 2008, there were no overdue or impaired balances and placements with banks and other financial institutions.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Debt securities

The following table presents an analysis of debt securities neither overdue nor impaired as at 31 December by rating agency designation, based on Moody's ratings or their equivalent to the respective issues of the debt securities.

	2009				
	Financial assets designated at fair value through profit or loss	**Available-for-sale securities**	**Held-to-maturity securities**	**Loans and receivables**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
Aaa	**-**	**-**	**-**	**-**	**-**
Aa1 to Aa3	**-**	**232,094**	**828,775**	**-**	**1,060,869**
A1 to A3	**569,372**	**228,079**	**1,462,243**	**-**	**2,259,694**
Lower than A3	**223,744**	**27,795**	**2,439**	**-**	**253,978**
Unrated	**-**	**600,434**	**1,637,017**	**9**	**2,237,460**
	793,116	**1,088,402**	**3,930,474**	**9**	**5,812,001**

	2008				
	Financial assets designated at fair value through profit or loss	Available-for-sale securities	Held-to-maturity securities	Loans and receivables	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Aaa	133,021	-	234,365	-	367,386
Aa1 to Aa3	194,452	-	2,421,248	-	2,615,700
A1 to A3	42,284	239,988	771,066	-	1,053,338
Lower than A3	-	27,785	-	-	27,785
Unrated	-	19,612	99,997	77,645	197,254
	369,757	287,385	3,526,676	77,645	4,261,463

For the above debt securities with no issue credit rating, their issuer ratings are analysed as follows:

	2009				
	Financial assets designated at fair value through profit or loss	**Available-for-sale securities**	**Held-to-maturity securities**	**Loans and receivables**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
Aaa	**-**	**-**	**-**	**-**	**-**
Aa1 to Aa3	**-**	**208,387**	**791,967**	**-**	**1,000,354**
A1 to A3	**-**	**158,979**	**845,050**	**-**	**1,004,029**
Lower than A3		**233,068**	**-**	**-**	**233,068**
Unrated	**-**	**-**	**-**	**9**	**9**
	-	**600,434**	**1,637,017**	**9**	**2,237,460**

	2008				
	Financial assets designated at fair value through profit or loss	Available-for-sale securities	Held-to-maturity securities	Loans and receivables	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Aaa	-	-	-	-	-
Aa1 to Aa3	-	-	99,997	77,645	177,642
A1 to A3	-	19,612	-	-	19,612
Lower than A3	-	-	-	-	-
Unrated	-	-	-	-	-
	-	19,612	99,997	77,645	197,254

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Debt securities (continued)

As at 31 December 2009, overdue loan and receivables amount to HK$9,000 (31 December 2008: Nil). There were no impaired, mortgage-backed or asset-backed debt securities as at 31 December 2009 and 31 December 2008.

4.2 Market Risk

Market risk is the risk of loss that results from movements in market rates and prices. The Group's market risk in the trading book arises from customer-related business. The risk includes potential losses arising from changes in foreign exchange and interest rates as well as equities and commodities prices. On the other hand, banking book positions are subject to interest rate risk and liquidity risk. In particular, the Group's bond investment portfolio is exposed to the potential losses arising from changes in market price of the debt securities as these positions are subject to monthly mark-to-market valuation. The Group manages market risk in its trading book separately from its banking book.

Market risk management framework

The Group's risk management objective is to enhance shareholder value by maintaining risk exposures within acceptable limits. Market risk management framework of the Group comprises three levels. The Board of Directors is the ultimate decision making authority. Formulation of the risk management procedures and implementation mechanism, and monitoring of the compliance are mainly responsible by senior management (including CE and Head of SCD). CMD, Finance Division and Settlement Section are responsible for the oversight of the Group's market risk to ensure that overall and individual market risks are within the Group's risk tolerance. Risk exposures are monitored on a regular basis to ensure that they are within established risk limits and are regularly reported to the senior management.

The Group's control of market risk is based on restricting individual operations to a list of permissible instruments authorised by senior management, as well as enforcing rigorous new product approval procedures to ensure all risks arising are thoroughly identified, properly measured and adequately controlled.

Market risk is managed within various major risk limits approved by the RC, including risk positions and / or risk factor sensitivities. These overall risk limits are divided into sub-limits by reference to different risk products, including interest rate, foreign exchange rate, commodity price and equity products. Transactions are classified into different risk product categories according to the prominent type of risk inherent in the transactions.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.2 Market Risk (continued)

Currency risk

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

	2009							
	Renminbi	US Dollars	HK Dollars	Euro	Japanese Yen	Pound Sterling	Others	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets								
Cash and balances with banks and other financial institutions	1,126,147	3,005,693	2,854,195	317,253	62,004	202,799	419,486	7,987,577
Placements with banks and other financial institutions maturing between one and twelve months	160,479	1,446,990	2,607,553	-	-	125,371	1,184,983	5,525,376
Financial assets designated at fair value through profit or loss	-	793,116	-	-	-	-	-	793,116
Derivative financial instruments	-	5,054	344,882	-	-	-	-	349,936
Advances and other accounts	1,237,635	3,635,810	13,038,338	22,086	23,487	158	624,854	18,582,368
Investment in securities								
-Available-for-sale securities	275,534	232,094	278,194	226	-	-	347,706	1,133,754
- Held-to-maturity securities	-	910,721	2,549,212	-	470,541	-	-	3,930,474
- Loans and receivables	-	4	5	-	-	-	-	9
Investment properties	-	-	78,800	-	-	-	-	78,800
Properties, plant and equipment	10,373	-	647,090	-	-	-	-	657,463
Other assets (including deferred tax assets)	16,819	937	887,753	-	-	-	487	905,996
Total assets	2,826,987	10,030,419	23,286,022	339,565	556,032	328,328	2,577,516	39,944,869

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.2 Market Risk (continued)

Currency risk (continued)

	2009							
	Renminbi	US Dollars	HK Dollars	Euro	Japanese Yen	Pound Sterling	Others	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Liabilities								
Deposits and balances of banks and other financial institutions	(114,306)	(319,247)	(13,617)	(7,194)	(4,467)	-	(9,895)	(468,726)
Financial liabilities designated at fair value through profit or loss	-	-	-	-	-	-	-	-
Derivative financial instruments	-	(12,941)	(151,445)	-	-	-	-	(164,386)
Deposits from customers	(2,276,459)	(6,103,995)	(22,763,597)	(326,323)	(45,281)	(303,791)	(1,997,809)	(33,817,255)
Other accounts and provisions (including current and deferred tax liabilities)	(55,892)	(295,780)	(960,714)	(19,948)	(1,723)	(4,573)	(65,747)	(1,404,377)
Total liabilities	(2,446,657)	(6,731,963)	(23,889,373)	(353,465)	(51,471)	(308,364)	(2,073,451)	(35,854,744)
Net on-balance sheet position	380,330	3,298,456	(603,351)	(13,900)	504,561	19,964	504,065	4,090,125
Off-balance sheet net notional position*	1,722	(2,875,382)	4,101,720	14,120	(503,954)	(47,865)	(496,189)	194,172
Contingent liabilities and commitments	120,659	1,649,489	3,283,530	50,415	76,336	417	4,304	5,185,150

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.2 Market Risk (continued)

Currency risk (continued)

	2008							
	Renminbi	US Dollars	HK Dollars	Euro	Japanese Yen	Pound Sterling	Others	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets								
Cash and balances with banks and other financial institutions	724,397	771,847	6,093,011	177,712	26,771	114,867	677,149	8,585,754
Placements with banks and other financial institutions maturing between one and twelve months	68,916	1,549,436	6,002,192	120,351	-	112,191	868,522	8,721,608
Financial assets designated at fair value through profit or loss	-	267,248	102,509	-	-	-	-	369,757
Derivative financial instruments	-	779	385,166	-	-	-	-	385,945
Advances and other accounts	1,167,194	3,004,555	11,694,881	12,534	27,362	2,335	-	15,908,861
Investment in securities								
-Available-for-sale securities	287,385	-	41,077	220	-	-	-	328,682
- Held-to-maturity securities	-	749,094	2,777,582	-	-	-	-	3,526,676
- Loans and receivables	-	-	77,645	-	-	-	-	77,645
Investment properties	-	-	80,050	-	-	-	-	80,050
Properties, plant and equipment	-	-	584,477	-	-	-	-	584,477
Other assets (including deferred tax assets)	1,071	3,350	636,122	-	1,051	-	-	641,594
Total assets	2,248,963	6,346,309	28,474,712	310,817	55,184	229,393	1,545,671	39,211,049

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.2 Market Risk (continued)

Currency risk (continued)

	2008							
	Renminbi	US Dollars	HK Dollars	Euro	Japanese Yen	Pound Sterling	Others	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Liabilities								
Deposits and balances of banks and other financial institutions	(91,067)	(123,475)	(315,421)	(1,076)	(442,458)	-	(98,585)	(1,072,082)
Financial liabilities designated at fair value through profit or loss	-	(377,788)	(390,721)	-	-	-	-	(768,509)
Derivative financial instruments	-	(7,865)	(200,980)	-	-	-	-	(208,845)
Deposits from customers	(1,631,627)	(5,515,191)	(22,314,131)	(305,163)	(23,130)	(205,201)	(1,455,354)	(31,449,797)
Other accounts and provisions (including current and deferred tax liabilities)	(234,269)	(209,683)	(1,471,077)	(6,841)	-	(2,921)	(47,468)	(1,972,259)
Total liabilities	(1,956,963)	(6,234,002)	(24,692,330)	(313,080)	(465,588)	(208,122)	(1,601,407)	(35,471,492)
Net on-balance sheet position	292,000	112,307	3,782,382	(2,263)	(410,404)	21,271	(55,736)	3,739,557
Off-balance sheet net notional position*	13,406	(134,623)	(124,567)	6,353	410,082	(28,999)	55,747	197,399
Contingent liabilities and commitments	89,962	1,023,825	3,506,167	36,856	31,159	1,220	-	4,689,189

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

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.2 Market Risk (continued)

Interest rate risk

The Group's interest rate risk exposures are mainly structural. The major types of interest rate risk from structural positions are:

- repricing risk – mismatches in the maturity or repricing periods of assets and liabilities
- basis risk – different pricing basis for different transactions so that yield on assets and cost of liabilities may change by different amounts within the same repricing period
- yield curve risk – non-parallel shifts in the yield curve, e.g. steepening or flattening yield curves, causing adverse effects on net interest income or economic value
- option risk – exercise of the options embedded in assets, liabilities and Off-Balance Sheet inducing a change in the cash flows of assets and liabilities

The Group has formulated an "Interest Rate Risk Management Policy" which sets out the framework and the methodologies to identify, measure, monitor and control interest rate risk.

Both the members of the Asset and Liability Management Committee ("ALCO") and RC are responsible for interest rate risk management. ALCO maintains oversight of interest rate risk and reviews the policies, guidelines and limits proposed by Finance Division. RC sanctions the interest rate risk management policies formulated by ALCO. The interest rate risk is identified and measured on a daily basis. The Treasury Division manages the interest rate risk according to the established policies. The Finance Division closely monitors the related risks according to approved limits and reports the results to ALCO regularly.

Gap analysis is one of the tools used to measure the Group's exposure to repricing risk. As the risk is complicated by having optionality embedded in certain products, behavioural assumptions are made to reflect more accurately the interest rate risk exposures. This gap analysis provides the Group with a static view of the maturity and repricing characteristics of its balance sheet positions. The Group uses interest rate derivatives to hedge its interest rate exposures and in most cases, plain vanilla interest rate swaps are used.

Sensitivities of earnings and economic value to interest rate changes (Earnings at Risk and Economic Value at Risk) are assessed through a hypothetical interest rate shock of 200 basis points across the yield curve on both sides. Earnings at Risk and Economic Value at Risk are controlled respectively within an approved percentage of the projected net interest income for the year and the latest capital base as sanctioned by RC. The results are reported to ALCO and RC on a regular basis. Apart from the hypothetical scenario, business-as-usual ("BAU") scenario has been established based on a simpler and more reasonable principle. It generates results of the impact on earnings and economic value under interest rate change assuming constant strategic business development and customer behaviour.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.2 Market Risk (continued)

Interest rate risk (continued)

The impact of basis risk is gauged by the projected change in net interest income under scenarios of imperfect correlation in the adjustment of the rates earned and paid on different instruments. Ratios of assets to liabilities with similar pricing basis are established to monitor such risk.

Stress test on yield curve risk is performed to assess the impact on earnings and economic value due to the steepening or flattening of the yield curve. The impact of optionality of demand and savings deposits and prepayment of mortgage loans is also assessed under different stress test scenarios.

The interest rate risk exposures in the Group are controlled through the use of limits :

1. Earnings at Risk limit.
2. Economic Value at Risk limit.
3. Interest Rate Mismatch Gap limits.

Before launching a new product or business, relevant departments are required to go through a risk assessment process, which include assessment of underlying interest rate risk and consideration of the adequacy of current risk management mechanism. Any material impact on interest rate risk noted during the risk assessment process will be reported to the Head of SCD.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.2 Market Risk (continued)

Interest rate risk (continued)

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

	2009						
	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets							
Cash and balances with banks and other financial institutions	7,341,290	-	-	-	-	646,287	7,987,577
Placements with banks and other financial institutions maturing between one and twelve months	-	3,775,781	1,749,595	-	-	-	5,525,376
Financial assets designated at fair value through profit or loss	-	-	-	526,187	266,929	-	793,116
Derivative financial instruments	-		-	-	-	349,936	349,936
Advances and other accounts	15,134,791	2,709,807	705,912	24,375	7,483	-	18,582,368
Investment in securities							
- Available-for-sale securities	139,320	673,548	182,726	92,808	-	45,352	1,133,754
- Held-to-maturity securities	696,787	2,072,561	998,509	162,617	-	-	3,930,474
- Loans and receivables	-	-	-	-	-	9	9
Investment properties	-	-	-	-	-	78,800	78,800
Properties, plant and equipment	-	-	-	-	-	657,463	657,463
Other assets (including deferred tax assets)	-	-	-	-	-	905,996	905,996
Total assets	23,312,188	9,231,697	3,636,742	805,987	274,412	2,683,843	39,944,869
Liabilities							
Deposits and balances of banks and other financial institutions	(237,305)	(114,306)	-	-	-	(117,115)	(468,726)
Financial liabilities designated at fair value through profit or loss	-	-	-	-	-	-	-
Derivative financial instruments	-	-	-	-	-	(164,386)	(164,386)
Deposits from customers	(25,691,917)	(4,267,882)	(2,353,052)	(33,625)	-	(1,470,779)	(33,817,255)
Other accounts and provisions (including current and deferred tax liabilities)	(455,475)	-	-	-	-	(948,902)	(1,404,377)
Total liabilities	(26,384,697)	(4,382,188)	(2,353,052)	(33,625)	-	(2,701,182)	(35,854,744)
Interest sensitivity gap	(3,072,509)	4,849,509	1,283,690	772,362	274,412	(17,339)	4,090,125

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.2 Market Risk (continued)

Interest rate risk (continued)

	2008						
	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets							
Cash and balances with banks and other financial institutions	8,178,523	-	-	-	-	407,231	8,585,754
Placements with banks and other financial institutions maturing between one and twelve months	-	8,660,344	61,264	-	-	-	8,721,608
Financial assets designated at fair value through profit or loss	224,964	-	102,509	42,284	-	-	369,757
Derivative financial instruments	-	-	-	-	-	385,945	385,945
Advances and other accounts	13,715,466	1,904,819	257,250	16,286	15,040	-	15,908,861
Investment in securities							
- Available-for-sale securities	-	-	69,686	217,699	-	41,297	328,682
- Held-to-maturity securities	328,308	1,922,598	423,262	852,508	-	-	3,526,676
- Loans and receivables	-	77,645	-	-	-	-	77,645
Investment properties	-	-	-	-	-	80,050	80,050
Properties, plant and equipment	-	-	-	-	-	584,477	584,477
Other assets (including deferred tax assets)	-	-	-	-	-	641,594	641,594
Total assets	22,447,261	12,565,406	913,971	1,128,777	15,040	2,140,594	39,211,049
Liabilities							
Deposits and balances of banks and other financial institutions	(631,106)	(35,028)	-	-	-	(405,948)	(1,072,082)
Financial liabilities designated at fair value through profit or loss	(215,925)	(409,496)	(143,088)	-	-	-	(768,509)
Derivative financial instruments	-	-	-	-	-	(208,845)	(208,845)
Deposits from customers	(21,669,699)	(7,250,469)	(1,411,314)	(33,223)	-	(1,085,092)	(31,449,797)
Other accounts and provisions (including current and deferred tax liabilities)	(542,539)	-	-	-	-	(1,429,720)	(1,972,259)
Total liabilities	(23,059,269)	(7,694,993)	(1,554,402)	(33,223)	-	(3,129,605)	(35,471,492)
Interest sensitivity gap	(612,008)	4,870,413	(640,431)	1,095,554	15,040	(989,011)	(3,739,557)

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.2 Market Risk (continued)

Interest rate risk (continued)

Sensitivity analysis to market risk exposure of the Group

The Group is principally exposed to HKD and USD in terms of interest rate risk. At 31 December 2009, if HKD and USD market interest rates had been 100 basis points lower with other variables held constant, profit before tax for the year would have been HK$20,500,000 (2008: HK$16,000,000) lower by HKD and USD assets liabilities structure. The impact on reserves would be insignificant. The sensitivity analysis set out above is illustrative only.

Interest rate exposures in banking book

The following is a summary of possible effects of market interest rates shocks on the Group's interest rate exposure for major currencies in its banking book. Subsidiaries are excluded from the analysis below:

	Impact on positions at 31 December	
Earnings perspective	**2009**	2008
Scenarios	**HK$'000**	HK$'000
Down 100 basis points parallel shift in HK dollar yield curves	**(22,000)**	(22,000)
Up 100 basis points parallel shift in US dollar yield curves	**(1,500)**	(6,000)

The stress tests set out above are illustrative only. The projections illustrate that stressful changes in market interest rates in response to exceptional but plausible events would have adverse effects both on earnings over the next twelve months. The stress tests measure the possible effect of interest rates shock on earnings is assessed by changes in net interest income. To construct stressful scenarios, severe assumptions are made, including a change in the correlation between HK dollar and US dollar interest rates, parallel movement of interest rates for the banking book positions of all repricing or maturity dates. In the absence of actions that would be taken to mitigate the impact of interest rates shock, all positions are assumed to run to maturity and reprice or mature simultaneously within a given time band. As the risk is complicated by having optionality embedded in certain products, behavioural assumptions are made to reflect more accurately the interest rate risk exposures.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.2 Market risk (continued)

Foreign exchange risk

Sensitivity analysis to market risk exposure of the Group (continued)

At 31 December 2009, if HKD had weakened/strengthened by 1% against USD with all other variable held constant, the profit before taxation for the year would have been HK$4,231,000 higher/lower, mainly as a result of foreign exchange gain/loss on translation of USD denominated financial assets larger than foreign exchange loss/gain on translation of USD denominated financial liabilities. If HKD had weakened/strengthened by 5% against CNY with all other variable held constant, the profit before taxation for the year would have been HK$19,103,000 higher/lower, mainly as a result of foreign exchange gain/loss on translation of CNY denominated financial assets larger than foreign exchange loss/gain on translation of CNY denominated financial liabilities.

At 31 December 2008, if HKD had weakened/strengthened by 1% against USD with all other variable held constant, the profit before taxation for the year would have been HK$223,000 lower/higher, mainly as a result of foreign exchange gain/loss on translation of USD denominated financial assets lesser than foreign exchange loss/gain on translation of USD denominated financial liabilities. If HKD had weakened/strengthened by 5% against CNY with all other variable held constant, the profit before taxation for the year would have been HK$15,270,000 higher/lower, mainly as a result of foreign exchange gain/loss on translation of CNY denominated financial assets larger than foreign exchange loss/gain on translation of CNY denominated financial liabilities.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.3 Liquidity Risk

Liquidity risk is the risk that the Group may not be able to fund increases in assets or meet obligations as they fall due without incurring unacceptable losses.

Liquidity risk management framework

The liquidity risk management framework of the Group comprises three levels. The Board of Directors and the RC are the ultimate decision making authority and are responsible for approving the liquidity management policy and assure the compliance with regulatory requirements. The senior management (including CE, Head of SCD and the Asset and Liability Management Committee) are responsible for the formulation of the liquidity management policy and procedures and monitoring of their implementation. The Treasury Division, assisted by other functional departments, including the Finance Division, is responsible for daily management of liquidity to monitor the liquidity risk and provide regular reports to the management and local regulatory bodies.

The Group has developed a robust liquidity risk management mechanism, by maintaining an appropriate size of highly-liquefiable assets and proper liability structure, enabling the Group to meet, even under adverse market conditions, all its obligations as they fall due, and to fund all its asset growth and strategic opportunities without forced liquidation of its assets at short notice.

At present, the Group has set up three Key Risk Indicators, which are 1-month liquidity ratio, 1-month mismatch ratio and loan-to-deposit ratio. The indicators mentioned are used as the major tools in the identification, measurement, monitoring and control of the liquidity risk on regular basis by setting limits, assessing and monitoring the ratios. Besides, the Group also monitors deposit stability, concentration of deposits from large depositors and liquidity profile of the investment portfolio.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

Liquidity risk management framework (continued)

The related risk management process includes:

- Perform cash-flow projections under normal and stressed scenarios, using the net mismatch gap between assets and liabilities to estimate the prospective net funding requirements;
- Set limits on mismatch ratio to control the size of the cumulative net mismatch positions;
- Maintain strong liquidity ratios to comply with both internal and external regulatory requirements;
- Maintain a diversified liability base to ensure sufficient funding sources;
- Maintain a proper level of highly liquid assets to serve as a liquidity buffer for emergency needs;
- Monitor the structure and stability of the deposit portfolio;
- Assess the ability to borrow from the inter-bank money market to avoid over-reliance on the money market for funding;
- Maintain a proper contingency plan, which includes setting early warning signals (including internal indicators and market indicators) with timely monitoring procedures and establishing a management reporting system and contingency procedures.

Before launching a new product or business, relevant departments are required to go through a risk assessment process, which includes assessment of underlying liquidity risk and consideration of the adequacy of the current risk management mechanism. Any material impact on liquidity risk noted during the risk assessment process will be reported to the Head of SCD.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

(A) Liquidity ratio

	2009	2008
Average liquidity ratio	**44.20%**	42.88%

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

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

(B) Analysis of undiscounted cash flows by contractual maturities

(a) Non-derivative cash flows

The table below presents the cash flows of the Group as at 31 December for non-derivative financial liabilities by remaining contractual maturities.

	2009					
	Up to 1 month	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
Financial liabilities						
Deposits and balances of banks and other financial institutions	**(354,436)**	**(114,643)**	**-**	**-**	**-**	**(469,079)**
Financial liabilities designated at fair value through profit or loss	**-**	**-**	**-**	**-**	**-**	**-**
Deposits from customers	**(27,124,104)**	**(4,272,016)**	**(2,413,602)**	**(35,739)**	**-**	**(33,845,461)**
Other financial liabilities	**(1,096,582)**	**(8,424)**	**(1,538)**	**(4,655)**	**-**	**(1,111,199)**
Total financial liabilities	**(28,575,122)**	**(4,395,083)**	**(2,415,140)**	**(40,394)**	**-**	**(35,425,739)**

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

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

(a) Non-derivative cash flows (continued)

	2008					
	Up to 1 month	1-3 months	3-12 Months	1-5 years	Over 5 years	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Financial liabilities						
Deposits and balances of banks and other financial institutions	(1,037,271)	(35,292)	-	-	-	(1,072,563)
Financial liabilities designated at fair value through profit or loss	(2,725)	(4,910)	(361,332)	(242,895)	(293,904)	(905,766)
Deposits from customers	(22,719,988)	(7,207,984)	(1,424,432)	(139,828)	-	(31,492,232)
Other financial liabilities	(1,247,168)	(5,730)	(4,932)	(3,798)	-	(1,261,628)
Total financial liabilities	(25,007,152)	(7,253,916)	(1,790,696)	(386,521)	(293,904)	(34,732,189)

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

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

(b) Derivative cash flows

(i) Derivatives settled on a net basis

The Group's derivatives that will be settled on a net basis include:

- Foreign exchange derivatives: non-deliverable OTC currency options, non-deliverable currency forwards; and
- Interest rate derivatives: interest rate swaps; and
- Bullion derivatives: bullion margin contracts.

The table below analyses the Group's derivative financial instruments as at 31 December that will be settled on a net basis into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the table are the net contractual undiscounted cash flows of derivatives with net negative fair value.

	2009					
	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Foreign exchange derivatives	(137,538)	-	(12,003)	-	-	(149,541)
Interest rate derivatives	-	(5,843)	(6,354)	(32,710)	(7,622)	(52,529)
Bullion derivatives	(233)	-	-	-	-	(233)
	(137,771)	(5,843)	(18,357)	(32,710)	(7,622)	(202,303)

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

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

(b) Derivative cash flows (continued)

(i) Derivatives settled on a net basis (continued)

	2008					
	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Foreign exchange derivatives	(168,635)	(2,115)	(13,323)	-	-	(184,073)
Interest rate derivatives	261	(110)	(514)	10,271	1,994	11,902
Bullion derivatives	(6,031)	-	-	-	-	(6,031)
	(174,405)	(2,225)	(13,837)	10,271	1,994	(178,202)

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

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

(b) Derivative cash flows (continued)

(ii) Derivatives settled on a gross basis

The Group's derivatives that will be settled on a gross basis include OTC currency options, currency forwards and OTC equity options.

The tables below analyse the Group's derivative financial instruments as at 31 December that will be settled on a gross basis into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the table are the gross contractual undiscounted cash flows for all derivatives that are settled on a gross basis

	2009					
	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Foreign exchange derivatives:						
- Outflow	(8,202,297)	(1,247,359)	(7,186)	-	-	(9,456,842)
- Inflow	8,223,794	1,249,248	7,460	-	-	9,480,502
Equity derivatives:						
- Outflow	(1,329)	-	-	-	-	(1,329)
- Inflow	1,329	-	-	-	-	1,329
Total outflow	(8,203,626)	(1,247,359)	(7,186)	-	-	(9,458,171)
Total inflow	8,225,123	1,249,248	7,460	-	-	9,481,831

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

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

(b) Derivative cash flows (continued)

(ii) Derivatives settled on a gross basis (continued)

	2008					
	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Foreign exchange derivatives:						
- Outflow	(30,987)	(1,671)	-	-	-	(32,658)
- Inflow	30,981	1,673	-	-	-	32,654
Equity derivatives:						
- Outflow	(633)	(276)	-	-	-	(909)
- Inflow	633	276	-	-	-	909
Total outflow	(31,620)	(1,947)	-	-	-	(33,567)
Total inflow	31,614	1,949	-	-	-	33,563

(c) Off-balance sheet items

Loan commitments

The contractual amounts of the Group's off-balance sheet financial instruments as at 31 December 2009 that commit it to extend credit to customers and other facilities amounting to HK$ 3,006,482,000 (2008: HK$3,414,849,000) can be drawn no later than 1 year.

Financial guarantees and other financial facilities

Financial guarantees and other financial facilities as at 31 December 2009 amounting to HK$1,487,757,000 (2008: HK$925,729,000) are maturing no later than 1 year.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

(C) Maturity analysis

Tables below analyse assets and liabilities of the Group as at 31 December into relevant maturity groupings based on the remaining period at balance sheet date to the contractual maturity date.

	2009							
	On demand	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Indefinite	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets								
Cash and balances with banks and other financial institutions	1,507,141	6,480,436	-	-	-	-	-	7,987,577
Placements with banks and other financial institutions maturing between one and twelve months	-	-	3,775,781	1,749,595	-	-	-	5,525,376
Financial assets designated at fair value through profit or loss								
– debt securities designated at fair value through profit or loss								
- others	-	-	-	-	526,186	266,930	-	793,116
Derivative financial instruments	307,835	33,005	2,049	2,713	1,440	2,894	-	349,936
Advances and other accounts								
– advances to customers	1,147,899	725,228	1,856,763	3,576,698	5,392,083	5,490,192	54,971	18,243,834
– trade bills	-	160,994	175,094	2,446	-	-	-	338,534
Investment in securities								
– debt securities held for available-for-sales								
- certificates of deposit held	-	139,319	208,386	77,710	155,359	-	-	580,774
- others	-	-	-	182,726	324,902	-	-	507,628
– debt securities held for held-to-maturity								
- certificates of deposit held	-	-	-	240,733	156,041	-	-	396,774
- others	-	470,541	99,999	2,502,575	460,585	-	-	3,533,700
– debt securities held for loans and receivables	-	-	-	-	-	-	9	9
– equity securities	-	-	-	-	-	-	45,352	45,352
Investment properties	-	-	-	-	-	-	78,800	78,800
Properties, plant and equipment	-	-	-	-	-	-	657,463	657,463
Other assets (including deferred tax assets)	3,680	869,933	-	31,787	71	-	525	905,996
Total assets	2,966,555	8,879,456	6,118,072	8,366,983	7,016,667	5,760,016	837,120	39,944,869

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

(C) Maturity analysis (continued)

	2009							
	On demand	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Indefinite	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Liabilities								
Deposits and balances of banks and other financial institutions	(117,116)	(237,304)	(114,306)	-	-	-	-	(468,726)
Financial liabilities designated at fair value through profit or loss – others	-	-	-	-	-	-	-	-
Derivative financial instruments	(137,734)	(11,646)	(87)	(2,372)	(8,184)	(4,363)	-	(164,386)
Deposits from customers	(19,931,915)	(7,190,776)	(4,267,882)	(2,393,057)	(33,625)	-	-	(33,817,255)
Other accounts and provisions (including current and deferred tax liabilities)	(532,181)	(595,433)	(154,328)	(33,126)	(89,309)	-	-	(1,404,377)
Total liabilities	(20,718,946)	(8,035,159)	(4,536,603)	(2,428,555)	(131,118)	(4,363)	-	(35,854,744)
Net liquidity gap	(17,752,392)	844,298	1,581,469	5,938,428	6,885,549	5,755,653	837,120	4,090,125

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

(C) Maturity analysis (continued)

	2008							
	On demand	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Indefinite	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets								
Cash and balances with banks and other financial institutions	1,080,477	7,505,277	-	-	-	-	-	8,585,754
Placements with banks and other financial institutions maturing between one and twelve months	-	-	8,660,344	61,264	-	-	-	8,721,608
Financial assets designated at fair value through profit or loss								
– debt securities designated at fair value through profit or loss								
- others	-	-	-	102,508	42,284	224,965	-	369,757
Derivative financial instruments	358,443	463	3,034	22,061	1,944	-	-	385,945
Advances and other accounts								
– advances to customers	1,207,415	955,869	1,138,648	2,442,009	5,348,420	4,575,315	37,947	15,705,623
– trade bills	90	91,584	105,763	5,801	-	-	-	203,238
Investment in securities								
– debt securities held for available-for-sales								
- others	-	-	-	69,686	217,699	-	-	287,385
– debt securities held for held-to-maturity								
- certificates of deposit held	-	-	100,085	-	-	-	-	100,085
- others	-	99,997	153,542	423,262	2,749,790	-	-	3,426,591
– debt securities held for loans and receivables	-	-	77,645	-	-	-	-	77,645
– equity securities	-	-	-	-	-	-	41,297	41,297
Investment properties	-	-	-	-	-	-	80,050	80,050
Properties, plant and equipment	-	-	-	-	-	-	584,477	584,477
Other assets (including deferred tax assets)	4,084	634,724	-	2,270	-	-	516	641,594
Total assets	2,650,509	9,287,914	10,239,061	3,128,861	8,360,137	4,800,280	744,287	39,211,049

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

(C) Maturity analysis (continued)

	2008							
	On demand	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Indefinite	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Liabilities								
Deposits and balances of banks and other financial institutions	(405,948)	(631,106)	(35,028)	-	-	-	-	(1,072,082)
Financial liabilities designated at fair value through profit or loss – others	-	-	-	(340,325)	(158,289)	(269,895)	-	(768,509)
Derivative financial instruments	(174,452)	(314)	(3,083)	(23,131)	(6,829)	(1,036)	-	(208,845)
Deposits from customers	(14,834,911)	(7,879,881)	(7,188,468)	(1,411,314)	(135,223)	-	-	(31,449,797)
Other accounts and provisions (including current and deferred tax liabilities)	(624,669)	(659,761)	(513,822)	(98,324)	(75,683)	-	-	(1,972,259)
Total liabilities	(16,039,980)	(9,171,062)	(7,740,401)	(1,873,094)	(376,024)	(270,931)	-	(35,471,492)
Net liquidity gap	(13,389,471)	116,852	2,498,660	1,255,767	7,984,113	4,529,349	744,287	3,739,557

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

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

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.4 Capital Management

The major objective of the Group's capital management is to maximise total shareholders' return while maintaining a capital adequacy position in relation to the Group's overall risk profile. The Group periodically reviews its capital structure and adjusts the capital mix where appropriate to achieve the required rate of return on capital.

The Group has developed and maintained a sound framework of policies and controls on capital management to support the development of the Group's business and to meet the statutory capital adequacy ratio. ALCO monitors the Group's capital adequacy. The Group has complied with all the statutory capital standards for all the periods.

For the implementation of Basel II in 2007, the Group has adopted the standardised approach under Pillar one to calculate the capital charge on credit risk, market risk and operational risk in compliance with the Banking (Capital) Rules. This new regulatory capital framework aligns regulatory capital requirements more closely with the inherent risks.

The Group established an Internal Capital Adequacy Assessment Process (ICAAP). Through this process, each material risk from the Group's main activities is assessed by pre-defined assessment models, and a comprehensive judgment of the overall risk profile is decided subsequently by taking into account the Group's governance structure, risk management quality, internal control environment and capital strength. Finally, the minimum CAR is derived through the procedures to relate the Group's overall risk profile to its capital adequacy. The minimum CAR aims to cover the various material risks undertaken by the Group. The Group considers this ICAAP process as an on-going process for capital management and periodically reviews and adjusts its capital structure in relation to the overall risk profile.

In addition, the annual capital plans of the Group are drawn up and discussed by the ALCO and submitted to the board for approval. The plan is built up by assessing the implications of various factors upon capital adequacy such as the business strategies, return on equity, risk appetite, credit rating, as well as regulatory requirements. Based on this study, our future capital demand and the way to obtain the capital sources are derived. The plan is to ensure the Group's capital adequacy and achieve optimal capital structure in order to align with its business development needs and risk profile.

(a) Capital adequacy ratio

	2009	2008
Capital adequacy ratio	**15.06%**	15.37%
Core capital ratio	**14.29%**	14.29%

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.4 Capital Management (continued)

(a) Capital adequacy ratio (continued)

The capital ratios are computed on the combined basis that comprises the positions of the Bank's local offices and oversea branches specified by the HKMA for its regulatory purposes and in accordance with the Banking (Capital) Rules.

The differences between the basis of consolidation for accounting and regulatory purposes are described in Note 26.

(b) Components of capital base after deductions

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

	2009	2008
	HK$'000	HK$'000
Core capital:		
Paid up ordinary share capital	**300,000**	300,000
Reserves	**2,845,085**	3,374,891
Profit and loss account	**255,303**	(601,103)
	3,400,388	3,073,788
Deductions from core capital	**(12,257)**	(12,251)
Core capital	**3,388,131**	3,061,537
Supplementary capital:		
Reserves on revaluation of premises and investment properties	**224**	224
Fair Value gain arising from holdings of available-for-sale securities	**715**	1,317
Collective loan impairment allowances	**46,566**	51,422
Regulatory reserve	**149,257**	191,495
	196,762	244,458
Deductions from supplementary capital	**(12,257)**	(12,252)
Supplementary capital	**184,505**	232,206
Total capital base after deductions	**3,572,636**	3,293,743

Subsidiaries which are not included in the consolidation group for the calculation of capital adequacy ratios are denoted in Note 26. Investment costs in such subsidiaries are deducted from the capital base.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.4 Capital Management (continued)

(c) Capital charge for credit, market and operational risks

The capital adequacy ratios shown above are calculated on the combined basis for regulatory purposes in accordance with the Banking (Capital) Rules. The table below summaries the capital requirements and capital charge calculated by applying 8% on the risk-weighted amounts, computed on the same combined basis for credit, market, and operational risks.

	2009	2008
	HK$'000	HK$'000
Credit risk	**1,780,656**	1,580,347
Market risk	**2,964**	13,837
Operational risk	**155,959**	155,062
	1,939,579	1,749,246

(i) Capital requirements for credit risk

	2009					
	Total exposures	**Exposures after CRM***		**Risk-weighted amount**		**Capital requirement****
		Rated	**Unrated**	**Rated**	**Unrated**	
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**	**HK$'000**
On-balance sheet exposures						
Sovereign	**1,278,930**	**1,577,074**	**-**	**13,748**	**-**	**1,100**
Public sector entity	**-**	**111,720**	**-**	**22,344**	**-**	**1,788**
Bank	**17,525,568**	**17,453,362**	**72,206**	**5,267,581**	**16,379**	**422,717**
Corporate	**11,884,794**	**962,653**	**10,287,896**	**619,419**	**10,287,896**	**872,585**
Cash items	**142,138**	**-**	**142,138**	**-**	**-**	**-**
Regulatory retail	**1,851,424**	**-**	**1,684,233**	**-**	**1,263,175**	**101,054**
Residential mortgage loans	**4,585,409**	**-**	**4,470,074**	**-**	**2,228,389**	**178,271**
Other exposures which are not past due	**1,466,279**	**-**	**1,427,278**	**-**	**1,427,278**	**114,182**
Past due exposures	**9,616**	**-**	**9,616**	**-**	**11,663**	**933**
Total for on-balance sheet exposures	**38,744,158**	**20,104,809**	**18,093,441**	**5,923,092**	**15,234,780**	**1,692,630**
Off-balance sheet exposures						
Off-balance sheet exposures other than OTC derivative transactions or credit derivative contracts	**1,087,569**	**26,116**	**1,061,453**	**6,653**	**1,024,573**	**82,498**
OTC derivative transactions	**132,530**	**126,851**	**5,679**	**63,425**	**5,679**	**5,528**
Total for off-balance sheet exposures	**1,220,099**	**152,967**	**1,067,132**	**70,078**	**1,030,252**	**88,026**
	39,964,257	**20,257,776**	**19,160,573**	**5,993,170**	**16,265,032**	**1,780,656**

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.4 Capital Management (continued)

(c) Capital charge for credit, market and operational risks (continued)

(i) Capital requirements for credit risk (continued)

	2008					
	Total exposures	Exposures after CRM* Rated	Exposures after CRM* Unrated	Risk-weighted amount Rated	Risk-weighted amount Unrated	Capital requirement**
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
On-balance sheet exposures						
Sovereign	401,224	404,779	-	17,184	-	1,375
Public sector entity	-	114,666	-	22,933	-	1,835
Bank	21,286,836	20,396,014	891,603	5,117,979	236,471	428,356
Corporate	9,269,441	63,333	8,837,904	63,333	8,837,904	712,099
Cash items	150,661	-	150,661	-	-	-
Regulatory retail	1,812,793	-	1,685,374	-	1,264,031	101,122
Residential mortgage loans	3,946,912	-	3,823,029	-	1,995,853	159,668
Other exposures which are not past due	1,331,615	-	1,252,259	-	1,252,259	100,181
Past due exposures	10,426	-	10,426	-	13,934	1,115
Total for on-balance sheet exposures	38,209,908	20,978,792	16,651,256	5,221,429	13,600,452	1,505,751
Off-balance sheet exposures						
Off-balance sheet exposures other than OTC derivative transactions or credit derivative contracts	976,367	8,530	967,837	2,244	912,510	73,180
OTC derivative transactions	34,344	30,308	4,036	13,661	4,036	1,416
Total for off-balance sheet exposures	1,010,711	38,838	971,873	15,905	916,546	74,596
	39,220,619	21,017,630	17,623,129	5,237,334	14,516,998	1,580,347

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

** For disclosure purposes, capital requirement is calculated by applying 8% on the risk-weighted amount, which may differ from the Bank's actual regulatory capital.

As at 31 December 2009, credit exposures deducted from the capital base amounted to HK$ 20,601,000 (2008: HK$ 20,590,000).

The Bank used the standardised (credit risk) approach ("STC approach") for calculation of credit risk.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.4 Capital Management (continued)

(c) Capital charge for credit, market and operational risks (continued)

(i) Capital requirements for credit risk (continued)

The External credit assessment institutions ("ECAI") recognised by the Group includes Standard & Poor's, Moody's and Fitch. The Group adopted external rating based approach to determine the risk weight of the following classes of exposures, including those of securitisation exposures:

- Sovereign
- Public sector entity
- Multilateral development bank
- Bank
- Securities firm
- Corporate

The process the Bank used to map ECAI issuer ratings to exposures booked in the banking book is a process prescribed in Part 4 of the Banking (Capital) Rules.

Counterparty credit risk exposures

The Group's counterparty credit risk arising from over-the-counter ("OTC") derivative transactions, repo-style transactions both in trading and banking book is subject to the same risk management framework as above mentioned. The Group established credit limit through formal credit approval procedures to control the pre-settlement credit risk arising from derivatives transactions and settlement limit to control the settlement risk arising from foreign exchange-related transactions in both the trading book and banking book. The Group monitors the risk exposure due to fluctuations in the market value by determining the current exposure value of the transactions. Exceptions or excesses are timely and closely identified and monitored by credit risk management units.

As the Group has not implemented capital allocation policy, there is no internal capital assigned for counterparty credit exposures.

The Group established prudent eligibility criteria and haircut policy of debt securities being pledged as collateral for repo-style transactions.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.4 Capital Management (continued)

(c) Capital charge for credit, market and operational risks (continued)

(i) Capital requirements for credit risk (continued)

Counterparty credit risk exposures (continued)

The Group formulated policy for classification of credit assets according to the probability of default of individual counterparty and the period of overdue. If there is objective evidence that an impairment loss has been incurred, impairment allowance will be provided according to regulatory and HK accounting requirements.

The following table summarises the Group's exposures to counterparty credit risk arising from OTC derivative transactions:

	2009	2008
	HK$'000	HK$'000
Gross total positive fair value	**40,601**	25,155
Credit equivalent amount	**132,530**	34,344
Less: recognised collateral	**-**	-
Net credit equivalent amount	**132,530**	34,344
Net credit equivalent amount analysed by type of issuer:		
Bank	**126,851**	30,308
Corporate	**5,679**	3,001
Others	**-**	1,035
	132,530	34.344
Risk weighted amount analysed by type of issuer:		
Bank	**63,423**	13,661
Corporate	**5,679**	3,001
Others	**-**	1,035
	69,102	17,697
Notional amount of recognised credit derivative contracts which provide credit protection	**-**	-

There is no effect of valid bilateral netting agreement on the credit equivalent amounts of the derivative transactions as at 31 December 2009 (2008: Nil).

There are no outstanding repo-style transactions or credit derivative contracts as at 31 December 2009 and 2008.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.4 Capital Management (continued)

(c) Capital charge for credit, market and operational risks (continued)

(i) Capital requirements for credit risk (continued)

Credit risk mitigation

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

The main types of recognised collaterals include cash deposit, gold bullion, debt securities, equities and funds for non past-due exposures. In addition, real property collateral is also recognised for past due exposures. Those collaterals taken by the Group are compliant with the comprehensive approach in its treatment of recognised collateral for credit risk mitigation in capital calculation as mentioned in the Banking (Capital) Rules.

According to the Banking (Capital) Rules, the recognised guarantees for credit risk mitigation under STC approach includes the guarantee given by sovereign, public sector entity, multilateral development bank, bank, securities firm with a lower risk weights than the counterparty; or corporate with external credit rating A- or above.

The concentration risk management for collaterals is embedded in the collateral management policy, including stress testing. To cope with the requirement under Pillar two, we have adopted a scorecard methodology to assess our credit concentration risk and consider whether add-on capital charge is needed to cover this risk.

Up to the date of report, the Group has not used any recognised credit derivative contracts, on- or off-balance sheet recognised netting for credit risk mitigation yet.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.4 Capital Management (continued)

(c) Capital charge for credit, market and operational risks (continued)

(i) Capital requirements for credit risk (continued)

Credit risk mitigation (continued)

Exposures, other than those arising from OTC derivative transactions and repo-style transactions, covered by recognised credit risk mitigation are analysed as follows:

	2009		2008	
	Covered by recognised collateral	**Covered by recognised guarantees**	Covered by recognised collateral	Covered by recognised guarantees
	HK$'000	**HK$'000**	HK$'000	HK$'000
On-balance sheet exposures				
Corporate	**419,847**	**227,554**	367,825	1,470
Regulatory retail	**82,096**	**71,939**	122,946	3,382
Residential mortgage loans	**4,964**	**110,371**	9,733	114,150
Other exposures which are not past due	**39,001**	**-**	79,356	-
Past due exposures	**5,520**	**1**	3,409	-
Off-balance sheet exposures	**66,470**	**19,300**	97,322	6,735
	617,898	**429,165**	680,591	125,737

Asset securitisation

The Bank has not acted as an originating institution in respect of securitisation transactions during the year.

(ii) Capital charge for market risk

	2009	2008
	HK$'000	HK$'000
Interest rate exposures	**732**	297
Foreign exchange exposures	**2,232**	13,540
	2,964	13,837

The Bank used the standardised (market risk) approach ("STM approach") for calculation of market risk.

The Bank's positions covered by STM approach are as follows:

	2009		2008	
	Long	**Short**	Long	Short
	HK$'000	**HK$'000**	HK$'000	HK$'000
Interest rate exposures	**973,716**	**974,075**	750,220	750,747
Foreign exchange exposures (Net)	**27,901**	**-**	169,256	-
	1,001,617	**974,075**	919,476	750,747

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.4 Capital Management (continued)

(c) Capital charge for credit, market and operational risks (continued)

(ii) Capital charge for market risk (continued)

Equity exposures in banking book

Equity holdings in other entities are accounted for in accordance with the underlying intentions of holdings, at the outset of the acquisition of the respective equity exposures. Bookings for the equity holdings taken for relationship and strategic reasons will be separated from the bookings for equity holdings taken for other reasons (including the reason of capital appreciation).

Gains or losses related to equity exposures are summarised below:

	2009	2008
	HK$'000	HK$'000
Realised gains from sales or liquidations	**-**	-
Unrealised gains on revaluation recognized in reserves but not through profit or loss	**1,589**	1,546
Unrealised gains included in supplementary capital	**715**	696

(iii) Capital charge for operational risk

	2009	2008
	HK$'000	HK$'000
Capital charge for operational risk	**155,959**	155,062

The Bank used the standardised (operational risk) approach ("STO approach") for calculation of operational risk.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.5 Fair values of financial assets and liabilities

(a) Financial instruments not measured at fair value

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

Balances with banks and other financial institutions and Trade bills

The maturities of these financial assets and liabilities are within one year and the carrying value approximates fair value.

Advances to customers, banks and other financial institutions

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

Held-to-maturity securities and loans and receivables

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

The carrying value and fair value of held-to-maturity securities as at 31 December 2009 amounted to HK$3,930,474,000 (2008: HK$3,526,676,000) and HK$3,929,751,000 (2008: HK$3,428,705,000) respectively; both the carrying value and fair value of loans and receivables as at 31 December 2009 amounted to HK$9,000 (2008: HK$77,645,000 and HK$91,617,000 respectively).

Deposits from customers

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

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.5 Fair values of financial assets and liabilities (continued)

(b) Financial instruments measured at fair value

Financial instruments measured at fair value are classified into following three levels:

– Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities including spot derivative contracts.

– Level 2: Valuation technique using inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly. This level includes the majority of the OTC derivative contracts and issued structured deposit.

– Level 3: Valuation technique using inputs for the asset or liability that is not based on observable market data (unobservable inputs). This level includes equity investment and debt instruments with significant unobservable components.

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

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

For certain illiquid debt securities and unlisted private equity held by the Group, management obtains valuation quotations from counterparties. The fair value of these financial instruments may be based on unobservable inputs which may have significant impact on the valuation of these financial instruments, and therefore, these instruments have been classified by the Group as level 3. The Group has established internal procedures to control and limit the Group’s exposure to such financial instruments.

There have been no significant transfers between level 1 and 2 during the year 2009.

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.5 Fair values of financial assets and liabilities (continued)

(b) Financial instruments measured at fair value (continued)

(i) Fair value hierarchy

	2009			
	Level 1	Level 2	Level 3	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Financial assets				
Financial assets designated at fair value through profit or loss				
- Debt securities	-	793,116	-	793,116
Derivative financial instruments	307,966	41,970	-	349,936
Available-for-sale securities			-	-
- Debt securities	-	507,628	580,774	1,088,402
- Equity securities	-		45,352	45,352
	307,966	1,342,714	626,126	2,276,806
Financial liabilities				
Financial liabilities designated at fair value through profit or loss	-	-	-	-
Derivative financial instruments	(137,786)	(26,600)	-	(164,386)
	(137,786)	(26,600)	-	(164,386)

Notes to the Financial Statements (continued)

4. Financial risk management (continued)

4.5 Fair values of financial assets and liabilities (continued)

(b) Financial instruments measured at fair value (continued)

(ii) Reconciliation of Level 3 items

	2009			
	Financial assets			
	Financial assets designated at fair value through profit or loss	Available-for-sale securities		
	Debt securities	Debt securities	Equity securities	Total
	HK$'000	HK$'000	HK$'000	HK$'000
At 1 January 2009	224,965	-	41,297	266,262
Total gains/(losses)				
- Profit or loss	17,786	-	-	17,786
- Other comprehensive income	-	(1,083)	4,055	2,972
Purchases	-	581,858	-	581,858
Sales	(242,751)	-	-	(242,751)
At 31 December 2009	-	580,775	45,352	626,127
Total gains/(losses) for the year included in profit or loss for assets held as at 31 December 2009	-	-`	-	-

Gains or losses included in profit or loss for the year as well as gains or losses relating to assets held as at 31 December 2009 are presented in “Net trading income” or “Net gain/(loss) on financial instruments designated at fair value through profit or loss” depending on the category of the related financial asset.

Notes to the Financial Statements (continued)

5. Net interest income

	2009	2008
	HK$'000	HK$'000
Interest income		
Cash and due from banks and other financial institutions	**171,829**	469,709
Advances to customers	**486,954**	636,414
Listed investments	**24,558**	3,796
Unlisted investments	**86,056**	190,220
Others	**6,707**	16,351
	776,104	1,316,490
Interest expense		
Due to banks, customers and other financial institutions	**(127,879)**	(476,761)
Debt securities in issue	**-**	(4,742)
Others	**(1,124)**	(7,716)
	(129,003)	(489,219)
Net interest income	**647,101**	827,271

Included within interest income is HK$359,000 (2008: HK$464,000) of interest with respect to income recognised on advances classified as impaired for the year ended 31 December 2009.

Included within interest income and interest expense are HK$755,428,000 (2008: HK$1,287,318,000) and HK$120,827,000 (2008: HK$468,804,000) for financial assets and financial liabilities that are not recognised at fair value through profit or loss respectively.

With effect from 1 January 2009, interest income and expense for interest rate derivatives held for trading have been reclassified from “Net interest income” to “Net trading income”. The impact on the respective line items is not material in either 2009 or 2008 and such comparative figures have not been restated.

Notes to the Financial Statements (continued)

6. Net fees and commission income

	2009 HK$'000	2008 HK$'000
Fees and commission income		
Securities brokerage		
- Stockbroking	**177,213**	125,251
- Bonds	**579**	31,591
Bills commissions	**41,910**	45,876
Loan commissions	**17,463**	19,706
Payment services	**20,370**	20,592
Insurance	**17,220**	15,463
Fund distribution	**5,024**	4,497
safe deposit box	**9,959**	9,866
Others		
- agency services	**1,127**	1,706
- BOC cards	**1,003**	1,055
- correspondent banking	**1,259**	1,364
- credit cards	**98**	125
- currency exchange	**250**	278
- dormant accounts	**880**	775
- information search	**2,267**	2,370
- low deposit balance accounts	**790**	1,020
- postage and telegrams	**1,032**	856
- sundries	**4,568**	10,926
	303,012	293,317
Fees and commission expenses		
Securities brokerage	**(28,619)**	(22,471)
Payment services	**(2,167)**	(2,227)
Others	**(13,488)**	(22,994)
	(44,274)	(47,692)
Net fees and commission income	**258,738**	245,625
Of which arise from		
- financial assets or financial liabilities not at fair value through profit or loss		
- Fees and commission income	**25,244**	26,544
- Fees and commission expenses	**(1)**	(401)
	25,243	26,143
- trust and other fiduciary activities		
- Fees and commission income	**8,832**	5,820
- Fees and commission expenses	**(2,679)**	(2,828)
	6,153	2,992

7. Net trading income

	2009 HK$'000	2008 HK$'000
Net gain/ (loss) from:		
- foreign exchange and foreign exchange products	**39,315**	63,855
- interest rate instruments	**(3,402)**	(9,503)
- commodities	**-**	806
	35,913	55,158

Notes to the Financial Statements (continued)

8. Net gain on investments in securities

	2009	2008
	HK$'000	HK$'000
Net gain from redemption of held-to-maturity securities	**-**	131

9. Other operating income

	2009	2008
	HK$'000	HK$'000
Dividend income from investments in securities		
- unlisted investments	**4,616**	4,197
Gross rental income from investment properties	**3,392**	2,966
Less: Outgoings in respect of investment properties	**(1)**	(60)
Others	**265**	725
	8,272	7,828

Included in the "Outgoings in respect of investment properties" is HK$ Nil (2008: HK$26,000) of direct operating expenses related to investment properties that were not let during the year.

10. Net reversal/(charge) of impairment allowances

	2009	2008
	HK$'000	HK$'000
Advances to customers		
Individually assessed		
- new allowances	**(6,584)**	(14,891)
- releases	**11,205**	1,919
- recoveries	**12,506**	9,500
Net reversal /(charge) of individually assessed loan impairment Allowances (Note 24)	**17,127**	(3,472)
Collectively assessed		
- new allowances	**(95)**	(9,249)
- releases	**4,926**	1,389
Net reversal/(charge) of collectively assessed loan impairment allowances (Note 24)	**4,831**	(7,860)
Net reversal/(charge) of loan impairment allowances	**21,958**	(11,332)
Others	**1,588**	(1,756)
Net reversal/(charge) of impairment allowances	**23,546**	(13,088)

Notes to the Financial Statements (continued)

11. Operating expenses

	2009	2008
	HK$'000	HK$'000
Staff costs (including directors' emoluments)		
- salaries and other costs	161,327	160,096
- pension cost	14,942	14,828
	176,269	174,924
Premises and equipment expenses (excluding depreciation)		
- rental of premises	21,314	19,422
- information technology	28,564	29,548
- others	4,921	4,345
	54,799	53,315
Depreciation (Note 28)	14,076	13,706
Auditor's remuneration		
- audit services	2,570	2,933
- non-audit services	117	97
Lehman Brothers related products*	174,636	135,321
Other operating expenses	54,468	39,484
	476,935	419,780

* Expenses incurred on Lehman Brothers related products were primarily in relation to the Lehman Brothers minibonds ("Minibonds") repurchase arrangements announced on 22 July 2009 as summarised below.

Under the Repurchase Scheme (details are disclosed in note 3.5), the Group has, without admission of liability, made an offer to repurchase at a price equivalent to 60% of the nominal value of the principal invested for eligible customers below the age of 65 as at 1 July 2009 or at 70% of the nominal value of the principal invested for eligible customers aged 65 or above as at 1 July 2009. If any recovery is made from the Minibonds, the Group will make further payments to eligible customers who have accepted the Repurchase Scheme according to the terms set out in the scheme. The Group has also made a voluntary offer to pay an ex gratia amount to customers who would have qualified as eligible customers but for their previous settlements with the Group, to bring them in line with the Repurchase Scheme offer. The Group has further made available an amount equivalent to the total commission income received as a Minibonds distributor of approximately HK$12,178,000 to the trustee of the Minibonds to fund the trustee's expenses in realising the value of the underlying collateral in respect of the outstanding Minibonds.

Notes to the Financial Statements (continued)

12. Net gain from disposal of/fair value adjustments on investment properties

	2009 HK$'000	2008 HK$'000
Net loss on disposal of investment properties	**(10)**	-
Net gain on fair value adjustments on investment properties (Note 27)	**17,750**	2,100
	17,740	2,100

13. Net loss from disposal of properties, plant and equipment

	2009 HK$'000	2008 HK$'000
Net loss on disposal of other fixed assets	**(1)**	(9)

14. Taxation

Taxation in the income statement represents:

	2009 HK$'000	2008 HK$'000
Hong Kong profits tax		
- current year taxation	**54,500**	117,070
- over-provision in prior years	**(500)**	(2,500)
Deferred tax charge (Note 33)	**15,182**	(16,536)
Hong Kong profits tax	**69,182**	98,034
Overseas taxation	**18,914**	25,050
	88,096	123,084

Hong Kong profits tax has been provided at the rate of 16.5 % on the estimated assessable profits arising in Hong Kong during 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 taxation on the Group's profit before taxation that differs from the theoretical amount that would arise using the taxation rate of Hong Kong is as follows:

	2009 HK$'000	2008 HK$'000
Profit before taxation	**509,276**	714,267
Calculated at a taxation rate of 16.5%	**84,030**	117,854
Effect of different taxation rates in other countries	**5,247**	4,864
Income not subject to taxation	**(2,281)**	(1,380)
Expenses not deductible for taxation purposes	**1,600**	4,246
Over-provision in prior years	**(500)**	(2,500)
Taxation charge	**88,096**	123,084
Effective tax rate	**17.30%**	17.23%

Notes to the Financial Statements (continued)

15. Profit attributable to equity holders of the Bank

The profit of the Bank for the year ended 31 December 2009 attributable to equity holders of the Bank and dealt with in the financial statements of the Bank amounted to HK$418,553,000 (2008: HK$587,198,000).

16. Dividends

	2009		2008	
	Per share HK$	**Total HK$'000**	Per share HK$	Total HK$'000
First interim dividend paid	**-**	**-**	226.00	678,000
First interim dividend declared	**48.50**	**145,500**	-	-
Second interim dividend declared	**-**	**-**	167.00	501,000
	48.50	**145,500**	393.00	1,179,000

At a meeting held on 31 December 2009, the Board declared a first interim dividend of HK$48.50 per ordinary share for 2009 amounting to HK$145,500,000.

17. Retirement benefit costs

The principal defined contribution schemes for the Group's employees are ORSO schemes exempted under the MPF Schemes Ordinance and the BOC-Prudential Easy Choice MPF Scheme. Under the ORSO schemes, employees make monthly contributions to the ORSO schemes equal to 5% of their basic salaries, while the employer makes monthly contributions equal to 5% to 15% of the employees' monthly basic salaries, depending on years of service. The employees are entitled to receive 100% of the employer's contributions upon termination of employment after completing 20 years of service, or at a scale ranging from 20% to 95% for employees who have completed between 3 to 20 years of service, on conditions of retirement, early retirement, permanent incapacity and ill-health or termination of employment other than summary dismissal.

With the implementation of the MPF Schemes Ordinance on 1 December 2000, the Group also participates in the BOC-Prudential Easy Choice MPF Scheme, of which the trustee is BOCI-Prudential Trustee and the investment manager is BOCI-Prudential Manager, which are related parties of the Bank.

The Group's total contributions made to the ORSO schemes for the year ended 31 December 2009 amounted to approximately HK$11,514,000 (2008: approximately HK$11,715,000), after a deduction of forfeited contributions of approximately HK$530,000 (2008: approximately HK$618,000). For the MPF Scheme, the Group contributed approximately HK$1,554,000 (2008: approximately HK$1,457,000) for the year ended 31 December 2009.

Notes to the Financial Statements (continued)

18. Share option schemes

(a) Share Option Scheme and Sharesave Plan

The principal terms of the Share Option Scheme and the Sharesave Plan were approved and adopted by written resolutions of all the shareholders of the Bank's intermediate holding company, BOCHKHL, dated 10 July 2002.

The purpose of the Share Option Scheme is to provide the participants with the opportunity to acquire proprietary interests in BOCHKHL. The Board of BOCHKHL (the "BOCHKHL Board") may, in its absolute discretion, offer to grant options under the Share Option Scheme to any person as the BOCHKHL Board may select. The subscription price for the shares shall be determined on the date of grant by the BOCHKHL Board as an amount per share calculated on the basis of established rules. An option may be exercised in whole or in part at any time after the date prescribed by the BOCHKHL Board and from time to time as specified in the offer and on or before the termination date prescribed by the BOCHKHL Board.

The purpose of the Sharesave Plan is to encourage broad-based employee ownership of the shares of BOCHKHL. The amount of the monthly contribution under the savings contract to be made in connection with an option shall be the amount which the relevant eligible employee is willing to contribute, which amount shall not be less than 1% and not more than 10% of the eligible employee's monthly salary as at the date of application or such other maximum or minimum amounts as permitted by the BOCHKHL Board. When an option is exercised during an exercise period, it may be exercised in whole or in part.

No options were granted pursuant to the Share Option Scheme or the Sharesave Plan during the year 2009 (2008: Nil).

(b) Pre-Listing Share Option Scheme

On 5 July 2002, several directors of the Group were granted options by BOC Hong Kong (BVI) Limited ("BOC (BVI)"), the immediate holding company of BOCHKHL, pursuant to a Pre-Listing Share Option Scheme to purchase from BOC (BVI) an aggregate of 3,652,800 existing issued shares of BOCHKHL. The Group has taken advantage of the transitional provisions set out in paragraph 53 of HKFRS 2 under which the new recognition and measurement policies have not been applied to all options granted to employees on or before 7 November 2002.

Notes to the Financial Statements (continued)

18. Share option schemes (continued)

(b) Pre-Listing Share Option Scheme (continued)

Details of the share options outstanding as at 31 December 2009 are disclosed as follows:

	Total number of share options to Directors of the Group	**Average Exercise price (HK$ per share)**
At 1 January 2009	**778,900**	
Less: Share options exercised during the year	**(723,000)**	**8.5**
At 31 December 2009	**55,900**	
Exercisable at 31 December 2009	**55,900**	

	Total number of share options to Directors of the Group	Average Exercise price (HK$ per share)
At 1 January 2008	934,300	
Less: Share options exercised during the year	(155,400)	8.5
At 31 December 2008	778,900	
Exercisable at 31 December 2008	778,900	

Share options were exercised on a regular basis throughout the year, the weighted average share price during the year was HK$16.80 (2008: HK$15.81).

The options granted under this scheme can be exercised at HK$8.50 per share in respect of the option price of HK$1.00. These options have a vesting period of four years from the date on which dealings in the shares commenced on the Stock Exchange with a valid exercise period of ten years. No offer to grant any options under the Pre-Listing Share Option Scheme will be made on or after the date on which dealings in the shares commenced on the Stock Exchange.

Notes to the Financial Statements (continued)

19. Directors' and senior management's emoluments

Directors' emoluments

Details of the emoluments paid to or receivable by the directors of the Bank in respect of their services rendered for the Bank and managing the subsidiaries within the Group during the year are as follows:

	2009	2008
	HK$'000	HK$'000
Fees	**1,800**	2,780
Other emoluments		
- basic salaries and allowances	**3,417**	3,047
- discretionary bonuses	**-**	1,781
- others (including pension contributions)	**514**	475
	5,731	8,083

Fees of HK$450,000 (2008: HK$660,000) were paid to the Independent Non-Executive Directors during the year.

In July 2002, options were granted to several Directors of the Group by BOC (BVI), the immediate holding company of BOCHKHL under the Pre-Listing Share Option Scheme as set out in Note 18(b). Full details of the scheme are stated in Note 18. During the year, certain options were exercised, but no benefits arising from the granting of these share options were included in the Directors' emoluments disclosed above or recognised in the income statement.

Notes to the Financial Statements (continued)

20. Cash and balances with banks and other financial institutions

	The Group and the Bank	
	2009	2008
	HK$'000	HK$'000
Cash	**142,138**	150,661
Balances with central banks	**665,308**	258,957
Balances with banks and other financial institutions	**699,695**	670,859
Placements with banks and other financial institutions maturing within one month	**6,480,436**	7,505,277
	7,987,577	8,585,754

21. Financial assets designated at fair value through profit or loss

	The Group and the Bank	
	2009	2008
	HK$'000	HK$'000
At fair value		
Debt securities		
- Listed in Hong Kong	**569,372**	-
- Listed outside Hong Kong	**223,744**	-
- Unlisted	**-**	369,757
	793,116	369,757

Financial assets designated at fair value through profit or loss are analysed by type of issuer as follows:

	The Group and the Bank	
	2009	2008
	HK$'000	HK$'000
Sovereigns	**43,082**	42,284
Corporate	**750,034**	-
Banks and other financial institutions	**-**	327,473
	793,116	369,757

Notes to the Financial Statements (continued)

22. Derivative financial instruments

The Group enters into the following equity, foreign exchange, interest rate and bullion related derivative financial instruments for trading and risk management purposes:

Currency forwards represent commitments to purchase and sell foreign currency on a future date.

Currency and interest rate swaps are commitments to exchange one set of cash flows for another. Swaps result in an exchange of currencies or interest rates (for example, fixed rate for floating rate) or a combination of all these (i.e. cross-currency interest rate swaps). Except for certain currency swap contracts, no exchange of principal takes place.

Foreign currency, interest rate and equity options are contractual agreements under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, either to buy (a call option) or sell (a put option) at or by a set date or during a set period, a specific amount of the financial instrument at a predetermined price. In consideration for the assumption of foreign exchange and interest rate risk, the seller receives a premium from the purchaser. Options are negotiated over-the-counter ("OTC") between the Group and its counterparty or traded through the stock exchange (for example, exchange-traded stock option).

The contract/notional amounts and fair values of derivative financial instruments held by the Group are set out in the following tables. The contract/notional amounts of these instruments indicate the volume of transactions outstanding at the balance sheet dates and certain of them provide a basis for comparison with fair value instruments recognised on the consolidated balance sheet. However, they do not necessarily indicate the amounts of future cash flows involved or the current fair values of the instruments and, therefore, do not indicate the Group's exposure to credit or market risks. The derivative financial instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in market interest rates, foreign exchange rates or equity prices relative to their terms. The aggregate fair values of derivative financial instruments assets and liabilities can fluctuate significantly from time to time.

Notes to the Financial Statements (continued)

22. Derivative financial instruments (continued)

The Group trades OTC derivative products mainly for customer business. The Group strictly follows risk management policies in providing derivative products to our customers and trading of derivative products in the interbank market.

Derivatives are also used to manage the interest rate risk of the banking book. A derivative instrument must be included in the approved product list before any transactions for that instrument can be made. There are limits to control the notional amount of exposure arising from derivative transactions, and the maximum tenor of the deal and management alert limit (MAL) in profit and loss is set.

The following tables summarise the contract/notional amounts of each significant type of derivative financial instrument as at 31 December:

	The Group and the Bank		
	2009		
	Trading	Not qualified for hedge accounting*	Total
	HK$'000	HK$'000	HK$'000
Exchange rate contracts			
Spot, forwards and swap	11,204,975	-	11,204,975
Foreign currency option contracts			
- Options purchased	15,659	-	15,659
- Options written	15,659	-	15,659
	11,236,293	-	11,236,293
Interest rate contracts			
Swaps	-	734,412	734,412
Bullion contracts	19,469	-	19,469
Equity contracts			
Equity option contracts			
- Options purchased	4,931	-	4,931
- Options written	4,931	-	4,931
	9,862	-	9,862
Total	11,265,624	734,412	12,000,036

* Derivative transactions which do not qualify as hedged for accounting purposes but are managed in conjunction with the financial instruments designated at fair value through profit or loss are separately disclosed in compliance with the requirements set out in the Banking (Disclosure) Rules.

Notes to the Financial Statements (continued)

22. Derivative financial instruments (continued)

	The Group and the Bank		
	2008		
	Trading	Not qualified for hedge accounting*	Total
	HK$'000	HK$'000	HK$'000
Exchange rate contracts			
Spot, forwards and swap	3,327,746	-	3,327,746
Foreign currency option contracts			
- Options purchased	5,917	-	5,917
- Options written	5,917	-	5,917
	3,339,580	-	3,339,580
Interest rate contracts			
Swaps	-	677,815	677,815
Bullion contracts	144,325	-	144,325
Equity contracts			
Equity option contracts			
- Options purchased	2,829	-	2,829
- Options written	2,829	-	2,829
	5,658	-	5,658
Total	3,489,563	677,815	4,167,378

Notes to the Financial Statements (continued)

22. Derivative financial instruments (continued)

The following tables summarise the fair values of each class of derivative financial instrument as at 31 December:

	The Group and the Bank 2009					
	Fair value assets			Fair value liabilities		
	Trading HK$'000	Not qualified for hedge accounting HK$'000	Total HK$'000	Trading HK$'000	Not qualified for hedge accounting HK$'000	Total HK$'000
Exchange rate contracts						
Spot, forwards and swap	344,807	-	344,807	151,371	-	151,371
Foreign currency option contracts						
- Options purchased	161	-	161	-	-	-
- Options written	-	-	-	161	-	161
	344,968	-	344,968	151,532	-	151,532
Interest rate contracts						
Swaps	-	4,333	4,333	-	12,546	12,546
Bullion contract	560	-	560	233	-	233
Equity contracts						
Equity option contracts						
- Options purchased	75	-	75	-	-	-
- Options written	-	-	-	75	-	75
	75	-	75	75	-	75
Total	345,603	4,333	349,936	151,840	12,546	164,386

	The Group and the Bank 2008					
	Fair value assets			Fair value liabilities		
	Trading HK$'000	Not qualified for hedge accounting HK$'000	Total HK$'000	Trading HK$'000	Not qualified for hedge accounting HK$'000	Total HK$'000
Exchange rate contracts						
Spot, forwards and forward	368,496	-	368,496	190,367	-	190,367
Foreign currency option contracts						
- Options purchased	78	-	78	-	-	-
- Options written	-	-	-	78	-	78
	368,574	-	368,574	190,445	-	190,445
Interest rate contracts						
Swaps	-	5,396	5,396	-	12,164	12,164
Bullion contract	11,770	-	11,770	6,031	-	6,031
Equity contracts						
Equity option contracts						
- Options purchased	205	-	205	-	-	-
- Options written	-	-	-	205	-	205
	205	-	205	205	-	205
Total	380,549	5,396	385,945	196,681	12,164	208,845

Notes to the Financial Statements (continued)

22. Derivative financial instruments (continued)

The credit risk weighted amounts of the above derivative financial instruments are as follows:

	The Group and the Bank	
	2009	2008
	HK$'000	HK$'000
Exchange rate contracts		
Forwards	**46,823**	16,605
Swap	**17,585**	-
Interest rate contracts		
Swaps	**4,696**	1,093
	69,104	17,698

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

There is no effect of bilateral netting agreement on the fair values or the credit risk-weighted amounts of the derivative financial instruments.

Notes to the Financial Statements (continued)

23. Advances and other accounts

	The Group and the Bank	
	2009	2008
	HK$'000	HK$'000
Personal loans and advances	**4,775,088**	4,250,849
Corporate loans and advances	**13,521,708**	11,526,255
Advances to customers	**18,296,796**	15,777,104
Loan impairment allowances		
- Individually assessed	**(6,396)**	(20,059)
- Collectively assessed	**(46,566)**	(51,422)
	(52,962)	(71,481)
Trade bills	**338,534**	203,238
Total	**18,582,368**	15,908,861

As at 31 December 2009, advances to customers included accrued interest on gross advances of HK$23,806,000 (2008: HK$40,881,000).

As at 31 December 2009 and 2008, no impairment allowance was made in respect of trade bills.

24. Loan impairment allowances

	The Group and the Bank		
	2009		
	Individual assessment		
	Personal	**Corporate**	**Total**
	HK$'000	**HK$'000**	**HK$'000**
At 1 January 2009	**204**	**19,855**	**20,059**
Credited to income statement (Note 10)	**(698)**	**(16,429)**	**(17,127)**
Loans written off during the year as uncollectible	**(250)**	**(8,416)**	**(8,666)**
Recoveries	**825**	**11,681**	**12,506**
Unwind of discount on allowance	**-**	**(359)**	**(359)**
Translation difference	**-**	**(17)**	**(17)**
At 31 December 2009	**81**	**6,315**	**6,396**

	The Group and the Bank		
	2009		
	Collective assessment		
	Personal	**Corporate**	**Total**
	HK$'000	**HK$'000**	**HK$'000**
At 1 January 2009	**2,910**	**48,512**	**51,422**
Charged/(credited) to income statement (Note 10)	**95**	**(4,926)**	**(4,831)**
Translation difference	**-**	**(25)**	**(25)**
At 31 December 2009	**3,005**	**43,561**	**46,566**

Notes to the Financial Statements (continued)

24. Loan impairment allowances (continued)

	The Group and the Bank		
	2008		
	Individual assessment		
	Personal	Corporate	Total
	HK$'000	HK$'000	HK$'000
At 1 January 2008	36	10,948	10,984
(Credited)/Charged to income statement (Note 10)	(141)	3,613	3,472
Loans written off during the year as uncollectible	-	(3,425)	(3,425)
Recoveries	319	9,181	9,500
Unwind of discount on allowance	(10)	(454)	(464)
Translation difference	-	(8)	(8)
At 31 December 2008	204	19,855	20,059

	The Group and the Bank		
	2008		
	Collective assessment		
	Personal	Corporate	Total
	HK$'000	HK$'000	HK$'000
At 1 January 2008	2,436	41,119	43,555
Charged to income statement (Note 10)	474	7,386	7,860
Translation difference	-	7	7
At 31 December 2008	2,910	48,512	51,422

Notes to the Financial Statements (continued)

25. Investment in securities

	The Group	
	2009	2008
	HK$'000	HK$'000
(a) Available-for-sale securities		
Debt securities, at fair value		
- Unlisted	**1,088,402**	287,385
Equity securities, at fair value		
- Unlisted	**45,352**	41,297
	1,133,754	328,682
(b) Held-to-maturity securities		
Listed, at amortised cost		
- in Hong Kong	**160,179**	-
- outside Hong Kong	**80,460**	157,190
Unlisted, at amortised cost	**3,689,835**	3,369,486
	3,930,474	3,526,676
(c) Loans and receivables		
Unlisted, at amortised cost	**9**	77,645
Total	**5,064,237**	3,933,003
Market value of listed held-to-maturity securities	**249,642**	155,823

	The Bank	
	2009	2008
	HK$'000	HK$'000
(a) Available-for-sale securities		
Debt securities, at fair value		
- Unlisted	**1,088,402**	287,385
Equity securities, at fair value		
- Unlisted	**2,174**	2,126
	1,090,576	289,511
(b) Held-to-maturity securities		
Listed, at amortised cost		
- in Hong Kong	**160,179**	-
- outside Hong Kong	**80,460**	157,190
Unlisted, at amortised cost	**3,689,835**	3,369,486
	3,930,474	3,526,676
(c) Loans and receivables		
Unlisted, at amortised cost	**9**	77,645
Total	**5,021,059**	3,893,832
Market value of listed held-to-maturity securities	**249,642**	155,823

Notes to the Financial Statements (continued)

25. Investment in securities (continued)

Investment in securities is analysed by type of issuer as follows:

	The Group 2009			
	Available-for-sale securities	**Held-to-maturity securities**	**Loans and receivables**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Sovereigns	**-**	**570,540**	**-**	**570,540**
Public sector entities	**-**	**-**	**-**	**-**
Banks and other financial institutions	**1,088,402**	**3,197,317**	**9**	**4,285,728**
Corporate entities	**45,352**	**162,617**	**-**	**207,969**
	1,133,754	**3,930,474**	**9**	**5,064,237**

	The Group 2008			
	Available-for-sale securities	Held-to-maturity securities	Loans and receivables	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Sovereigns	-	99,997	-	99,997
Public sector entities	-	-	-	-
Banks and other financial institutions	287,385	3,426,679	77,645	3,791,709
Corporate entities	41,297	-	-	41,297
	328,682	3,526,676	77,645	3,933,003

	The Bank 2009			
	Available-for-sale Securities	**Held-to-maturity securities**	**Loans and receivables**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Sovereigns	**-**	**570,540**	**-**	**570,540**
Public sector entities	**-**	**-**	**-**	**-**
Banks and other financial institutions	**1,088,402**	**3,197,317**	**9**	**4,285,728**
Corporate entities	**2,174**	**162,617**	**-**	**164,791**
	1,090,576	**3,930,474**	**9**	**5,021,059**

	The Bank 2008			
	Available-for-sale securities	Held-to-maturity securities	Loans and receivables	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Sovereigns	-	99,997	-	99,997
Public sector entities	-	-	-	-
Banks and other financial institutions	287,385	3,426,679	77,645	3,791,709
Corporate entities	2,126	-	-	2,126
	289,511	3,526,676	77,645	3,893,832

Notes to the Financial Statements (continued)

25. Investment in securities (continued)

The movements in investment in securities are summarised as follows:

	The Group		
	2009		
	Available-for-sale securities	**Held-to-maturity securities**	**Loans and Receivables**
	HK$'000	**HK$'000**	**HK$'000**
At 1 January 2009	**328,682**	**3,526,676**	**77,645**
Additions	**870,954**	**4,029,468**	**2,482,100**
Disposals, redemptions and maturity	**(68,084)**	**(3,630,720)**	**(2,566,106)**
Amortisation	**104**	**4,587**	**6,370**
Change in fair value	**2,053**	**-**	**-**
Exchange differences	**45**	**463**	**-**
At 31 December 2009	**1,133,754**	**3,930,474**	**9**

	The Group		
	2008		
	Available-for-sale securities	Held-to-maturity securities	Loans and receivables
	HK$'000	HK$'000	HK$'000
At 1 January 2008	119,996	4,666,248	1,007,472
Additions	188,692	4,112,483	989,695
Disposals, redemptions and maturity	-	(5,176,096)	(1,955,903)
Amortisation	2,035	13,578	75,403
Change in fair value	12,187	-	-
Exchange differences	5,772	(89,537)	(39,022)
At 31 December 2008	328,682	3,526,676	77,645

Notes to the Financial Statements (continued)

25. Investment in securities (continued)

	The Bank		
	2009		
	Available-for-sale securities	**Held-to-maturity securities**	**Loans and receivables**
	HK$'000	**HK$'000**	**HK$'000**
At 1 January 2009	**289,511**	**3,526,676**	**77,645**
Additions	**870,954**	**4,029,468**	**2,482,100**
Disposals, redemptions and maturity	**(68,084)**	**(3,630,720)**	**(2,566,106)**
Amortisation	**104**	**4,587**	**6,370**
Change in fair value	**(1,954)**	**-**	**-**
Exchange differences	**45**	**463**	**-**
At 31 December 2009	**1,090,576**	**3,930,474**	**9**

	The Bank		
	2008		
	Available-for-sale securities	Held-to-maturity securities	Loans and receivables
	HK$'000	HK$'000	HK$'000
At 1 January 2008	91,333	4,666,248	1,007,472
Additions	188,692	4,112,483	989,695
Disposals, redemptions and maturity	-	(5,176,096)	(1,955,903)
Amortisation	2,035	13,578	75,403
Change in fair value	1,679	-	-
Exchange differences	5,772	(89,537)	(39,022)
At 31 December 2008	289,511	3,526,676	77,645

Available-for-sale and held-to-maturity securities are analysed as follows:

	The Group			
	2009	2008	**2009**	2008
	Available-for-sale securities		**Held-to-maturity securities**	
	HK$'000	HK$'000	**HK$'000**	HK$'000
Treasury bills	**-**	-	**570,540**	99,997
Certificates of deposit held	**580,774**	-	**396,774**	100,085
Others	**552,980**	328,682	**2,963,160**	3,326,594
	1,133,754	328,682	**3,930,474**	3,526,676

	The Bank			
	2009	2008	**2009**	2008
	Available-for-sale Securities		**Held-to-maturity securities**	
	HK$'000	HK$'000	**HK$'000**	HK$'000
Treasury bills	**-**	-	**570,540**	99,997
Certificates of deposit held	**580,774**	-	**396,774**	100,085
Others	**509,802**	289,511	**2,963,160**	3,326,594
	1,090,576	289,511	**3,930,474**	3,526,676

Notes to the Financial Statements (continued)

26. Investment in subsidiaries

	The Bank	
	2009	2008
	HK$'000	HK$'000
Unlisted shares, at cost	**3,913**	3,913
Amount due from subsidiaries (Note)	**20,351**	20,340
Amount due to subsidiaries (Note)	**(33,197)**	(30,888)
	(8,933)	(6,635)

Note: Amounts due from/to subsidiaries are unsecured, interest-free and have no fixed terms of repayment.

The following is a list of subsidiaries as at 31 December 2009:

Name	Place of incorporation	Particulars of issued share capital	Interest held	Principal activities
Chiyu Banking Corporation (Nominees) Limited	Hong Kong	1,000 shares of HK$100 each	100%	Nominee service and investment holding
Seng Sun Development Company Limited	Hong Kong	2,800 shares of HK$1,000 each	100%	Investment holding and leasing of properties to group companies
Pacific Trend Profits Corporation	The British Virgin Islands	1 share of US$1 each	100%	Investment holding
Glory Cardinal Limited	Hong Kong	2 shares of HK$1 each	*100%	Investment holding
Glister Company Limited	Hong Kong	2 shares of HK$1 each	*100%	Investment holding
Grace Charter Limited	Hong Kong	2 shares of HK$1 each	*100%	Investment holding

* Shares held indirectly by the Bank

Remarks:

All the subsidiaries listed in the above table are not included in the combined basis for regulatory purposes in respect of capital adequacy. The Bank's Hong Kong Offices and overseas branches specified by the HKMA form the combined basis for its regulatory purposes in accordance with the Banking (Capital) Rules. For accounting purposes, subsidiaries are consolidated in accordance with the accounting standards issued by the HKICPA pursuant to section 18A of the Professional Accountants Ordinance.

Notes to the Financial Statements (continued)

27. Investment properties

	The Group and the Bank	
	2009	2008
	HK$'000	HK$'000
At 1 January	**80,050**	64,450
Disposals	**(19,000)**	-
Fair value gains (Note 12)	**17,750**	2,100
Reclassification from properties, plant and equipment (Note 28)	**-**	13,500
At 31 December	**78,800**	80,050

As at 31 December 2009, investment properties are included in the consolidated balance sheet at valuation carried out at 31 December 2009 on the basis of their fair value by an independent firm of chartered surveyors, Savills Valuation and Professional Services Limited.

The carrying value of investment properties is analysed based on the remaining terms of the leases as follows:

	The Group and the Bank	
	2009	2008
	HK$'000	HK$'000
Held in Hong Kong		
On long-term lease (over 50 years)	**73,700**	74,570
Held outside Hong Kong		
On medium-term lease (10 – 50 years)	**5,100**	5,480
	78,800	80,050

Notes to the Financial Statements (continued)

28. Properties, plant and equipment

	The Group		
	Premises	Equipment, fixtures and fittings	Total
	HK$'000	HK$'000	HK$'000
Net book value at 1 January 2009	**551,790**	**32,687**	**584,477**
Additions	**-**	**4,919**	**4,919**
Disposals	**-**	**(49)**	**(49)**
Revaluation	**82,199**	**-**	**82,199**
Depreciation for the year (Note 11)	**(6,439)**	**(7,637)**	**(14,076)**
Reclassification to investment properties (Note 27)	**-**	**-**	**-**
Exchange adjustments	**-**	**(7)**	**(7)**
Net book value at 31 December 2009	**627,550**	**29,913**	**657,463**
At 31 December 2009			
Cost or valuation	**627,550**	**109,563**	**737,113**
Accumulated depreciation and impairment	**-**	**(79,650)**	**(79,650)**
Net book value at 31 December 2009	**627,550**	**29,913**	**657,463**
Net book value at 1 January 2008	541,130	30,198	571,328
Additions	-	9,600	9,600
Disposals	-	(9)	(9)
Revaluation	30,741	-	30,741
Depreciation for the year (Note 11)	(6,581)	(7,125)	(13,706)
Reclassification to investment properties (Note 27)	(13,500)	-	(13,500)
Exchange adjustments	-	23	23
Net book value at 31 December 2008	551,790	32,687	584,477
At 31 December 2008			
Cost or valuation	551,790	107,706	659,496
Accumulated depreciation and impairment	-	(75,019)	(75,019)
Net book value at 31 December 2008	551,790	32,687	584,477

The analysis of cost or valuation of the above assets is as follows:			
At 31 December 2009			
At cost	**-**	**109,563**	**109,563**
At valuation	**627,550**	**-**	**627,550**
	627,550	**109,563**	**737,113**
At 31 December 2008			
At cost	-	107,706	107,706
At valuation	551,790	-	551,790
	551,790	107,706	659,496

Notes to the Financial Statements (continued)

28. Properties, plant and equipment (continued)

	The Bank		
	Premises	Equipment, fixtures and fittings	Total
	HK$'000	HK$'000	HK$'000
Net book value at 1 January 2009	**545,590**	**32,687**	**578,277**
Additions	**-**	**4,919**	**4,919**
Disposals	**-**	**(49)**	**(49)**
Revaluation	**81,848**	**-**	**81,848**
Depreciation for the year	**(6,288)**	**(7,637)**	**(13,925)**
Reclassification to investment properties (Note 27)	**-**	**-**	**-**
Exchange adjustments	**-**	**(7)**	**(7)**
Net book value at 31 December 2009	**621,150**	**29,913**	**651,063**
At 31 December 2009			
Cost or valuation	**621,150**	**109,563**	**730,713**
Accumulated depreciation and impairment	**-**	**(79,650)**	**(79,650)**
Net book value at 31 December 2009	**621,150**	**29,913**	**651,063**
Net book value at 1 January 2008	536,130	30,198	566,328
Additions	-	9,600	9,600
Disposals	-	(9)	(9)
Revaluation	29,391	-	29,391
Depreciation for the year	(6,431)	(7,125)	(13,556)
Reclassification to investment properties (Note 27)	(13,500)	-	(13,500)
Exchange adjustments	-	23	23
Net book value at 31 December 2008	545,590	32,687	578,277
At 31 December 2008			
Cost or valuation	545,590	107,706	653,296
Accumulated depreciation and impairment	-	(75,019)	(75,019)
Net book value at 31 December 2008	545,590	32,687	578,277

	Premises	Equipment, fixtures and fittings	Total
The analysis of cost or valuation of the above assets is as follows:			
At 31 December 2009			
At cost	**-**	**109,563**	**109,563**
At valuation	**621,150**	**-**	**621,150**
	621,150	**109,563**	**730,713**
At 31 December 2008			
At cost	-	107,706	107,706
At valuation	545,590	-	545,590
	545,590	107,706	653,296

Notes to the Financial Statements (continued)

28. Properties, plant and equipment (continued)

The carrying value of premises is analysed based on the remaining terms of the leases as follows:

	The Group	
	2009	2008
	HK$'000	HK$'000
Held in Hong Kong		
On long-term lease (over 50 years)	**431,780**	360,790
On medium-term lease (10 – 50 years)	**169,770**	167,340
Held outside Hong Kong		
On long-term lease (over 50 years)	**23,500**	21,570
On medium-term lease (10 – 50 years)	**2,500**	2,090
	627,550	551,790

	The Bank	
	2009	2008
	HK$'000	HK$'000
Held in Hong Kong		
On long-term lease (over 50 years)	**431,780**	360,790
On medium-term lease (10 – 50 years)	**163,370**	161,140
Held outside Hong Kong		
On long-term lease (over 50 years)	**23,500**	21,570
On medium-term lease (10 – 50 years)	**2,500**	2,090
	621,150	545,590

As at 31 December 2009, premises are included in the consolidated balance sheet at valuation carried out at 31 December 2009 on the basis of their fair value by an independent firm of chartered surveyors, Savills Valuation and Professional Services Limited.

As a result of the above-mentioned revaluations, changes in value of the Group's and the Bank's premises were recognised in the Group's and the Bank's premises revaluation reserve and the income statement respectively as follows:

	The Group	
	2009	2008
	HK$'000	HK$'000
Increase in valuation credited to premises revaluation reserve	**82,199**	30,741

	The Bank	
	2009	2008
	HK$'000	HK$'000
Increase in valuation credited to premises revaluation reserve	**81,848**	29,391

As at 31 December 2009, the net book value of premises that would have been included in the Group's consolidated balance sheet had the assets been carried at cost less accumulated depreciation and impairment losses was HK$ 154,043,000 (2008: HK$155,607,000).

Notes to the Financial Statements (continued)

29. Other assets

	The Group and the Bank	
	2009	2008
	HK$'000	HK$'000
Repossessed assets	**-**	7,190
Accounts receivable and prepayments	**874,587**	634,404
Current tax prepaid	**31,409**	-
	905,996	641,594

30. Financial liabilities designated at fair value through profit or loss

	The Group and the Bank	
	2009	2008
	HK$'000	HK$'000
Structured deposits (Note 31)	**-**	**768,509**

The carrying amount of financial liabilities designated at fair value through profit or loss as at 31 December 2009 is less than the amount that the Group and the Bank would be contractually required to pay at maturity to the holder by HK$ Nil (2008: HK$14,979,000). The amount of change in their fair values, during the year and cumulatively, attributable to changes in credit risk is insignificant.

Notes to the Financial Statements (continued)

31. Deposits from customers

	The Group	
	2009	2008
	HK$'000	HK$'000
Current, savings and other deposit accounts (per consolidated balance sheet)	**33,817,255**	31,449,797
Structured deposits reported as financial liabilities designated at fair value through profit or loss (Note 30)	**-**	768,509
	33,817,255	32,218,306
Analysed by :		
Demand deposits and current accounts		
- corporate customers	**1,663,117**	1,602,658
- individual customers	**554,085**	332,705
	2,217,202	1,935,363
Savings deposits		
- corporate customers	**3,862,892**	2,521,612
- individual customers	**13,781,584**	10,116,034
	17,644,476	12,637,646
Time, call and notice deposits		
- corporate customers	**5,217,639**	4,733,983
- individual customers	**8,737,938**	12,142,805
	13,955,577	16,876,788
	33,817,255	31,449,797

Notes to the Financial Statements (continued)

31. Deposits from customers (continued)

	The Bank	
	2009	2008
	HK$'000	HK$'000
Current, savings and other deposit accounts (per consolidated balance sheet)	**33,851,546**	31,483,825
Structured deposits reported as financial liabilities designated at fair value through profit or loss (Note 30)	**-**	768,509
	33,851,546	32,252,334
Analysed by :		
Demand deposits and current accounts		
- corporate customers	**1,681,209**	1,620,725
- individual customers	**554,085**	332,705
	2,235,294	1,953,430
Savings deposits		
- corporate customers	**3,879,091**	2,537,573
- individual customers	**13,781,584**	10,116,034
	17,660,675	12,653,607
Time, call and notice deposits		
- corporate customers	**5,217,639**	4,733,983
- individual customers	**8,737,938**	12,142,805
	13,955,577	16,876,788
	33,851,546	31,483,825

32. Other accounts and provisions

	The Group		The Bank	
	2009	2008	**2009**	2008
	HK$'000	HK$'000	**HK$'000**	HK$'000
Dividend payable	**145,904**	501,404	**145,904**	501,404
Accruals and other payables	**1,136,586**	1,276,838	**1,136,313**	1,276,364
Provisions	**38,646**	118,567	**38,646**	118,567
	1,321,136	1,896,809	**1,320,863**	1,896,335

	The Group and the Bank	
Movement of provisions	**2009**	2008
	HK$'000	HK$'000
At 1 January	**118,567**	-
Allowance for the year, net	**184,354**	135,321
Utilised during the year	**(264,275)**	(16,754)
At 31 December	**38,646**	118,567

The provisions were primarily in relation to the Lehman Brothers minibonds related products.

Notes to the Financial Statements (continued)

33. Deferred taxation

Deferred tax is recognised in respect of the temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements in accordance with HKAS 12 "Income Taxes".

The major components of deferred tax assets and liabilities recorded in the consolidated balance sheet, and the movements during the year are as follows:

	The Group 2009					
	Accelerated tax depreciation HK$'000	**Property revaluation HK$'000**	**Losses HK$'000**	**Impairment allowance HK$'000**	**Other temporary differences HK$'000**	**Total HK$'000**
At 1 January 2009	**6,235**	**73,205**	**(366)**	**(7,189)**	**(18,502)**	**53,383**
Charged/(credited) to income statement (Note 14)	**(183)**	**2,021**	**(19)**	**871**	**12,492**	**15,182**
Charged to other comprehensive income	**-**	**10,079**	**-**	**-**	**(329)**	**9,750**
At 31 December 2009	**6,052**	**85,305**	**(385)**	**(6,318)**	**(6,339)**	**78,315**

	The Group 2008					
	Accelerated tax depreciation HK$'000	Property revaluation HK$'000	Losses HK$'000	Impairment allowance HK$'000	Other temporary differences HK$'000	Total HK$'000
At 1 January 2008	6,211	68,110	(375)	(8,115)	1,505	67,336
Charged/(credited) to income statement (Note 14)	24	1,234	9	926	(18,729)	(16,536)
Charged to other comprehensive income	-	3,861	-	-	(1,278)	2,583
At 31 December 2008	6,235	73,205	(366)	(7,189)	(18,502)	53,383

	The Bank 2009				
	Accelerated tax depreciation HK$'000	**Property revaluation HK$'000**	**Impairment allowance HK$'000**	**Other temporary differences HK$'000**	**Total HK$'000**
At 1 January 2009	**6,057**	**72,632**	**(7,189)**	**(18,502)**	**52,998**
Charged/(credited) to income statement	**(185)**	**2,020**	**871**	**12,492**	**15,198**
Charged to other comprehensive income	**-**	**10,027**	**-**	**(329)**	**9,698**
At 31 December 2009	**5,872**	**84,679**	**(6,318)**	**(6,339)**	**77,894**

	The Bank 2008				
	Accelerated tax depreciation HK$'000	Property revaluation HK$'000	Impairment allowance HK$'000	Other temporary differences HK$'000	Total HK$'000
At 1 January 2008	6,020	67,738	(8,115)	218	65,861
Charged/(credited) to income statement	37	1,235	926	(18,729)	(16,531)
Charged to other comprehensive income	-	3,659	-	9	3,668
At 31 December 2008	6,057	72,632	(7,189)	(18,502)	52,998

Notes to the Financial Statements (continued)

33. Deferred taxation (continued)

Deferred tax assets and liabilities are offset on an individual entity basis when there is a legal right to set off current tax assets against current tax liabilities and when the deferred taxation relates to the same authority. The following amounts, determined after appropriate offsetting, are shown in the consolidated balance sheet:

	The Group		The Bank	
	2009	2008	**2009**	2008
	HK$'000	HK$'000	**HK$'000**	HK$'000
Deferred tax assets	**-**	-	**-**	-
Deferred tax liabilities	**(78,315)**	(53,383)	**(77,894)**	(52,998)
	(78,315)	(53,383)	**(77,894)**	(52,998)

	The Group	
	2009	2008
	HK$'000	HK$'000
Deferred tax assets to be recovered after more than twelve months	**-**	-
Deferred tax liabilities to be settled after more than twelve months	**(84,654)**	(71,885)
	(84,654)	(71,885)

	The Bank	
	2009	2008
	HK$'000	HK$'000
Deferred tax assets to be recovered after more than twelve months	**-**	-
Deferred tax liabilities to be settled after more than twelve months	**(84,234)**	(71,499)
	(84,234)	(71,499)

The deferred tax charged for each component of other comprehensive income during the year is as follows:

	The Group	
	2009	2008
	HK$'000	HK$'000
Revaluation of premises	**10,079**	3,861
Fair value changes of available-for-sale securities	**(329)**	(1,278)
	9,750	2,583

	The Bank	
	2009	2008
	HK$'000	HK$'000
Revaluation of premises	**10,027**	3,659
Fair value changes of available-for-sale securities	**(329)**	9
	9,698	3,668

Notes to the Financial Statements (continued)

34. Share capital

	2009	2008
	HK$'000	HK$'000
Authorised:		
3,000,000 ordinary shares of HK$100 each	**300,000**	300,000
Issued and fully paid:		
3,000,000 ordinary shares of HK$100 each	**300,000**	300,000

35. Reserves

The Group's and the Bank's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity and statement of changes in equity respectively on pages 25 to 26 of the financial statements.

Notes to the Financial Statements (continued)

36. Notes to consolidated cash flow statement

(a) Reconciliation of operating profit to operating cash inflow before taxation:

	2009	2008
	HK$'000	HK$'000
Operating profit	**491,537**	712,176
Depreciation	**14,076**	13,706
Net (reversal)/ charge of loan impairment allowances	**(21,958)**	11,332
Unwind of discount on impairment	**(359)**	(464)
Advances written off net of recoveries	**3,840**	6,075
Change in cash and balances with banks and other financial institutions with original maturity over three months	**(847,993)**	205,163
Change in placements with banks and other financial institutions with original maturity over three months	**(261,340)**	1,776,722
Change in financial assets designated at fair value through profit or loss	**(423,359)**	666,665
Change in derivative financial instruments	**(8,450)**	(51,542)
Change in advances and other accounts	**(2,654,988)**	(2,571,746)
Change in investment in securities	**(658,638)**	1,773,045
Change in other assets	**(232,993)**	407,804
Change in deposits and balances of banks and other financial institutions	**(603,356)**	(13,513)
Change in financial liabilities designated at fair value through profit or loss	**(768,509)**	(1,716,683)
Change in deposits from customers	**2,367,458**	2,121,769
Change in other accounts and provisions	**(220,173)**	6,742
Exchange difference	**350**	1,863
Operating cash (outflow)/inflow before taxation	**(3,824,855)**	3,349,114
Cash flows from operating activities included:		
- Interest received	**834,855**	1,421,719
- Interest paid	**(179,740)**	(526,297)
- Dividend received	**4,616**	4,197

(b) Analysis of the balances of cash and cash equivalents

	2009	2008
	HK$'000	HK$'000
Cash and balances with banks and other financial institutions with original maturity within three months	**6,998,122**	8,444,292
Placements with banks and other financial institutions with original maturity within three months	**2,843,176**	6,300,748
Treasury bills with original maturity within three months	**570,540**	99,997
	10,411,838	14,845,037

Notes to the Financial Statements (continued)

37. Contingent liabilities and commitments

The following is a summary of the contractual amounts of each significant class of contingent liability and commitment and the corresponding aggregate credit risk weighted amount:

	2009	2008
	HK$'000	HK$'000
Direct credit substitutes	**12,718**	17,829
Transaction-related contingencies	**127,809**	155,096
Trade-related contingencies	**1,347,230**	752,804
Commitments that are unconditionally cancellable without prior notice	**732,943**	267,529
Other commitments with an original maturity of		
- up to one year	**2,273,539**	3,147,320
- over one year	**690,911**	348,611
	5,185,150	4,689,189
Credit risk weighted amount	**1,031,226**	914,754

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

38. Capital commitments

The Group and the Bank have the following outstanding capital commitments not provided for in the financial statements:

	2009	2008
	HK$'000	HK$'000
Authorised and contracted for but not provided for	**3,328**	1,665
Authorised but not contracted for	**-**	960
	3,328	2,625

The above capital commitments mainly relate to commitments to purchase computer equipment and software, and to renovate the Group's and the Bank's premises.

Notes to the Financial Statements (continued)

39. Operating lease commitments

(a) As lessee

The Group and the Bank have commitments to make the following future minimum lease payments under non-cancellable operating leases:

	2009	2008
	HK$'000	HK$'000
Land and buildings		
- not later than one year	**16,537**	19,428
- later than one year but not later than five years	**29,283**	30,900
- later than five years	**1,590**	405
	47,410	50,733

Certain non-cancellable operating leases included in the tables above were subject to renegotiation and rent adjustment with reference to market rates prevailing at specified agreed dates.

(b) As lessor

The Group and the Bank have contracted with tenants for the following future minimum lease receivables under non-cancellable operating leases:

	2009	2008
	HK$'000	HK$'000
Land and buildings		
- not later than one year	**2,545**	3,375
- later than one year but not later than five years	**478**	2,826
	3,023	6,201

The Group and the Bank lease its investment properties (Note 27) under operating lease arrangements, with leases typically for a period from one to three years. The terms of the leases generally require the tenants to pay security deposits and provide for periodic rent adjustments according to the prevailing market conditions. None of the leases includes contingent rentals.

40. Litigation

The Group is currently being served a number of claims and counterclaims by various independent parties. These claims and counterclaims are in relation to the normal commercial activities of the Group.

No material provision was made against these claims and counterclaims because the directors believe that the Group has meritorious defences against the claimants or the amounts involved in these claims are not expected to be material.

Notes to the Financial Statements (continued)

41. Segmental reporting

The Group has adopted the new HKFRS 8 "Operating Segments" effective this year. After assessing the internal financial reporting process, it was concluded that the original segments classification has already complied with the new standard.

The Group engages in many businesses in several regions. For segmental reporting purposes, information is solely provided in respect of business segments. Geographical segment information is not presented because over 90% of the Group's revenues and profits before tax and assets are derived from Hong Kong.

Information about four business segments is provided in segmental reporting. They are Personal Banking, Corporate Banking, Treasury and Investment Activities. The classification of the Group's operating segments is based on customer segment and product type.

Both Personal Banking and Corporate Banking segments provide general banking services. Personal Banking serves individual customers while Corporate Banking deals with non individual customers. The Treasury segment is responsible for managing the capital, liquidity, and the interest rate and foreign exchange positions of the Group in addition to proprietary trades. Investment Activities include the Group's holdings of premises, investment properties and equity investments. "Others" refers to those items related to the Group as a whole but independent of the other four business segments.

Revenues, expenses, assets and liabilities of any business segment mainly include items directly attributable to the segment. In relation to occupation of the Group's premises, rentals are internally charged on market rates according to the areas occupied. For management overheads, allocations are made on reasonable bases. Inter-segment funding is charged according to the internal funds transfer pricing mechanism of the Group.

Notes to the Financial Statements (continued)

41. Segmental reporting (continued)

	2009							
	Personal HK$'000	Corporate HK$'000	Treasury HK$'000	Investment HK$'000	Others HK$'000	Subtotal HK$'000	Eliminations HK$'000	Consolidated HK$'000
Net interest income/(expenses)								
- external	40,161	336,408	270,532	-	-	647,101	-	647,101
- inter-segment	70,923	(28,354)	(41,713)	(856)	-	-	-	-
	111,084	308,054	228,819	(856)	-	647,101	-	647,101
Net fees and commission income /(expenses)	173,319	85,572	(153)	-	-	258,738	-	258,738
Net trading income	30,994	8,881	(3,958)	(4)	-	35,913	-	35,913
Net loss on financial instruments designated at fair value through profit or loss	-	-	(5,098)	-	-	(5,098)	-	(5,098)
Net gain on investments in securities	-	-	-	-	-	-	-	-
Other operating income	233	533	-	30,306	-	31,072	(22,800)	8,272
Net operating income before impairment allowances	315,630	403,040	219,610	29,446	-	967,726	(22,800)	944,926
Net reversal of impairment allowances	1,378	22,168	-	-	-	23,546	-	23,546
Net operating income	317,008	425,208	219,610	29,446	-	991,272	(22,800)	968,472
Operating expenses	(209,668)	(62,863)	(6,926)	(8,981)	(211,297)*	(499,735)	22,800	(476,935)
Operating profit/(loss)	107,340	362,345	212,684	20,465	(211,297)	491,537	-	491,537
Net gain from disposal of/fair value adjustments on investment properties	-	-	-	17,740	-	17,740	-	17,740
Net loss from disposal of properties, plant and equipment	-	-	-	(1)	-	(1)	-	(1)
Profit/(loss) before taxation	107,340	362,345	212,684	38,204	(211,297)	509,276	-	509,276
Assets								
Segment assets	7,014,291	13,913,780	18,255,910	721,041	39,847	39,944,869	-	39,944,869
Liabilities								
Segment liabilities	28,711,597	6,329,210	518,806	147,321	147,810	35,854,744	-	35,854,744
Other information								
Additions of properties, plant and equipment	-	-	-	4,919	-	4,919	-	4,919
Depreciation	5,450	1,511	147	5,962	1,006	14,076	-	14,076
Amortisation of securities	-	-	11,061	-	-	11,061	-	11,061

Notes to the Financial Statements (continued)

41. Segmental reporting (continued)

	2008							
	Personal HK$'000	Corporate HK$'000	Treasury HK$'000	Investment HK$'000	Others HK$'000	Subtotal HK$'000	Eliminations HK$'000	Consolidated HK$'000
Net interest (expenses)/income								
- external	(215,919)	423,900	619,290	-	-	827,271	-	827,271
- inter-segment	494,564	(114,045)	(367,923)	(12,596)	-	-	-	-
	278,645	309,855	251,367	(12,596)	-	827,271	-	827,271
Net fees and commission income /(expenses)	171,717	74,419	(713)	-	202	245,625	-	245,625
Net trading income	32,342	24,030	(2,272)	1,058	-	55,158	-	55,158
Net gain on financial instruments designated at fair value through profit or loss	-	-	9,031	-	-	9,031	-	9,031
Net gain on investments in securities	-	-	131	-	-	131	-	131
Other operating income	726	424	-	29,957	-	31,107	(23,279)	7,828
Net operating income before impairment allowances	483,430	408,728	257,544	18,419	202	1,168,323	(23,279)	1,145,044
Net charge of impairment allowances	(967)	(12,121)	-	-	-	(13,088)	-	(13,088)
Net operating income	482,463	396,607	257,544	18,419	202	1,155,235	(23,279)	1,131,956
Operating expenses	(207,622)	(67,119)	(6,678)	(8,653)	(152,987)*	(443,059)	23,279	(419,780)
Operating profit/(loss)	274,841	329,488	250,866	9,766	(152,785)	712,176	-	712,176
Net gain from disposal of/fair value adjustments on investment properties	-	-	-	2,100	-	2,100	-	2,100
Net loss from disposal of properties, plant and equipment	-	-	-	(9)	-	(9)	-	(9)
Profit/(loss) before taxation	274,841	329,488	250,866	11,857	(152,785)	714,267	-	714,267
Assets								
Segment assets	5,940,481	11,530,931	21,088,656	644,436	6,545	39,211,049	-	39,211,049
Liabilities								
Segment liabilities	28,030,177	5,918,266	810,860	502,985	209,204	35,471,492	-	35,471,492
Other information								
Additions of properties, plant and equipment	-	-	-	9,600	-	9,600	-	9,600
Depreciation	5,568	1,346	157	6,275	360	13,706	-	13,706
Amortisation of securities	-	-	91,016	-	-	91,016	-	91,016

* Includes the expenses incurred on Lehman Brothers related products (Note 11)

Notes to the Financial Statements (continued)

42. Loans to directors and officers

Particulars of advances made to directors and officers of the Bank pursuant to section 161B of the Hong Kong Companies Ordinance are as follows:

	2009 HK$'000	2008 HK$'000
Aggregate amount of relevant loans outstanding at year end	**835**	**1,085**
Maximum aggregate amount of relevant loans outstanding during the year	**1,084**	**1,306**

43. Significant related party transactions

Related parties are those parties that have the ability to control the other party or exercise significant influence over the other party in making financial or operating decisions. Parties are also considered to be related if they are subject to common control. Related parties may be individual or other entities.

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

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

(i) General information of the parent companies

Central Huijin is the controlling entity of BOC. It is a wholly-owned subsidiary of CIC which is a wholly state-owned company engaging in foreign currency investment and management.

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

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

The Group's immediate holding company is BOCHK, which is in turn controlled by BOC.

Notes to the Financial Statements (continued)

43. Significant related party transactions (continued)

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

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

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

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

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

(b) Summary of transactions entered into during the ordinary course of business with other related parties

The aggregate income and expenses arising from related party transactions with other related parties of the Group are summarised as follows:

	2009	2008
	HK$'000	HK$'000
Income statement items:		
Interest expense	**(8,225)**	(14,631)
Insurance commission received	**9,415**	10,275
Administrative services fees paid/payable	**(4,980)**	(2,482)
Balance sheet items:		
Deposits from customers	**(1,724,015)**	(1,733,168)

Notes to the Financial Statements (continued)

43. Significant related party transactions (continued)

(c) Key management personnel

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

The key management compensation for the year ended 31 December 2009 and 2008 is detailed as follows:

	2009	2008
	HK$'000	HK$'000
Salaries and other short-term employee benefits	**5,731**	8,083

44. Currency concentrations

The following is a summary of the major foreign currency exposures arising from trading, non-trading and structural positions.

2009
Equivalent in thousand of HK$

	US Dollars	**Swiss Francs**	**Pound Sterling**	**Australian Dollars**	**New Zealand Dollars**	**Renminbi Yuan**	**Others**	**Total**
Spot assets	**11,004,206**	**22,005**	**328,319**	**1,231,432**	**716,007**	**2,471,219**	**1,504,284**	**17,277,472**
Spot liabilities	**(7,693,866)**	**(2,602)**	**(308,356)**	**(1,177,372)**	**(712,876)**	**(2,447,609)**	**(584,915)**	**(12,927,596)**
Forward purchases	**3,897,149**	**106,812**	**10,261**	**8,023**	**1,973**	**485,882**	**780,652**	**5,290,752**
Forward sales	**(6,774,645)**	**(125,015)**	**(58,126)**	**(57,980)**	**(2,720)**	**(484,160)**	**(1,697,760)**	**(9,200,406)**
Net long/(short) position	**432,844**	**1,200**	**(27,902)**	**4,103**	**2,384**	**25,332**	**2,261**	**440,222**
Net structural position	**-**	**-**	**-**	**-**	**-**	**360,314**	**-**	**360,314**

2008
Equivalent in thousand of HK$

	US Dollars	Euro	Pound Sterling	Australian Dollars	New Zealand Dollars	Renminbi Yuan	Others	Total
Spot assets	6,715,039	310,763	229,389	802,527	588,802	2,185,128	208,593	11,040,241
Spot liabilities	(6,581,930)	(312,986)	(208,112)	(771,893)	(585,682)	(2,034,826)	(708,380)	(11,203,809)
Forward purchases	506,026	15,586	8,393	6,446	1,348	382,375	519,694	1,439,868
Forward sales	(652,399)	(9,235)	(37,391)	(38,487)	(3,775)	(368,969)	(19,396)	(1,129,652)
Net long/(short) position	(13,264)	4,128	(7,721)	(1,407)	693	163,708	511	146,648
Net structural position	-	-	-	-	-	68,182	-	68,182

Notes to the Financial Statements (continued)

45. Cross-border claims

The information on cross-border claims discloses exposures to foreign counterparties on which the ultimate risk lies, and is derived according to the location of the counterparties after taking into account any transfer of risk. In general, such transfer of risk takes place if the claims are guaranteed by a party in a country, which is different from that of the counterparty, or if the claims are on an overseas branch of a bank whose head office is located in another country. Only regions constituting 10% or more of the aggregate cross-border claims are analysed by geographical areas and disclosed as follows:

	Banks	**Public sector entities**	**Others**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
At 31 December 2009				
Asia, other than Hong Kong				
- Mainland China	**6,772,000**	**307,000**	**2,005,000**	**9,084,000**
- Others	**2,730,000**	**471,000**	**411,000**	**3,612,000**
	9,502,000	**778,000**	**2,416,000**	**12,696,000**
Western Europe	**6,376,000**	**-**	**135,000**	**6,511,000**
Total	**15,878,000**	**778,000**	**2,551,000**	**19,207,000**

	Banks	Public sector entities	Others	Total
	HK$'000	HK$'000	HK$'000	HK$'000
At 31 December 2008				
Asia, other than Hong Kong				
- Mainland China	5,735,000	297,000	752,000	6,784,000
- Others	4,540,000	-	426,000	4,966,000
	10,275,000	297,000	1,178,000	11,750,000
Western Europe	8,418,000	-	7,000	8,425,000
Total	18,693,000	297,000	1,185,000	20,175,000

Notes to the Financial Statements (continued)

46. Non-bank Mainland China exposures

Non-bank counterparties are identified in accordance with the definitions set out in the prudential return "Quarterly Analysis of Loans and Advances and Provisions" issued by the HKMA. Exposures in Mainland China to non-bank counterparties at 31 December are summarised as follows:

	2009			
	On-balance sheet exposure	**Off-balance sheet exposure**	**Total exposure**	**Individually assessed impairment allowances**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Mainland China entities	**4,023,693**	**788,694**	**4,812,387**	**-**
Companies and individuals outside Mainland China where the credit is granted for use in Mainland China	**2,186,050**	**913,418**	**3,099,468**	**6,269**
Other non-bank Mainland China exposures	**462,949**	**38,310**	**501,259**	**-**
	6,672,692	**1,740,422**	**8,413,114**	**6,269**

	2008			
	On-balance sheet exposure	Off-balance sheet exposure	Total exposure	Individually assessed impairment allowances
	HK$'000	HK$'000	HK$'000	HK$'000
Mainland China entities	2,788,073	602,618	3,390,691	-
Companies and individuals outside Mainland China where the credit is granted for use in Mainland China	2,018,862	361,605	2,380,467	6,520
Other non-bank Mainland China exposures	262,572	553	263,125	-
	5,069,507	964,776	6,034,283	6,520

47. Ultimate holding company

The Group is subject to the control of the State Council of the PRC Government through CIC, its wholly-owned subsidiary Central Huijin, and BOC in which Central Huijin has controlling equity interests.

48. Approval of financial statements

The financial statements were approved and authorised for issue by the Board of Directors on 10 March 2010.

Branch Network

BRANCH (Br.)	ADDRESS	TELEPHONE
HONG KONG ISLAND		
Central Br.	78, Des Voeux Road Central, Hong Kong	2843 0187
North Point Br.	390-394, King's Road, North Point, Hong Kong	2570 6381
Wanchai Br.	325, Hennessy Road, Wanchai, Hong Kong	2572 2823
Sheung Wan Br.	Shop 3, G/F, Lee Fung Building, 315-349 Queen's Road Central, Hong Kong	2544 1678
Western Br.	443, Queen's Road West, Hong Kong	2548 2298
Quarry Bay Br.	967-967A, King's Road, Quarry Bay, Hong Kong	2811 3131
Aberdeen Br.	G/F, 138-140, Aberdeen Main Road, Aberdeen, Hong Kong	2553 0603
KOWLOON		
Hung Hom Br.	23-25, Gillies Avenue, Hung Hom, Kowloon	2362 0051
Kwun Tong Br.	42-44, Mut Wah Street, Kwun Tong, Kowloon	2343 4174
Sham Shui Po Br.	235-237, Laichikok Road, Kowloon	2789 8668
San Po Kong Br.	61-63, Hong Keung Street, San Po Kong, Kowloon	2328 5691
Yau Ma Tei Br.	117-119, Shanghai Street, Yaumatei, Kowloon	2332 2533
Castle Peak Road Br.	G/F, 226-228 Castle Peak Road, Kowloon	2720 5187
Kowloon Bay Br.	G/F, Shop 10, Kai Lok House, Kai Yip Estate, Kowloon Bay, Kowloon	2796 8968
Tokwawan Br.	G/F, Shop 11-13, 78 Tokwawan Road, Kowloon	2765 6118
Tsz Wan Shan Br.	Shop 703A, 7/F., Tsz Wan Shan Shopping Centre, 23 Yuk Wah ST., Tsz Wan Shan, Kowloon	2322 3313
NEW TERRITORIES		
Tuen Mun Yau Oi Estate Br.	Shop 103-104, G/F Restaurant Block Yau Oi Estate Tuen Mun N. T.	2452 3666
Kwai Hing Estate Br.	Shop 1, G/F, Hing Yat House, Kwai Hing Estate, Kwai Chung, N. T.	2487 3332
Tai Po Tai Wo Estate Br.	Shop 112-114, G/F., On Wo House, Tai Wo Estate, Tai Po, N. T.	2656 3386
Belvedere Garden Br.	Shop 5A, G/F., Belvedere Square, Tsuen Wan, N.T	2411 6789
Tsuen Wan Br.	Shop 1 and 1D, Level 2, Discovery Park Commercial Centre, Tsuen Wan, N.T.	2413 8111
Shatin Sui Wo Court Br.	Shop F7, Commercial Centre, Sui Wo Court, Shatin, N.T.	2601 5888
Ma On Shan Br.	Shop 313, Level 3, Ma On Shan Plaza Bayshore Tower, Ma On Shan, N.T.	2640 0733
Sheung Tak Estate Br.	Shop 238, Sheung Tak Shopping Centre, Sheung Tak Est., Tseung Kwan O, N.T.	2178 2278
THE MAINLAND OF CHINA		
Xiamen Br.	Unit 111-113, 1/F, 861 Xiahe Road, Xiamen, Fujian Province, China	(86-592) 585 7690
Xiamen Jimei Sub-Br.	No.88 Jiyuan Road Jimei Xiamen, China	(86-592) 619 3300
Fuzhou Br.	1/F, International Bldg., 210 Wusi Road, Fuzhou, Fujian Province, China	(86-591) 8781 0078