

Standard Chartered Bank (Hong Kong) Limited

Directors' Report and Consolidated Financial Statements

For the year ended 31 December 2012

Standard Chartered Bank (Hong Kong) Limited Contents

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Report of the directors

The directors have pleasure in submitting their annual report together with the audited financial statements for the year ended 31 December 2012.

Principal place of business

Standard Chartered Bank (Hong Kong) Limited (the "Bank") is a bank incorporated and domiciled in Hong Kong and has its registered office at 32/F., 4 – 4A Des Voeux Road Central, Hong Kong.

Principal activities

The Bank is a licensed bank registered under the Hong Kong Banking Ordinance. The Bank's principal activities are the provision of banking and related financial services. The principal activities and other particulars of the Bank's principal subsidiaries are set out in note 19 to the financial statements.

Financial statements

The profit of the Bank and its subsidiaries for the year ended 31 December 2012 and the state of the Bank's and its subsidiaries' affairs as at that date are set out in the financial statements on pages 5 to 125.

During the year ended 31 December 2012, the directors had declared and paid an ordinary dividend of HK\$1.6005 (2011: HK\$3.0114) per each "A" and "B" ordinary share totalling HK\$3,100 million (2011: HK\$5,833 million).

Details of the movements in reserves are set out in the consolidated statement of changes in equity.

Charitable donations

Charitable donations made by the Bank and its subsidiaries during the year amounted to HK\$8 million (2011: HK\$10 million).

Fixed assets

Details of the movements in fixed assets are set out in note 21 to the financial statements.

Share capital

There were no movements in the Bank's share capital during the year.

Directors

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

Executive directors

Benjamin Hung Pi Cheng

Ling Fou Tsong (appointed on 24 April 2012)

Tan Siew Boi

Saleem Razvi (resigned on 2 April 2012)

Report of the directors (continued)

Non-executive directors
Katherine Tsang King Suen, Chairperson
Jaspal Singh Bindra
Julian Fong Loong Choon
Janardhan Parthasarathi Cadambi (appointed on 5 April 2012)
Ma Xuezheng*
Norman Lyle*
Chan Wing Kin*
Raymond Kwok Ping Luen* (resigned on 27 July 2012)

Mr Ling Fou Tsong and Mr Janardhan Parthasarathi Cadambi were re-elected at the 2012 annual general meeting in accordance with Article 109 of the Bank's Articles of Association.

Directors' service contracts

The maximum term of appointment of independent non-executive directors is 2 years. Their remuneration is determined by the shareholders at the annual general meeting.

Directors' interests in Share Option Schemes

Certain directors of the Bank have been granted options under various share option schemes of Standard Chartered PLC, the ultimate holding company of the Bank. During the year, Jaspal Singh Bindra, Katherine Tsang King Suen, Benjamin Hung Pi Cheng, Julian Fong Loong Choon, Saleem Razvi, Ling Fou Tsong, Tan Siew Boi and Janardhan Parthasarathi Cadambi were granted options under these schemes.

Directors' rights to acquire shares

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

Directors' interests in contracts

No contract of significance to which the Bank, its holding companies, subsidiaries or fellow subsidiaries was a party and in which a director of the Bank had a material interest, subsisted at the end of the year or at any time during the year.

^{*} Independent non-executive directors

Report of the directors (continued)

Auditor

The financial statements have been audited by KPMG who will retire and, being eligible, offer themselves for re-appointment. A resolution for the re-appointment of KPMG as the auditor of the Bank is to be proposed at the forthcoming annual general meeting.

On behalf of the Board

Katherine Tsang King Suen Chairperson

Hong Kong, 5 March 2013

Independent auditor's report to the shareholders of Standard Chartered Bank (Hong Kong) Limited

(Incorporated in Hong Kong SAR with limited liability)

We have audited the consolidated financial statements of Standard Chartered Bank (Hong Kong) Limited (the "Bank") and its subsidiaries (together "the Bank and its subsidiaries") set out on pages 5 to 125, which comprise the consolidated and the bank balance sheets as at 31 December 2012, the consolidated income statement, the consolidated statement of comprehensive income, the consolidated and the bank 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 information.

Directors' responsibility for the financial statements

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

Auditor's responsibility

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

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

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

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

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Bank and of the Bank and its subsidiaries as at 31 December 2012 and of the Bank and its subsidiaries' profit and cash flows for the year then ended in accordance with International Financial Reporting Standards and with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

KPMG

Certified Public Accountants

8th Floor, Prince's Building 10 Chater Road Central, Hong Kong

5 March 2013

Consolidated income statement For the year ended 31 December 2012

(Expressed in millions of Hong Kong dollars)

	Note	2012 HK\$'M	2011 HK\$'M
Interest income	4(a)	18,349	15,200
Interest expense	4(b)	(6,052)	(3,477)
Net interest income		12,297	11,723
Fee and commission income		7,480	7,067
Fee and commission expense		(702)	(654)
Net fee and commission income	4(c)	6,778	6,413
Net trading income	4(d)	3,079	2,631
Net gains/(losses) from financial instruments designated			
at fair value through profit or loss	4(e)	188	(30)
Net gains from disposal of available-for-sale securities	5	149	307
Other operating income	4(f)	1,162	450
		11,356	9,771
		=======================================	
Total operating income		23,653	21,494
Staff costs		(6,693)	(6,272)
Premises and equipment		(1,862)	(1,343)
Others		(4,398)	(3,753)
Operating expenses	4(g)	(12,953)	(11,368)
Operating profit before impairment		10,700	10,126
Impairment charges on advances to banks and customers	6(a)	(789)	(592)
Other impairment charges	6(b)	(1,043)	(141)
Operating profit after impairment		8,868	9,393
Share of profit of associates		893	570
Profit before taxation		9,761	9,963
Taxation	7(a)	(1,523)	(1,619)
Taxation	Γ(α)		(1,013)
Profit after taxation		8,238	8,344
Attributable to:			
Equity shareholders of the Bank		8,221	8,324
Non-controlling interests		17	20
			0.044
Profit after taxation		8,238	8,344

Consolidated statement of comprehensive income For the year ended 31 December 2012

(Expressed in millions of Hong Kong dollars)

	2012 HK\$'M	2011 HK\$'M
Profit after taxation	8,238	8,344
Other comprehensive income/(losses):		
Defined benefit plans:		
 Actuarial losses 	(61)	(399)
- Related tax effect	10	65
Available-for-sale securities:		
 Changes in fair value recognised during the year 	1,115	(365)
 Changes in fair value transferred to the income statement on disposal 	(149)	(307)
 Transfer to the income statement on fair value hedged items 		
attributable to hedged risk	213	(421)
- Related tax effect	(207)	178
Cash flow hedges:		
 Changes in fair value recognised during the year 	94	113
 Transfer to the income statement on termination 		
of hedging derivatives	(16)	31
- Related tax effect	(13)	(24)
Net changes in share option equity reserve	76	10
Surplus on revaluation of buildings and leasehold land held for own use	2	_
Exchange difference		99
Other comprehensive income/(losses) for the year, net of tax	1,185	(1,020)
Total comprehensive income for the year	9,423	7,324
Attributable to:		
Shareholders of the Bank	9,406	7,304
Non-controlling interests	17	20
	9,423	7,324

Consolidated balance sheet as at 31 December 2012

(Expressed in millions of Hong Kong dollars)

	Note	2012 HK\$'M	2011 HK\$'M
Assets			
Cash and balances with banks, central banks and other financial institutions Placements with banks and other financial institutions Hong Kong SAR Government certificates of indebtedness Trading assets Financial assets designated at fair value Investment securities Advances to customers Amounts due from immediate holding company Amounts due from fellow subsidiaries Interest in associates Fixed assets Goodwill and intangible assets Current tax assets Deferred tax assets Other assets	10 11(a) 12 13 14 17 15(a) 18 20 21 22 27	20,492 143,581 32,481 28,414 3,216 174,379 408,018 58,731 20,591 7,101 23,746 1,821 13 89 17,001	21,777 136,513 31,401 35,377 4,275 135,090 389,763 50,957 17,531 6,619 10,522 1,741 3 319 11,966
Liabilities			
Hong Kong SAR currency notes in circulation Deposits and balances of banks and other financial institutions Deposits from customers Trading liabilities Financial liabilities designated at fair value Debt securities in issue Amounts due to immediate holding company Amounts due to fellow subsidiaries Current tax liabilities Deferred tax liabilities Other liabilities Subordinated liabilities	12 24 28 26 25 18 18 27 29 31	32,481 12,281 756,589 23,068 3,612 10,006 19,606 5,117 629 43 18,204 11,267	31,401 15,729 672,940 24,638 3,487 13,265 13,023 5,073 917 5 19,775 13,100
Equity			
Share capital Reserves	32 33	97 46,652	97 40,346
Shareholders' equity Non-controlling interests		46,749 22	40,443 58
		46,771	40,501
		939,674	853,854
Advances to customers Amounts due from immediate holding company Amounts due from fellow subsidiaries Interest in associates Fixed assets Goodwill and intangible assets Current tax assets Deferred tax assets Other assets Liabilities Hong Kong SAR currency notes in circulation Deposits and balances of banks and other financial institutions Deposits from customers Trading liabilities Financial liabilities designated at fair value Debt securities in issue Amounts due to immediate holding company Amounts due to fellow subsidiaries Current tax liabilities Deferred tax liabilities Other liabilities Subordinated liabilities Equity Share capital Reserves Shareholders' equity	15(a) 18 18 20 21 22 27 23 12 24 28 26 25 18 18 27 29 31	408,018 58,731 20,591 7,101 23,746 1,821 13 89 17,001 939,674 	389,76 50,95 17,53 6,61 10,52 1,74 31 11,96 853,85 31,40 15,72 672,94 24,63 3,48 13,26 13,02 5,07 91 19,77 13,10 813,35

Approved and authorised for issue by the Board of Directors on 5 March 2013.

Tsang King Suen Katherine

Hung Pi Cheng Benjamin

Chairperson

Director

Ling Fou Tsong Director Wang Wei Min Company Secretary

Balance sheet as at 31 December 2012

(Expressed in millions of Hong Kong dollars)

	Note	2012 HK\$'M	2011 HK\$'M
Assets			
Cash and balances with banks, central banks and other financial institutions Placements with banks and other financial institutions Hong Kong SAR Government certificates of indebtedness Trading assets Financial assets designated at fair value Investment securities Advances to customers Amounts due from immediate holding company Amounts due from fellow subsidiaries Amounts due from subsidiaries of the Bank Investments in subsidiaries of the Bank Interest in associates Fixed assets Goodwill and intangible assets Deferred tax assets Other assets	10 11(a) 12 13 14 17 15(a) 18 18 18 19 20 21 22 27 23	20,331 143,571 32,481 28,410 3,216 174,312 395,386 57,746 20,460 33,693 1,100 4,059 2,830 1,011 38 14,406	21,676 136,477 31,401 35,377 4,275 133,263 377,477 50,279 17,370 19,181 1,096 4,814 2,919 921 275 10,978
		933,050	847,779
Liabilities			
Hong Kong SAR currency notes in circulation Deposits and balances of banks and other financial institutions Deposits from customers Trading liabilities Financial liabilities designated at fair value Debt securities in issue Amounts due to immediate holding company Amounts due to fellow subsidiaries Amounts due to subsidiaries of the Bank Current tax liabilities Other liabilities Subordinated liabilities	12 24 28 26 25 18 18 18 29 31	32,481 11,356 755,487 23,065 3,612 10,006 19,124 5,008 2,017 596 17,205 11,267	31,401 14,734 672,425 24,638 3,487 13,265 12,366 3,602 1,891 762 18,987 13,100
Equity			
Share capital Reserves	32 33	97 41,729	97 37,024
Shareholders' equity		41,826	37,121
		933,050	847,779

Approved and authorised for issue by the Board of Directors on 5 March 2013.

Tsang King Suen Katherine

Hung Pi Cheng Benjamin

Chairperson

Director

Ling Fou Tsong

Wang Wei Min

Director

Company Secretary

Consolidated statement of changes in equity For the year ended 31 December 2012

(Expressed in millions of Hong Kong dollars)

					Attributal	ble to equity sl	hareholders of	the Bank						
-					Available-						Share			
	Share capital HK\$'M	Share premium HK\$'M	Capital redemption reserve HK\$'M	Cash flow hedge reserve HK\$'M	for-sale investment reserve HK\$'M	Revaluation reserve HK\$'M	Pension reserve HK\$'M	Exchange reserve HK\$'M	Property revaluation reserve HK\$'M	Retained profits HK\$'M	option equity reserve HK\$'M	Total HK\$'M	Non- controlling interests HK\$'M	Total HK\$'M
At 1 January 2011 Total comprehensive	97	12,477	3,804	(121)	45	146	(110)	150	-	22,190	294	38,972	69	39,041
income	_	-	-	120	(915)	-	(334)	99	-	8,324	10	7,304	20	7,324
Dividend paid Transfer to retained	-	-	-	-	-	-	-	-	-	(5,833)	-	(5,833)	(31)	(5,864)
profits -							(15)			15				
At 31 December 2011 Total comprehensive	97	12,477	3,804	(1)	(870)	146	(459)	249	-	24,696	304	40,443	58	40,501
income	_	-	-	65	972	-	(51)	121	2	8,221	76	9,406	17	9,423
Dividend paid										(3,100)		(3,100)	(53)	(3,153)
At 31 December 2012	97	12,477	3,804	64	102	146	(510)	370	2	29,817	380	46,749	22	46,771

Statement of changes in equity For the year ended 31 December 2012

(Expressed in millions of Hong Kong dollars)

					Available-			Share	
			Capital	Cash flow	for-sale			option	
	Share	Share	redemption	hedge	investment	Pension	Retained	equity	
	capital	premium	reserve	reserve	reserve	reserve	profits	reserve	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
At 1 January 2011	97	12,477	3,804	(115)	51	(143)	20,027	294	36,492
Total comprehensive income	-	-	-	114	(923)	(316)	7,624	(37)	6,462
Dividend paid							(5,833)		(5,833)
At 31 December 2011	97	12,477	3,804	(1)	(872)	(459)	21,818	257	37,121
Total comprehensive income	-	-	-	65	983	(51)	6,762	46	7,805
Dividend paid							(3,100)		(3,100)
At 31 December 2012	97	12,477	3,804	64	111	(510)	25,480	303	41,826

During the year ended 31 December 2012, the directors had declared and paid an ordinary dividend of HK\$1.6005 (2011: HK\$3.0114) per each 'A' and 'B' ordinary share totalling HK\$3,100 million (2011: HK\$5,833 million).

Consolidated cash flow statement For the year ended 31 December 2012

(Expressed in millions of Hong Kong dollars)

	Note	2012 HK\$'M	2011 HK\$'M
Operating activities			
Profit before taxation		9,761	9,963
Adjustments for:			
Impairment charges on advances to banks and customers		789	592
Advances written off net of recoveries		(845)	(682)
Unwinding of discount on loan impairment charges		(19)	(23)
Other impairment charges		1,043	141
Depreciation		753	315
Amortisation of intangible assets		85	93
Gains on disposal of fixed assets		(3)	(20)
Net losses/(gains) on revaluation of investment properties		30	(5)
Share of profit of associates		(893)	(570)
Interest expense on subordinated liabilities		355	410
Fair value (gains)/losses transferred from reserves on			
cash flow hedges		(16)	31
Exchange translation on subordinated liabilities		149	(6)
		11,189	10,239
(Increase)/decrease in operating assets:			
Placements with banks and other financial institutions			
with original maturity beyond three months		(14,097)	(5,764)
Trading assets		(5,296)	9,695
Financial assets designated at fair value		1,059	2,285
Investment securities		(28,176)	(1,235)
Gross advances to customers		(18,232)	(54,446)
Amounts due from immediate holding company and fellow subsidiaries	S	(2,032)	(10,996)
Other assets		(5,775)	(3,239)
Increase/(decrease) in operating liabilities:			
Deposits and balances of banks and other financial institutions		(3,524)	(4,047)
Deposits from customers		83,638	99,668
Debt securities in issue		(3,259)	13,265
Financial liabilities designated at fair value		125	435
Amounts due to immediate holding company and fellow subsidiaries		2,013	(13,194)
Trading liabilities		(1,569)	(11,808)
Other liabilities		(2,452)	3,324
Cash generated from operations		13,612	34,182
Income tax paid		(1,756)	(827)
Net cash generated from operating activities		11,856	33,355

Consolidated cash flow statement (continued) For the year ended 31 December 2012

(Expressed in millions of Hong Kong dollars)

	Note	2012 HK\$'M	2011 HK\$'M
Investing activities			
Dividend received from associates		104	70
Payment for purchase of an associate		(54)	_
Payment for additional investment in associates		_	(1,507)
Proceeds from disposal of a subsidiary		158	_
Payment for purchase of fixed assets		(14,036)	(7,799)
Payment for purchase of intangible assets		(165)	(115)
Proceeds from disposal of fixed assets		34	90
Proceeds from disposal of intangible assets			2
Net cash used in investing activities		(13,959)	(9,259)
Financing activities			
Payment for redemption of subordinated liabilities		(2,335)	_
Proceeds from issuance of subordinated liabilities		_	4,597
Interest paid on subordinated liabilities		(345)	(350)
Dividend paid to shareholders of the Bank		(3,100)	(5,833)
Dividend paid to non-controlling interests		(53)	(31)
Net cash used in financing activities		(5,833)	(1,617)
Net (decrease)/increase in cash and cash equivalents		(7,936)	22,479
Cash and cash equivalents at 1 January		148,525	124,308
Effect of foreign exchange		559	1,738
Cash and cash equivalents at 31 December	34	141,148	148,525
Cash flows from operating activities include:			
Interest received		17,318	14,500
Interest paid		5,184	2,731
Dividends received		25	19

Notes to the financial statements

(Expressed in millions of Hong Kong dollars)

1 Principal activities

The principal activities of Standard Chartered Bank (Hong Kong) Limited (the "Bank") and its subsidiaries (together referred to as the "Bank and its subsidiaries") are the provision of banking and related financial services.

2 Significant accounting policies

(a) Statement of compliance

These financial statements have been prepared in accordance with all applicable Hong Kong Financial Reporting Standards ("HKFRSs"), which collective term includes all applicable Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs") and Interpretations issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), accounting principles generally accepted in Hong Kong and the requirements of the Hong Kong Companies Ordinance. As HKFRSs are consistent with International Financial Reporting Standards ("IFRSs"), which collective term includes all applicable individual International Financial Reporting Standards, International Accounting Standards and Interpretations issued by the International Accounting Standards Board ("IASB"), these financial statements also comply with IFRSs.

(b) Basis of preparation of the financial statements

(i) Basis of Preparation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries made up to 31 December 2012.

The consolidated and the Bank's financial statements have been prepared under the historical cost convention, as modified by the revaluation of investment properties, available-for-sale assets, and financial assets and liabilities (including derivatives) at fair value through profit or loss.

The preparation of financial statements in conformity with adopted HKFRS/IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Bank and its subsidiaries' accounting policies. Actual results may differ from these estimates. The significant judgements made by management in applying the accounting policies and key sources of uncertainty were the same as those applied to the consolidated financial statements as at and for the year ended 31 December 2011.

The accounting policies set out below have been applied consistently across the Bank and its subsidiaries and to all periods presented in these financial statements.

(ii) Consolidated Financial Statements

During the year, the Bank had subordinated debts in issue. These subordinated debts were issued under a note issuance programme which is listed on the Stock Exchange of Hong Kong. Consequently, the Bank is required to produce consolidated financial statements in accordance with HKAS 27/IAS 27 "Consolidated and Separate Financial Statements".

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)

(c) Subsidiaries and non-controlling interests

Subsidiaries are entities controlled by the Bank and its subsidiaries. Control exists when the Bank and its subsidiaries have the power to directly or indirectly govern the financial and operating policies so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account.

An investment in a subsidiary is consolidated into the consolidated financial statements from the date that control commences until the date that control ceases. Intra-group balances and transactions and any unrealised profits arising from intra-group transactions are eliminated in full in preparing the consolidated financial statements. Unrealised losses resulting from intra-group transactions are eliminated in the same way as unrealised gains but only to the extent that there is no evidence of impairment.

Non-controlling interests represent the portion of the net assets of subsidiaries attributable to interests that are not owned by the Bank, whether directly or indirectly through subsidiaries, and in respect of which the Bank and its subsidiaries have not agreed any additional terms with the holders of those interests which would result in the Bank and its subsidiaries as a whole having a contractual obligation in respect of those interests that meet the definition of a financial liability. Non-controlling interests are presented in the consolidated balance sheet within equity, separately from equity attributable to the equity shareholders of the Bank. Non-controlling interests are presented on the face of the consolidated income statement and the consolidated statement of comprehensive income as an allocation of the total profit or loss and total comprehensive income for the year between non-controlling interests and the equity shareholders of the Bank.

Where losses applicable to the non-controlling interest exceed its interest in the equity of a subsidiary, the excess, and any further losses applicable to the non-controlling interest, are charged against the Bank and its subsidiaries' interest except to the extent that the non-controlling interest has a binding obligation to, and is able to, make additional investment to cover the losses. If the subsidiary subsequently reports profits, the Bank and its subsidiaries' are allocated all such profits until the non-controlling interest's share of losses previously absorbed by the Bank and its subsidiaries have been recovered.

In the Bank's balance sheet, its investments in subsidiaries are stated at cost less impairment losses, if any.

(d) Associates

Associates are entities in respect of which the Bank has significant influence, but not control, over the financial and operating policies and procedures. Investments in associates are accounted for using the equity method of accounting in the consolidated financial statements and are initially recognised at cost. The Bank and its subsidiaries' investment in associates includes goodwill identified on acquisition and accumulated impairment loss.

The Bank and its subsidiaries' share of its associates' post-acquisition profits or losses are recognised in the income statement, and the share of post-acquisition movements in other comprehensive income are recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment in the consolidated balance sheet. When the Bank and its subsidiaries' share of losses in an associate is equal to or exceeds its interest in the associate, including any other unsecured receivables, the Bank and its subsidiaries do not recognise further losses, unless they have incurred obligations or made payments on behalf of the associate.

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)

(d) Associates (continued)

Unrealised gains and losses on transactions between the Bank and its associates are eliminated to the extent of the Bank and its subsidiaries' interest in the associates.

In the Bank's balance sheet, investment in associates are stated at cost less impairment losses and dividends from pre-acquisition profits received prior to 1 January 2009, if any.

(e) Intangible assets

(i) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Bank and its subsidiaries' share of the net identifiable assets and contingent liabilities of the acquired subsidiary/ associate at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in "Goodwill and intangible assets". Goodwill on acquisitions of associates is included in "Interest in associates".

Goodwill included in "Goodwill and intangible assets" is tested annually for impairment and carried at cost less any accumulated impairment losses. Goodwill is allocated to cash-generating units for the purpose of impairment testing.

(ii) Acquired intangibles

At the date of acquisition of a subsidiary or associate, intangible assets which are deemed separable and that arise from contractual or other legal rights are capitalised and included within the net identifiable assets acquired. These intangible assets are initially measured at fair value, which reflects market expectations of the probability that the future economic benefits embodied in the asset will flow to the entity, and are amortised on the basis of their expected useful lives (4 to 16 years). At each balance sheet date, these assets are assessed for indicators of impairment. In the event that an asset's carrying amount is determined to be greater than its recoverable amount, the asset is written down immediately.

(iii) Computer software

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. Costs associated with the development of software are capitalised where it is probable that it will generate future economic benefits in excess of its cost. Computer software costs are amortised on the basis of expected useful life (3 to 5 years). Costs associated with maintaining software are recognised as an expense as incurred. At each balance sheet date, these assets are assessed for indicators of impairment. In the event that an asset's carrying amount is determined to be greater than its recoverable amount, the asset is written down immediately.

(f) Investment properties

Investment properties are land and buildings which are owned either to earn rental income or for long term investments or for both. Investment properties are stated in the balance sheet at fair value. Any gains or losses arising from a change in fair value or from the disposal of an investment property is recognised in the income statement.

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)

(g) Other property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and impairment, if any. Cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the 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 Bank and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Depreciation on fixed assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

- Buildings, leasehold land and leasehold improvements, are depreciated over the shorter of their estimated useful lives, being 50 years from the date of completion, and the unexpired terms of the lease.
- Equipment and motor vehicles, are depreciated over 3 to 15 years.
- Aircraft and vessels, are depreciated over 25 years.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. At each balance sheet date, these assets are assessed for indicators of impairment. In the event that an asset's carrying amount is determined to be greater than its recoverable amount, the asset is written down immediately.

Gains and losses on disposals are included in the income statement.

(h) Leases

Where the Bank and its subsidiaries are the lessees

The leases entered into by the Bank and its subsidiaries are primarily operating leases. The total payments made under operating leases are charged to the income statement on a straight-line basis over the period of the leases.

Where the Bank and its subsidiaries are the lessors

When assets are leased to customers under finance leases, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognised over the term of the lease using the net investment method (before tax), which reflects a constant periodic rate of return ignoring tax cash flows.

Assets leased to customers under operating leases are included within Fixed assets and depreciated over their estimated useful lives. Rental income on these leased assets is recognised in the income statement on a straight-line basis unless another systematic basis is more representative.

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)

(i) Financial assets and liabilities (excluding derivatives)

Financial assets are classified into the following categories: financial assets held at fair value through profit or loss, loans and receivables, and available-for-sale financial assets. Financial liabilities are classified as either held at fair value through profit or loss, or at amortised cost. Management determines the classification of the financial assets and liabilities on initial recognition or, where appropriate, at the time of reclassification.

(i) Financial assets and liabilities held at fair value through profit or loss

This category has two sub-categories: financial assets and liabilities held for trading, and those designated at fair value through profit or loss at inception. A financial asset or liability is classified as trading if acquired principally for the purpose of selling or repurchasing 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.

Financial assets and liabilities may be designated at fair value through profit or loss when:

- the designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities on a different basis, or
- a group of financial assets and/or liabilities is managed and its performance evaluated on a fair value basis, or
- assets or liabilities include embedded derivatives and such derivatives are not recognised separately.

(ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and it is expected that substantially all of the initial investment will be recovered, other than because of credit deterioration.

(iii) Available-for-sale assets

Available-for-sale assets are those non-derivative financial assets intended to be held for an indefinite period of time, which may be sold in response to liquidity requirements or changes in interest rates, exchange rates or equity prices.

(iv) Financial liabilities held at amortised cost

Financial liabilities, which include borrowings, not classified as held at fair value through profit or loss are classified as amortised cost instruments.

Initial recognition

Purchases and sales of financial assets and liabilities held at fair value through profit or loss or which are available-for-sale are initially recognised using trade date accounting (the date on which the Bank and its subsidiaries commit to purchase or sell the asset). Loans and receivables are recognised when cash is advanced to the borrowers. Other financial assets and financial liabilities are initially recognised on value date at fair value plus directly attributable transaction costs.

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)

(i) Financial assets and liabilities (excluding derivatives) (continued)

Subsequent measurement

Financial assets and liabilities held at fair value through profit or loss are subsequently carried at fair value, with gains and losses arising from changes in fair value taken directly to the income statement.

Available-for-sale financial assets are subsequently carried at fair value, with gains and losses arising from changes in fair value taken to a separate component of equity until the asset is sold, or is impaired, when the cumulative gain or loss is transferred to the income statement.

Loans and receivables are subsequently carried at amortised cost using the effective interest method.

Financial liabilities other than those held at fair value through profit or loss are subsequently stated at amortised cost, with any difference between proceeds net of directly attributable transaction costs and the redemption value recognised in the income statement over the period of the borrowings using the effective interest method.

In addition to these instruments, the carrying value of a financial instrument carried at amortised cost that is the hedged item in a qualifying fair value hedge relationship is adjusted by the fair value gain or loss attributable to the hedged risk.

Fair value of financial assets and liabilities

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

The fair values of quoted financial assets or financial liabilities in active markets are based on current prices. If the market for a financial asset or financial liability is not active, and for unlisted securities, the Bank and its subsidiaries establish 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.

Reclassifications

Reclassifications of financial assets, other than as disclosed below, or of financial liabilities between measurement categories are not permitted following their initial recognition.

Held for trading non-derivative financial assets can only be transferred out of the held at fair value through profit or loss category in the following circumstances: (i) to the available-for-sale category, where, in rare circumstances, they are no longer held for the purpose of selling or repurchasing in the near term; or (ii) to the loans and receivables category, where they are no longer held for the purpose of selling or repurchasing in the near term and they would have met the definition of a loan and receivable on initial recognition and the Bank and its subsidiaries have the intent and ability to hold the assets for the foreseeable future or until maturity.

Financial assets can only be transferred out of the available-for-sale category to the loans and receivables category, where they would have met the definition of a loan and receivable on initial recognition and the Bank and its subsidiaries have the intent and ability to hold the assets for the foreseeable future or until maturity.

Financial assets are reclassified at their fair value on the date of reclassification. For financial assets reclassified out of the available-for-sale category into loans and receivables, any gain or loss on those assets recognised in shareholders' equity prior to the date of reclassification is amortised to the income statement over the remaining life of the financial asset, using the effective interest method.

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)

(i) Financial assets and liabilities (excluding derivatives) (continued)

Renegotiated loans

Loans and receivables with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the Bank and its subsidiaries have made concessions that they would not otherwise consider. Renegotiated loans and receivables are subject to ongoing monitoring to determine whether they remain impaired or past due.

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Bank and its subsidiaries have transferred substantially all risks and rewards of ownership. Financial liabilities are derecognised when they are extinguished, i.e. when the obligation is discharged, cancelled or expires.

(j) Derivative financial instruments and hedge accounting

Derivatives are categorised as trading unless they are designated as hedging instruments.

Derivative contracts are initially recognised at fair value on the date on which they are entered into and are subsequently re-measured at their fair value. Fair values are obtained from market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models and option pricing models, as appropriate. All derivatives are carried as assets when their fair values are positive and as liabilities when their fair values are negative.

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

The method of recognising the resulting fair value gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Bank and its subsidiaries designate certain derivatives as either: (1) hedges of the fair value of recognised assets or liabilities, or commitments (fair value hedge); or, (2) hedges of highly probable future cash flows attributable to a recognised asset or liability, or a forecasted transaction (cash flow hedge). Hedge accounting is used for derivatives designated in this way provided certain criteria are met.

The Bank and its subsidiaries document, at the inception of the transaction, the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Bank and its subsidiaries also document the assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

(i) Fair value hedge

Changes in the fair value of derivatives that are designated and that qualify as fair value hedging instruments are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective interest method is used is amortised to the income statement over the period to maturity or derecognition.

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)

(j) Derivative financial instruments and hedge accounting (continued)

(ii) Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedging instruments are recognised in equity. The gain or loss relating to the ineffective portion is recognised immediately in the income statement.

Amounts accumulated in equity are recycled to the income statement in the periods in which the hedged item affects profit or loss.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

Derivatives that do not qualify for hedge accounting

Certain derivative transactions do not qualify for hedge accounting. Changes in the fair value of any derivative instruments that do not qualify for hedge accounting are recognised immediately in the income statement.

(k) Impairment of financial assets

The Bank and its subsidiaries assess at 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.

The following factors are considered in assessing objective evidence of impairment:

- whether the counterparty is in default of principal or interest payments;
- a counterparty files for bankruptcy protection (or the local equivalent) where this would avoid or delay repayment of its obligation;
- the Bank and its subsidiaries file to have the counterparty declared bankrupt or file a similar order in respect of a credit obligation;
- the Bank and its subsidiaries consent to a restructuring of the obligation, resulting in a diminished financial obligation, demonstrated by a material forgiveness of debt or postponement of scheduled payments;
- the Bank and its subsidiaries sell a credit obligation at a material credit-related economic loss; or

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)

(k) Impairment of financial assets (continued)

 there is observable data indicating that there is a measurable decrease in the estimated future cash flows of a group of financial assets, although the decrease cannot yet be identified with specific individual financial assets.

Assets carried at amortised cost

The Bank and its subsidiaries first assess whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Bank and its subsidiaries determine that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost 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 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 Bank and its subsidiaries may measure impairment on the basis of an instrument's fair value using observable market price.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable. For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e. on the basis of the Bank's grading process that considers asset type, industry, geographical location, collateral type, past-due status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

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

To the extent a loan is irrecoverable, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are credited to the income statement.

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

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)

(k) Impairment of financial assets (continued)

Available-for-sale assets

A significant or prolonged decline in the fair value of an equity security below its cost is considered, amongst other factors in determining whether the equity security is impaired. Where objective evidence of impairment exists for available-for-sale financial assets, the cumulative loss (measured as the difference between the acquisition 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. 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. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement.

(I) Offsetting financial transactions

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

(m) Fiduciary activities

The Bank and its subsidiaries commonly act as trustee and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, trusts, retirement benefit plans and other institutions. The assets and income arising thereon are excluded from these financial statements, as they are not assets and income of the Bank and its subsidiaries.

(n) Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including: cash and balances with banks, central banks and other financial institutions, trading assets, placements with banks and other financial institutions, and amounts due from immediate holding company and fellow subsidiaries.

(o) Revenue recognition

(i) Interest income and expense

Interest income and expense on available-for-sale assets, financial assets or liabilities held at amortised cost and financial assets and liabilities held at fair value through profit or loss excluding derivatives is recognised in the income statement using the effective interest rate method.

The effective interest rate 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 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 Bank and its subsidiaries estimate cash flows considering all contractual terms of the financial instrument (for example, prepayment options) but does not consider future credit losses. The calculation includes all amounts paid or received between parties to the contract that are an integral part of the effective interest rate, including transaction costs and all other premiums or discounts.

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)

(o) Revenue recognition (continued)

(i) Interest 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 at the original effective interest rate of the financial asset applied to the impaired carrying amount.

(ii) Fees and commissions

Fees and commissions are generally recognised on an accrual basis when the service has been provided or significant act performed. Loan syndication fees are recognised as revenue when the syndication has been completed and the Bank and its subsidiaries have retained no part of the loan package for itself or have retained a part at the same effective interest rate as for the other participants. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-apportioned basis.

(iii) Other income from financial assets and liabilities

Gains and losses arising from changes in the fair value of financial assets and liabilities held at fair value through profit or loss, as well as any interest receivable or payable, are included in the income statement in the period in which they arise.

Gains and losses arising from changes in the fair value of available-for-sale financial assets other than foreign exchange gains and losses from monetary items, are recognised directly in equity, until the financial asset is derecognised or impaired at which time the cumulative gain or loss previously recognised in equity is recognised in the income statement.

Dividends on equity instruments are recognised in the income statement when the Bank and its subsidiaries' right to receive payment is established.

(p) Income tax

Income tax payable on profits, based on the applicable tax law in each jurisdiction, is recognised as an expense in the period in which profits arise. The tax effects of income tax losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

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

Deferred tax assets are recognised where it is probable that future taxable profits will be available against which the temporary differences can be utilised.

Current and deferred tax relating to items which are charged or credited directly to equity, are credited or charged directly to equity and are subsequently recognised in the income statement together with the current or deferred gain or loss.

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)

(p) Income tax (continued)

Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset. Current tax assets are offset against current tax liabilities, and deferred tax assets against deferred tax liabilities if the Bank and its subsidiaries have a legally enforceable right to set off current tax assets against current tax liabilities and the following additional conditions are met:

- in the case of current tax assets and liabilities, the Bank or its subsidiaries intend either to settle
 on a net basis, or to realise the asset and settle the liability simultaneously; or
- in the case of deferred tax assets and liabilities, if they relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities for which a legal right of set off exists.

(q) Provisions

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

(r) Employee benefits

(i) Short term employee benefits

Salaries, annual bonuses, and the cost of non-monetary benefits are accrued in the year in which the associated services are rendered by employees.

(ii) Pension obligations

The Bank and its subsidiaries operate a number of defined contribution and defined benefit plans.

For defined contribution plans, the Bank and its subsidiaries pay contributions to publicly or privately administered pension insurance plans on a mandatory, contractual or voluntary basis, and such amounts are charged to operating expenses. The Bank and its subsidiaries have no further payment obligations once the contributions have been paid.

For funded defined benefit plans, the net liability recognised in the balance sheet represents the present value of the defined benefit obligations at the balance sheet date less the fair value of plan assets. The defined benefit obligations are calculated annually by independent actuaries using the projected unit method. The present value of the defined benefit obligations is determined by discounting the estimated future cash outflows using an interest rate equal to the yield on high-quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have a term to maturity approximating to the term of the related pension liability.

Actuarial gains and losses that arise are recognised in shareholders' equity and presented in the consolidated statement of other comprehensive income in the period they arise. Past service costs are recognised immediately to the extent that benefits are vested and are otherwise recognised over the average period until benefits are vested on a straight-line basis. Current service costs and any past service costs, together with the unwinding of the discount on plan liabilities, offset by the expected return on plan assets where applicable, are charged to operating expenses.

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)

(r) Employee benefits (continued)

(iii) Share-based compensation

The Group operates equity-settled share-based compensation plans in which the Bank and its subsidiaries' employees participate. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. For deferred share awards granted as part of an annual performance award, the expense is recognised over the period from the start of the period to the vesting date. For all other awards the expense is recognised over the period from the start of the date of grant to the vesting date.

For equity-settled awards, the total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example, profitability and growth targets). The fair value of equity instruments granted is based on market prices, if available, at the date of grant. In the absence of market prices, the fair value of the instruments is estimated using an appropriate valuation technique, such as a binomial option pricing model.

Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. At each balance sheet date, the Bank and its subsidiaries revise its estimates of the number of options that are expected to vest. It recognises the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment to equity over the remaining vesting period. Forfeitures prior to vesting attributable to factors other than the failure to satisfy a non-market vesting condition are treated as a cancellation and the remaining unamortised charge is debited to the income statement at the time of cancellation.

(s) Translation of foreign currencies

Foreign currency transactions are translated into Hong Kong dollars using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions, and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies, are recognised in the income statement.

Non-monetary assets and liabilities are translated at historical exchange rates if held at historical cost or year-end exchange rates if held at fair value, and the resulting foreign exchange gains and losses are recognised in either the income statement or shareholders' equity depending on the treatment of the gain or loss on the asset or liability.

The results and financial position of all foreign operations that have a functional currency different from the Bank's presentation currency are accounted for as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the balance sheet date.
- income and expenses for each income statement are translated at average exchange rates or at rates on the date of the transaction where exchange rates fluctuate significantly; and
- all resulting exchange differences are recognised as a separate component of equity.

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

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)

(t) Related parties

For the purposes of these financial statements, parties are considered to be related to the Bank and its subsidiaries if the Bank and its subsidiaries have the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Bank and its subsidiaries and the party are subject to common control or common significant influence. Related parties may be individuals (being members of key management personnel, significant shareholders and/or their close family members) or other entities and include (i) associates and joint ventures of the Group, (ii) entities which are under the significant influence of related parties of the Bank where those parties are individuals, and (iii) post-employment benefit plans which are for the benefit of employees of the Bank or of any entity that is a related party of the Bank.

(u) Segment reporting

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

(v) Sale and repurchase agreements

Where securities are sold subject to a commitment to repurchase them at a predetermined price ('repos'), they remain on the balance sheet and a liability is recorded in respect of the consideration received. Securities purchased under commitments to re-sell ('reverse repos') are not recognised on the balance sheet and the consideration paid is recorded in 'Advances to customers' or 'Placements with banks and other financial institutions' as appropriate. The difference between the sale and repurchase price is treated as interest and recognised over the life of the agreement.

Securities borrowed are not recognised in the financial statements, unless these are sold to third parties, in which case the purchase and sale are recorded with the gain or loss included in trading income.

3 Changes in accounting policies

Amendments to HKFRSs/IFRSs and new Interpretations

The HKICPA/IASB has issued several amendments to HKFRSs/IFRSs that are first effective for the current accounting period commencing 1 January 2012.

The Bank and its subsidiaries adopted the following amendments to existing accounting standards from 1 January 2012.

Amendments to HKFRS 7/IFRS 7 Financial instruments: Disclosure requires additional disclosures when an asset is transferred but is not derecognised. These amendments also require disclosure of assets that are derecognised but where the entity continues to have a continuing exposure to the asset after sale. Note 38(c) provides the disclosure with respect to transferred assets.

None of the other amendments had a material impact on the Bank and its subsidiaries' financial statements.

(Expressed in millions of Hong Kong dollars)

4 Operating profit

The operating profit for the year is stated after taking into account the following:

		2012 HK\$'M	2011 HK\$'M
(a)	Interest income		
	Interest income on listed securities	497	457
	Interest income on unlisted securities	2,240	2,501
	Other interest income	15,612	12,242
	Amount shown in the income statement	18,349	15,200
	Less: interest income arising from trading assets	(265)	(194)
	Less: interest income on financial assets designated at fair value	(161)	(166)
	Total interest income on financial assets that are		
	not measured at fair value through profit or loss	17,923	14,840

Other interest income includes interest income on unwinding of discounts on loan impairment charges of HK\$19 million (note 16) (2011: HK\$23 million), and fair value gains of HK\$16 million transferred from reserves on cash flow hedges (2011: fair value losses of HK\$31 million).

		2012 HK\$'M	2011 HK\$'M
(b)	Interest expense		
	Interest expense on customer deposits, deposits of banks, certificates of deposit issued, debt securities issued, trading		
	liabilities and financial liabilities designated at fair value	5,697	3,067
	Interest expense on subordinated liabilities	355	410
	Amount shown in the income statement	6,052	3,477
	Less: interest expense arising from trading liabilities Less: interest expense arising from financial liabilities designated	(130)	(14)
	at fair value	(38)	(7)
	Total interest expense on financial liabilities that are		
	not measured at fair value through profit or loss	5,884	3,456

(Expressed in millions of Hong Kong dollars)

4 Operating profit (continued)

		2012 HK\$'M	2011 HK\$'M
(c)	Net fee and commission income Net fee and commission income (other than amounts included in determining the effective interest rate) arising from financial assets or financial liabilities that are not held for trading or designated at fair value		
	fee and commission incomefee and commission expense	2,975 173 ————	2,866
	Net fee and commission income from trust and other fiduciary activities where the Bank and its subsidiaries hold or invest assets on behalf of its customers		
	fee and commission incomefee and commission expense	441 117 ================================	471 128
		2012 HK\$'M	2011 HK\$'M
(d)	Net trading income Gains less losses from dealing in foreign currencies Gains less losses from trading securities Gains less losses from other dealing activities	2,209 49 821	2,293 147 191
	Amount shown in the income statement	3,079	2,631
	Add: interest income arising from trading assets Less: interest expense arising from trading liabilities	265 (130)	194 (14)
	Net income from trading instruments	3,214	2,811
		2012 HK\$'M	2011 HK\$'M
(e)	Net gains/(losses) from financial instruments designated at fair value		
	Net gains/(losses) as shown in the income statement Add: interest income arising from financial assets designated at fair value Less: interest expense arising from financial liabilities designated	188 161	(30) 166
	at fair value	(38)	(7)
		<u>311</u> =	129

(Expressed in millions of Hong Kong dollars)

4 Operating profit (continued)

		2012 HK\$'M	2011 HK\$'M
(f)	Other operating income		
(1)	Rental income from operating lease assets	1,070	229
	Dividend income from listed available-for-sale securities	1	1
	Dividend income from unlisted available-for-sale securities	24	18
	Gains on disposal of fixed assets	3	20
	Net (losses)/gains on disposal of financial instruments		
	measured at amortised cost	(17)	109
	Net (losses)/gains on revaluation of investment properties (note 21)	(30)	5
	Others	111	68
		1,162	450
		=======================================	
			Restated
		2012	2011
		HK\$'M	HK\$'M
(g)	Operating expenses		
	Staff costs		
	 contributions to defined contribution plans 	188	166
	- expense in respect of the defined benefits plans (note 30(d))	17	24
	- equity-settled share-based payment expenses	457	501
	- salaries and other staff costs	6,031	5,581
	Depreciation (note 21) Premises and equipment expense, excluding depreciation	753	315
	- rental of premises	713	680
	- others	396	348
	Amortisation	000	010
	- other intangible assets (note 22)	85	93
	Auditor's remuneration	17	16
	Others	4,296	3,644
		12,953	11,368
5	Net gains from disposal of available-for-sale securities		
		2012	2011
		HK\$'M	HK\$'M
	Net gains transferred from reserves	149	307

(Expressed in millions of Hong Kong dollars)

6 Impairment charges

		2012 HK\$'M	2011 HK\$'M
(a)	Impairment charges on advances to banks and customers		
	Individual impairment provisions (note 16)	1 106	000
	additionsreleases	1,196 (76)	803 (81)
	- recoveries	(344)	(211)
		776	511
	Portfolio impairment charges (note 16)	13	81
		789	592
(b)	Other impairment charges		
	Charges for an interest in an associate	465	_
	Charges for risk participation transactions Releases for contingent liabilities	583	(7)
	(Releases)/charges relating to debt securities classified as loans and	_	(7)
	receivables	(5)	148
		1,043	141
7	Taxation in the consolidated income statement		
(a)	Taxation in the consolidated income statement represents:		
		2012	2011
		HK\$'M	HK\$'M
	Current tax	1 405	1 001
	Hong Kong profits tax Overseas taxation	1,465 46	1,321 102
	Over-provision in respect of prior years	(46)	(39)
		1,465	1,384
	Deferred tax (note 27)	C.F.	100
	Origination/reversal of temporary differences (Over)/under-provision in respect of prior years	65 (7)	190 45
	(Over, and of provision in respect of prior years		
		58	235
		1,523	1,619

The provision for Hong Kong profits tax for 2012 is calculated at 16.5% (2011: 16.5%) of the estimated assessable profits for the year. Taxation for overseas subsidiaries is charged at the appropriate current rates of taxation ruling in the relevant countries.

(Expressed in millions of Hong Kong dollars)

7 Taxation in the consolidated income statement (continued)

(b) Reconciliation between tax expenses and accounting profit at applicable tax rates:

	2012 HK\$'M	2011 HK\$'M
Profit before taxation	9,761	9,963
Notional tax on profit before taxation, calculated at		
Hong Kong profits tax rate of 16.5%	1,610	1,644
Tax effect of non-deductible expenses	165	86
Tax effect of non-taxable revenue	(209)	(154)
(Over)/under-provision in prior years	(53)	6
Tax effect of different tax rates of subsidiaries operating		
in other jurisdictions	8	32
Others	2	5
Actual tax expense	1,523	1,619

8 Directors' remuneration

Directors' remuneration disclosed pursuant to section 161 of the Hong Kong Companies Ordinance is as follows:

	Bank	
		Restated
	2012	2011
	HK\$'M	HK\$'M
Fees	1	1
Salaries and other emoluments	115	87
	116	88

9 Segmental reporting

The Bank and its subsidiaries manage its businesses using two main business segments:

- Consumer Banking which provides financial services to customers including lending and deposit taking activities, credit card facilities and investment services; and
- Wholesale Banking which provides financial services to corporations and institutions, including lending and deposit taking activities, structured finance products, syndicated loans, cash management, investment advice, distributing fixed income and equity investments, brokerage services, interbank and capital market activities and proprietary trading.

In addition, certain items which do not fall within the two main business segments, including unallocated central costs are reported in "Other Banking". Financial information is presented internally to the Bank's senior management using these three business segments.

(Expressed in millions of Hong Kong dollars)

9 Segmental reporting (continued)

The Bank and its subsidiaries comprise only one geographical segment as over 90% of the business is based in Hong Kong. Geographical segment is classified by the location of the principal operations of the subsidiary or, in the case of the Bank, the location of the branch responsible for reporting the results or advancing the funds.

(a) Segment results, assets and liabilities

Revenue and expenses are allocated to the reportable segments with reference to income generated by those segments and the expenses incurred by those segments or which otherwise arise from the depreciation or amortisation of assets attributable to those segments.

	Cons	sumer	Wholesale		Other		Inter-segment		Consolidated	
	bar	ıking	ban	nking	banking eliminations		To	otal		
	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Operating income										
 Net interest income 	6,685	5,961	6,673	6,038	(619)	(76)			12,739	11,923
- Other operating income	4,175	4,227	8,405	7,071	(6)	(17)			12,574	11,281
	10,860	10,188	15,078	13,109	(625)	(93)			25,313	23,204
Operating expenses	(5,951)	(5,442)	(6,234)	(5,502)	29	53			(12,156)	(10,891)
Operating profit before impairment	4,909	4,746	8,844	7,607	(596)	(40)			13,157	12,313
Impairment charges	(739)	(552)	(168)	(250)		(1)			(907)	(803)
Profit before taxation	4,170	4,194	8,676	7,357	(596)	(41)			12,250	11,510
Total assets	253,230	217,638	683,632	621,646	92,329	85,107	(46,660)	(42,112)	982,531	882,279
Segment liabilities	367,457	323,749	544,964	497,985	69,237	62,473	(46,660)	(42,112)	934,998	842,095

(b) Reconciliation of reportable segment revenues, profit before taxation, assets and liabilities

Revenue

	Consolidated		
	2012	2011	
	HK\$'M	HK\$'M	
Reportable segment revenue	25,313	23,204	
Income relating to Financial Market products	(1,521)	(1,025)	
Cost of free funds	208	203	
Others	(347)	(888)	
Total operating income	23,653	21,494	

(Expressed in millions of Hong Kong dollars)

9 Segmental reporting (continued)

(b) Reconciliation of reportable segment revenues, profit before taxation, assets and liabilities (continued)

	Cons	olidated
	2012 HK\$'M	2011 HK\$'M
	ΠΨΜ	ΤΠΨΙ
Profit before taxation		
Reportable segment profit before taxation	12,250	11,510
Income relating to Financial Market products	(1,521)	(1,025)
Cost of free funds	208	203
Reallocations of impairment charges	(947)	(55)
Others	(229)	(670)
Profit before taxation	9,761	9,963
	Cons	olidated
	2012	2011
	HK\$'M	HK\$'M
Assets		
Reportable segment assets	982,531	882,279
Assets of group companies not included in consolidated total assets	(2,221)	(3,264)
Others	(40,636)	(25,161)
Total assets	939,674	853,854
	=====	
	Cons	olidated
	2012	2011
	HK\$'M	HK\$'M
Liabilities		
Reportable segment liabilities	934,998	842,095
Liabilities of group companies not included in consolidated total liabilities	(1,928)	(2,701)
Others	(40,167)	(26,041)
Total liabilities	892,903	813,353

Income and profit before taxation recognised in the consolidated financial statements represent an arm's length compensation for the services provided and risks borne. For internal management reporting purposes, income and profit before taxation are allocated on a global perspective. In addition, for internal management reporting purposes, a charge is allocated to reportable segments for the use of interest-free funds.

Reportable segment assets and liabilities include assets and liabilities which are not booked on the Bank and its subsidiaries' balance sheets but which contribute to the reportable segment's income and profit before taxation.

(Expressed in millions of Hong Kong dollars)

10 Cash and balances with banks, central banks and other financial institutions

	Consolidated			Bank		
	2012	2012 2011		2011		
	HK\$'M	HK\$'M	HK\$'M	HK\$'M		
Cash in hand	1,833	1,737	1,821	1,714		
Balances with central banks	12,600	9,036	12,600	9,036		
Balances with banks and other						
financial institutions	6,059	11,004	5,910	10,926		
	20,492	21,777	20,331	21,676		

11 Placements with banks and other financial institutions

(a) Placements with banks and other financial institutions

	Cons	olidated	Bank		
	2012 2011		2012	2011	
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	
Gross placements with banks and other financial institutions					
 maturing within one month 	47,206	53,814	47,197	53,778	
 maturing between one month to one year 	95,154	81,198	95,153	81,198	
- maturing between one year to five years	1,222	1,504	1,222	1,504	
Less: impairment charges individually assessed	143,582	136,516	143,572	136,480	
(note 16(b))	(1)	(3)	(1)	(3)	
	143,581	136,513	143,571	136,477	
Of which:					
Balances under collateralised reverse					
repurchase agreements	2,362	10,771	2,362	10,771	

(b) Impaired placements with banks and other financial institutions

	Consolida	ated and Bank
	2012	2011
	HK\$'M	HK\$'M
Gross impaired advances to banks	44	64
Impairment charges – individually assessed	(1)	(3)
	43	61
Gross impaired advances to banks as a % of gross advances to banks	0.03%	0.05%

There is no collateral held against impaired advances to banks.

(Expressed in millions of Hong Kong dollars)

12 Hong Kong SAR Government certificates of indebtedness and currency notes in circulation

The Hong Kong Special Administrative Region currency notes in circulation are secured by the deposit of funds in respect of which the Government of Hong Kong Special Administrative Region certificates of indebtedness are held.

13 Trading assets

	Cons	olidated	В	ank
	2012	2011	2012	2011
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Trading securities	27,651	34,381	27,651	34,381
Placements with banks and other financial				
institutions	_	21	_	21
Advances to customers	186	185	186	185
Positive fair values of trading derivatives	577	790	573	790
	28,414	35,377	28,410	35,377
			Consolidat	ed and Bank
			2012	2011
			HK\$'M	HK\$'M
Trading securities:				
Treasury bills (including Exchange Fund Bills)			8,702	13,738
Certificates of deposit held			1,079	2,120
Debt securities			17,369	18,513
Equity securities			501	10,010
Equity 300diffied				
			27,651	34,381
Issued by:				
Central governments and central banks			24,270	30,360
Public sector entities			16	71
Banks and other financial institutions			1,446	2,956
Corporate entities			1,919	994
			27,651	34,381
By place of listing:			4.4.500	40.007
Listed in Hong Kong			14,563	13,827
Listed outside Hong Kong			3,591	2,999
			18,154	16,826
Unlisted			9,497	17,555
			27,651	34,381

(Expressed in millions of Hong Kong dollars)

14 Financial assets designated at fair value

	Consolidated and Bank	
	2012	2011
	HK\$'M	HK\$'M
Debt securities	3,216	4,275
Issued by:		
Corporate entities	3,216	4,275
By place of listing:		
Listed outside Hong Kong	2,268	3,216
Unlisted	948	1,059
	3,216	4,275

The above financial assets designated at fair value represent certain debt securities with embedded derivatives that are not separately recognised.

15 Advances to customers

(a) Advances to customers

Consolidated

	2012 HK\$'M	2011 HK\$'M
Gross advances to customers	406,222	379,110
Trade bills	2,857	11,787
	409,079	390,897
Less : Impairment charges		
- individually assessed (note 16(a))	(494)	(580)
- collectively assessed (note 16(a))	(567)	(554)
	408,018	389,763
Of which:		
Balances under collateralised reverse repurchase agreements and		
securities borrowing transactions	1,072	<u>2,327</u>

(Expressed in millions of Hong Kong dollars)

15 Advances to customers (continued)

(a) Advances to customers (continued)

Bank

		2012 HK\$'M	2011 HK\$'M
	Gross advances to customers Trade bills	393,472 2,857	366,712 11,787
	Less : Impairment charges	396,329	378,499
	individually assessed (note 16(a))collectively assessed (note 16(a))	(489) (454)	(578) (444)
		395,386	377,477
	Of which:		
	Balances under collateralised reverse repurchase agreements and securities borrowing transactions	1,072	2,327
(b)	Impaired advances to customers		
	Consolidated		
		2012 HK\$'M	2011 HK\$'M
	Gross impaired advances to customers Impairment charges – individually assessed	1,352 (494)	971 (580)
		858	391
	Gross impaired advances to customers as a % of gross advances to customers	0.33%	0.25%
	Fair value of collateral held against the covered portion of impaired advances to customers	749	577
	Covered portion of impaired advances to customers Uncovered portion of impaired advances to customers	307 1,045	249 722

(Expressed in millions of Hong Kong dollars)

15 Advances to customers (continued)

(b) Impaired advances to customers (continued)

Bank

	2012 HK\$'M	2011 HK\$'M
Gross impaired advances to customers Impairment charges – individually assessed	1,325 (489)	962 (578)
	836	384
Gross impaired advances to customers as a % of gross advances to customers	0.33%	0.25%
Fair value of collateral held against the covered portion of impaired advances to customers	729	577
Covered portion of impaired advances to customers Uncovered portion of impaired advances to customers	298 1,027	249 713

The covered portion of impaired advances to customers represents the amount of collateral held against outstanding balances. It does not include any collateral held over and above outstanding exposures.

(Expressed in millions of Hong Kong dollars)

15 Advances to customers (continued)

(c) Net investment in finance leases

Net investment in finance leases

Advances to customers include the net investment in equipment leased to customers under finance leases. The total minimum lease payments receivable under finance leases and their present values at the year end, are as follows:

Consolidated

		2012			2011	
	Present			Present		
	value of	Interest		value of	Interest	
	the minimum	income	Total	the minimum	income	Total
	lease	relating	minimum	lease	relating	minimum
	payments	to future	lease	payments	to future	lease
	receivable	periods	payments	receivable	periods	payments
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Within 1 year	7	_	7	58	2	60
After 1 year but within 5 years	_	_	_	12	1	13
After 5 years	_	_	_	1	_	1
Alter 5 years						
	7		7	71	3	74
Impairment charges:						
- individually assessed						
- individually assessed						
Net investment in finance leases	7			71		
Bank						
		2012			2011	
	Present			Present		
	value of	Interest		value of	Interest	
	the minimum	income	Total	the minimum	income	Total
	lease	relating	minimum	lease	relating	minimum
	payments	to future	lease	payments	to future	lease
	receivable	periods	payments	receivable	periods	payments
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Within 1 year	_	_	_	1	_	1
After 1 year but within 5 years	_	_	_	_	_	_
After 5 years	_	_	_	_	_	_
Titol o your						
	-			1		1
Impairment charges:						
- individually assessed						

(Expressed in millions of Hong Kong dollars)

16 Movement in impairment charges on advances to banks and customers

(a) Advances to customers

Consolidated

	2012	
Individually	Collectively	
assessed	assessed	Total
HK\$'M	HK\$'M	HK\$'M
580	554	1,134
(1,189)	_	(1,189)
344	_	344
776	13	789
(17)		(17)
494	567	1,061
	2011	
Individually	Collectively	
assessed	assessed	Total
HK\$'M	HK\$'M	HK\$'M
775	473	1,248
(893)	_	(893)
211	_	211
508	81	589
(21)		(21)
580	554	1,134
	assessed HK\$'M 580 (1,189) 344 776 (17) 494 Individually assessed HK\$'M 775 (893) 211 508 (21)	Individually assessed HK\$'M HK\$'M HK\$'M

(Expressed in millions of Hong Kong dollars)

16 Movement in impairment charges on advances to banks and customers (continued)

(a) Advances to customers (continued)

Bank

		2012	
	Individually	Collectively	
	assessed	assessed	Total
	HK\$'M	HK\$'M	HK\$'M
At 1 January 2012	578	444	1,022
Amounts written off	(889)	_	(889)
Recoveries of advances written off in previous years	294	_	294
Net charge to the income statement	523	10	533
Unwind of discount on loan impairment charges	(17)		(17)
At 31 December 2012 (note 15(a))	489	<u>454</u>	943
		2011	
	Individually	Collectively	
	assessed	assessed	Total
	HK\$'M	HK\$'M	HK\$'M
At 1 January 2011	774	374	1,148
Amounts written off	(688)	_	(688)
Recoveries of advances written off in previous years	180	_	180
Net charge to the income statement	333	70	403
Unwind of discount on loan impairment charges	(21)		(21)
At 31 December 2011 (note 15(a))	578	444	1,022

(b) Placements with banks and other financial institutions

Consolidated and Bank

	Individually assessed	
	2012	2011
	HK\$'M	HK\$'M
At 1 January	3	2
Charge to the income statement (note 6(a))	_	3
Unwind of discount on loan impairment charges (note 4(a))	(2)	(2)
At 31 December (note 11(a))	1	3

(Expressed in millions of Hong Kong dollars)

17 Investment securities

	Consolidated			Bank	
	2012	2011	2012	2011	
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	
Available-for-sale securities					
Treasury bills (including Exchange Fund Bills)	33,507	34,516	33,507	34,516	
Certificates of deposit held	31,756	23,787	31,756	23,787	
Debt securities	99,706	66,320	99,706	66,320	
Equity shares	526	423	526	423	
Less: impairment charges	(6)	(6)	(6)	(6)	
	165,489	125,040	165,489	125,040	
Lagra and receivables. Dabt accomities	0.016	10.004	0.040	0.050	
Loans and receivables – Debt securities	8,916	10,084	8,849	8,253	
Less: impairment charges	(26)	(34)	(26)	(30)	
	8,890	10,050	8,823	8,223	
	174,379	135,090	174,312	133,263	
leaved by					
Issued by: Available-for-sale securities					
Central governments and central banks	56,040	42,689	56,040	42,689	
Public sector entities	3,162	3,143	3,162	3,143	
Banks and other financial institutions	88,744	71,042	88,744	71,042	
Corporate entities	17,543	8,166	17,543	8,166	
	165,489	125,040	165,489	125,040	
Loans and receivables - Debt securities					
Banks and other financial institutions	_	1,715	_	1,715	
Corporate entities	8,890	8,335	8,823	6,508	
	8,890	10,050	8,823	8,223	
	174,379	135,090	174,312	133,263	

(Expressed in millions of Hong Kong dollars)

17 Investment securities (continued)

	Consolidated		Bank	
	2012	2011	2012	2011
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
By place of listing: Available-for-sale securities				
Listed in Hong Kong	4,581	2,540	4,581	2,540
Listed outside Hong Kong	66,327	34,104	66,327	34,104
	70,908	36,644	70,908	36,644
Unlisted	94,581	88,396	94,581	88,396
	165,489	125,040	165,489	125,040
Loans and receivables - Debt securities				
Listed outside Hong Kong	1,519	_	1,519	_
Unlisted	7,371	10,050	7,304	8,223
	8,890	10,050	8,823	8,223
	174,379	135,090	174,312	133,263

18 Amounts due from/to immediate holding company, fellow subsidiaries and subsidiaries of the Bank

During the year, the Bank and its subsidiaries entered into transactions with related parties in the ordinary course of its banking business including lending, acceptance and placement of inter-bank deposits, correspondent banking transactions, banking operation/outsourcing activities and off-balance sheet transactions.

The Bank has entered into various risk participation transactions with related companies. For funded risk participation transactions, the Bank undertakes to deposit an amount equal to the participating balances with the related companies. When there is a default, under the undertaking clause of the agreement, the Bank is obligated to honor the risk participation by transferring such deposits to the related companies.

During the year, HK\$583 million of such deposits has been transferred to the related companies. As at 31 December 2012, the amount due from group companies shown on the balance sheet is stated net of HK\$1,585 million in respect of such obligations.

(Expressed in millions of Hong Kong dollars)

18 Amounts due from/to immediate holding company, fellow subsidiaries and subsidiaries of the Bank (continued)

Consolidated

The amounts of material transactions during the year are set out below:

	Immedi	ate holding		
	company		Fellow s	subsidiaries
		Restated		Restated
	2012	2011	2012	2011
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Operating income	560	655	<u>214</u>	172
Operating expenses	1,583	1,163	569	538

The amounts due from/to immediate holding company and fellow subsidiaries stated on the consolidated balance sheet included the following:

	2	2012	2011		
	Immediate		Immediate		
	holding	Fellow	holding	Fellow	
	company	subsidiaries	company	subsidiaries	
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	
Amounts due from:					
Cash and balances with banks and other					
financial institutions	2,156	4,271	3,712	3,148	
Placements with banks and other financial					
institutions	45,952	14,585	37,190	11,708	
Trading assets					
 Unlisted debt securities 	_	_	17	_	
 Positive fair values of trading derivatives 	6,097	81	2,569	103	
Financial assets designated at fair value					
 Listed debt securities 	_	98	_	221	
Investment securities					
 Listed available-for-sale debt securities 	_	1,305	_	2,119	
Other assets					
 Positive fair values of hedging derivatives 	911	_	802	99	
- Others	3,615	251	6,667	133	
	58,731	20,591	50,957	17,531	

(Expressed in millions of Hong Kong dollars)

18 Amounts due from/to immediate holding company, fellow subsidiaries and subsidiaries of the Bank (continued)

Consolidated (continued)

		2012	2011		
	Immediate		Immediate		
	holding	Fellow	holding	Fellow	
	company	subsidiaries	company	subsidiaries	
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	
Amounts due to:					
Deposits and balances of banks and other					
financial institutions	9,681	2,995	4,767	2,024	
Deposits from customers	_	5	_	5	
Trading liabilities:					
 Negative fair values of trading derivatives 	5,642	76	3,377	12	
Financial liabilities designated at fair value:					
 Structured customer deposits 	186	_	_	_	
Debt securities in issue	_	1,144	_	1,084	
Other liabilities					
 Negative fair values of hedging derivatives 	1,654	264	1,358	16	
- Others	2,443	633	3,521	1,932	
	19,606	5,117	13,023	5,073	

The contractual amounts of contingent liabilities and commitments to the immediate holding company and fellow subsidiaries are set out below:

	2	2012		2011	
	Immediate		<i>Immediate</i>		
	holding	Fellow	holding	Fellow	
	company	subsidiaries	company	subsidiaries	
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	
Financial guarantees and other credit related					
contingent liabilities	3,529	5	11,943	108	
Loan commitments and other credit related					
commitments	1,550	50,402	2,004	41,330	

Bank

The amounts of material transactions during the year are set out below:

		te holding pany	Fellow su	ubsidiaries		idiaries e Bank
		Restated	Restated			
	2012	2011	2012	2011	2012	2011
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Operating income	551	622	223	218	1,217	1,053
Operating expenses	1,583	1,163	569	538	24	

(Expressed in millions of Hong Kong dollars)

18 Amounts due from/to immediate holding company, fellow subsidiaries and subsidiaries of the Bank (continued)

Bank (continued)

The amounts due from/to immediate holding company, fellow subsidiaries and subsidiaries of the Bank stated on the balance sheet included the following:

		2012			2011	
	Immediate holding company HK\$'M	Fellow subsidiaries HK\$'M	Subsidiaries of the Bank HK\$'M	Immediate holding company HK\$'M	Fellow subsidiaries HK\$'M	Subsidiaries of the Bank HK\$'M
Amounts due from:						
Cash and balances with banks and other						
financial institutions Placements with banks and other financial	1,255	4,195	-	3,182	3,000	-
institutions	45,952	14,584	7,998	37,190	11,708	7,311
Trading assets	,	,	,	,	,	,
- Unlisted debt securities	-	-	-	17	-	-
 Positive fair values of trading derivatives Financial assets designated at fair value 	6,093	81	-	2,566	103	_
- Listed debt securities	_	98	_	_	221	_
Investment securities						
Listed available-for-sale debt securities	-	1,305	-	-	2,119	-
Advances to customers Other assets	_	_	23,168	_	_	10,332
Positive fair values of hedging derivatives	911	_	_	802	99	_
- Others	3,535	197	2,527	6,522	120	1,538
	57,746	20,460	33,693	50,279	17,370	19,181
Amounts due to:						
Deposits and balances of banks and other						
financial institutions	9,681	2,995	722	4,767	2,024	442
Deposits from customers	-	5	171	-	5	325
Trading liabilities: - Negative fair values of trading derivatives	5.642	76	_	3,377	12	_
Financial liabilities designated at fair value:	0,042	70		0,011	12	
 Structured customer deposits 	186	_	_	_	_	_
Debt securities in issue	-	1,144	-	-	1,084	-
Other liabilities - Negative fair values of hedging derivatives	1,654	264	_	1,358	16	_
- Others	1,961	524	1,124	2,864	461	1,124
						-
	19,124	5,008	2,017	12,366	3,602	1,891

The contractual amounts of contingent liabilities and commitments to the immediate holding company, fellow subsidiaries and subsidiaries of the Bank are set out below:

	2012			2011		
	Immediate holding company HK\$'M	Fellow subsidiaries HK\$'M	Subsidiaries of the Bank HK\$'M	Immediate holding company HK\$'M	Fellow subsidiaries HK\$'M	Subsidiaries of the Bank HK\$'M
Financial guarantees and other credit related contingent liabilities Loan commitments and other credit	3,529	5	83	11,943	108	131
related commitments	1,550	50,402	14,748	2,004	41,330	21,479

837

4,059

1,646

4,814

Notes to the financial statements (continued)

Listed investment, at cost less impairment losses, if any

(Expressed in millions of Hong Kong dollars)

20

19 Investments in subsidiaries of the Bank

Investments in subsidia	aries of the Bank			
				Bank
			20 HK\$	
Unlisted shares, at cost I	ess impairment cha	arges, if any	1,10	00 1,096
The following list contain assets or liabilities of the	* *	lars of subsidiaries which	principally affe	cted the results,
Name of company	Place of incorporation	Particulars of issued and paid up capital and securities	Proportion of ownership interest held by the Bank	Principal activity
Standard Chartered APR Limited	United Kingdom	21,971,715 ordinary shares of US\$1 each	100%	Investment holdings
Standard Chartered Securities (Hong Kong) Limited	Hong Kong	1,000,000 ordinary shares of HK\$10 each	100%	Equity capital markets, corporate finance and institutional brokerage
Prime Credit Limited ("PCL")	Hong Kong	400,000 ordinary shares of HK\$100 each	100%	Provision of banking and related financial services
Standard Chartered Leasing Group Limited	Hong Kong	30,000 ordinary shares of US\$1 each	100%	Provision of leasing services
Interest in associates				
Consolidated				
			20 HK\$	
Share of net assets Goodwill Less: Impairment losses			5,84 1,71 (46	1,717
			7,10	01 6,619
Bank				
			20 HK\$	
Unlisted investments, at	cost less impairme	nt losses, if any	3,22	

(Expressed in millions of Hong Kong dollars)

20 Interest in associates (continued)

The associated companies of the Bank and its subsidiaries are:

Name of associate	Place of establishment and operation	Particulars of issued and paid up capital	Proportion of ownership interest	Principal activity
Asia Commercial Joint Stock Bank ("ACB")	Vietnam	937,696,506 ordinary shares of VND10,000 each	15%	Provision of banking and related financial services
China Bohai Bank Company Limited ("Bohai")	The People's Republic of China	13,855,000,000 ordinary shares of RMB1 each	20%	Provision of banking and related financial services
Merchant Solutions Private Limited ("MS")	Singapore	560,000 "A" shares and 440,000 "B" shares	44%	Credit card merchant acquiring business
Shenzhen Prime Credit Limited	The People's Republic of China	RMB112,660,000 ordinary shares	30%	Provision of consumer financing services

Shareholdings in associated companies include a listed investment of HK\$2,016 million (2011: HK\$2,457 million). At the balance sheet date, the investment based on quoted market prices was valued at HK\$862 million (2011: HK\$1,142 million). Impairment testing on the investment has been carried out using a value-in-use methodology resulting in an impairment charge of HK\$465 million.

The Bank and its subsidiaries' investment in ACB is less than 20% but it has been accounted for as an associate, as the Bank has representation on the Board of Directors and also through a Technical Support and Assistance Agreement, which includes the secondment of staff to ACB, is able to exercise significant influence over the company's management, financial and operating policies.

In respect of the year ended 31 December 2012, the share of the results of MS and ACB was included in these financial statements based on accounts drawn up to 30 September 2012, but taking into account any events or transactions in the subsequent period from 1 October 2012 to 31 December 2012 that would materially affect the results. Bohai's result was included in the financial statements based on accounts drawn up to 30 November 2012. The Bank and its subsidiaries have taken advantage of the provision contained in HKAS 28/IAS 28 "Investments in Associates" whereby it is permitted to include the attributable share of associates' results based on accounts drawn up to a non-coterminous period and where the difference is not greater than three months.

The Bank and its subsidiaries' unrecognised share of profits of associates for the year is HK\$12 million (2011: HK\$7 million). Where there are accumulated unrecognised share of associates' losses, subsequent profits earned are not recognised until previously unrecognised losses are extinguished. The Bank and its subsidiaries' unrecognised share of losses of associates net of unrecognised profits on a cumulative basis is HK\$66 million (2011: HK\$78 million).

(Expressed in millions of Hong Kong dollars)

20 Interest in associates (continued)

Summary of financial information of associates

	Assets HK\$'M	Liabilities HK\$'M	Equity HK\$'M	Revenue HK\$'M	Profit HK\$'M
2012					
100 per cent	615,010	584,891	30,119	20,841	4,690
Effective interest of the Bank	110.005	110.050	5.040	0.000	000
and its subsidiaries	118,905	113,056	5,849	3,689	893
	Assets	Liabilities	Equity	Revenue	Profit
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
2011					
100 per cent	439,969	414,542	25,427	16,501	3,115
Effective interest of the Bank					
and its subsidiaries	82,933	78,031	4,902	2,844	570

21 Fixed assets

Consolidated

	2012							
	Buildings and leasehold land held for own use HK\$'M	Equipment, furniture & fixtures HK\$'M	Operating lease assets HK\$'M	Sub-total HK\$'M	Investment properties HK\$'M	Total fixed assets HK\$'M		
Cost or valuation:								
At 1 January 2012	2,958	488	7,359	10,805	586	11,391		
Additions	119	67	13,843	14,029	7	14,036		
Disposals and write-offs	(54)	(115)	_	(169)	(17)	(186)		
Surplus on revaluation credited								
to property revaluation reserve	2	_	_	2	_	2		
Reclassifications	(79)	73	_	(6)	6	_		
Fair value adjustments (note 4(f))	_	_	_	_	(30)	(30)		
At 31 December 2012	2,946	513	21,202	24,661	552	25,213		
Representing:								
Cost	2,946	513	21,202	24,661	_	24,661		
Valuation	_	_	_	_	552	552		
	2,946	513	21,202	24,661	552	25,213		
Accumulated depreciation:								
At 1 January 2012	535	241	93	869	_	869		
Charge for the year (note 4(g))	96	143	514	753	_	753		
Attributable to assets sold or								
written off	(40)	(115)		(155)		(155)		
At 31 December 2012	591	269	607	1,467	_	1,467		
						<u></u>		
Net book value:								
At 31 December 2012	2,355	244	20,595	23,194	552	23,746		
	====			=====		====		

(Expressed in millions of Hong Kong dollars)

21 Fixed assets (continued)

Consolidated (continued)

	2011							
	Buildings and							
	leasehold	Equipment,	Operating					
	land held for	furniture	lease		Investment	Total		
	own use	& fixtures	assets	Sub-total	properties	fixed assets		
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M		
Cost or valuation:								
At 1 January 2011	2,862	389	_	3,251	541	3,792		
Additions	150	180	7,359	7,689	110	7,799		
Disposals and write-offs	(52)	(83)	_	(135)	(70)	(205)		
Reclassifications	(2)	2	_	_	_	(===)		
Fair value adjustments (note 4(f))	(=)	_	_	_	5	5		
Tall value adjustments (note +(i))								
At 31 December 2011	2,958	488	7,359	10,805	586	11,391		
Representing:								
Cost	2,958	488	7,359	10,805	_	10,805		
Valuation	-	_	-	-	586	586		
	2,958	488	7,359	10,805	586	11,391		
Accumulated depreciation:								
At 1 January 2011	492	197	_	689	_	689		
Charge for the year (note 4(g))	95	127	93	315	_	315		
Attributable to assets sold or								
written off	(52)	(83)	_	(135)	_	(135)		
At 31 December 2011	535	241	93	869	-	869		
Net book value:								
At 31 December 2011	2,423	247	7,266	9,936	586	10,522		

(Expressed in millions of Hong Kong dollars)

21 Fixed assets (continued)

Bank

	Buildings and		2012		
	leasehold	Equipment,			
	land held for own use	furniture & fixtures	Sub-total	Investment properties	Total fixed assets
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Cost or valuation:					
At 1 January 2012	2,694	456	3,150	531	3,681
Additions	116	48	164	_	164
Disposals and write-offs	(40)	(110)	(150)	_	(150)
Reclassifications	(71)	` 71 [′]	_	_	_
Fair value adjustments				(28)	(28)
At 31 December 2012	2,699	465	3,164	503	3,667
Representing:					
Cost	2,699	465	3,164	_	3,164
Valuation	_	-	-	503	503
	2,699	465	3,164	503	3,667
Accumulated depreciation:					
At 1 January 2012	527	235	762	_	762
Charge for the year	91	133	224	_	224
Attributable to assets sold or					
written off	(39)	(110)	(149)		(149)
At 31 December 2012	579	258	837		837
Net book value:					
At 31 December 2012	2,120	207	2,327	503	2,830

(Expressed in millions of Hong Kong dollars)

21 Fixed assets (continued)

Bank (continued)

	5 " "		2011		
	Buildings and leasehold	Equipment,			
	land held for	furniture		Investment	Total
	own use	& fixtures	Sub-total	properties	fixed assets
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Cost or valuation:					
At 1 January 2011	2,686	372	3,058	541	3,599
Additions	42	157	199	106	305
Disposals and write-offs	(32)	(75)	(107)	(106)	(213)
Reclassifications	(2)	2	_	_	_
Fair value adjustments				(10)	(10)
At 31 December 2011	2,694	456	3,150	531	3,681
Representing:					
Cost	2,694	456	3,150	_	3,150
Valuation				531	531
	2,694	456	3,150	531	3,681
Accumulated depreciation:					
At 1 January 2011	473	188	661	_	661
Charge for the year	86	122	208	_	208
Attributable to assets sold or					
written off	(32)	(75)	(107)		(107)
At 31 December 2011	527	235	762		762
Net book value:					
At 31 December 2011	2,167	221	2,388	531	2,919

(Expressed in millions of Hong Kong dollars)

21 Fixed assets (continued)

Buildings and leasehold land held for own use:

	Cons	olidated		Bank	
	2012	2011	2012	2011	
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	
Leasehold in Hong Kong, at cost					
 long-term leases 	33	33	_	_	
- medium-term leases	2,044	2,114	2,032	2,095	
- short-term leases	88	72	88	72	
	2,165	2,219	2,120	2,167	
Freehold outside Hong Kong, at cost	190	204			
	2,355	2,423	2,120	2,167	
Investment properties:					
	Cons	olidated		Bank	
	2012	2011	2012	2011	
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	
Leasehold in Hong Kong, at fair value					
- medium-term lease	8	_	_	_	
Freehold outside Hong Kong, at fair value	544	586	503	531	
	552	586	503	531	

Investment properties were revalued as at 31 December 2012 on an open market value basis. The valuation was carried out by an independent firm, CBRE Limited, which has among its staff, members of the Royal Institute of Chartered Surveyors with recent experience in the location and category of the property being valued.

Operating lease assets:

Assets leased to customers under operating leases consist of commercial aircraft and vessels. At 31 December, the total future minimum lease receivables under operating leases are as follows:

	Cons	solidated
	2012	2011
	HK\$'M	HK\$'M
Within 1 year	2,057	747
After 1 year but within 5 years	5,906	2,807
After 5 years	9,992	4,486
	17,955	8,040

(Expressed in millions of Hong Kong dollars)

22 Goodwill and intangible assets

Consolidated

	Capitalised software and other	2012	
	intangible assets HK\$'M	Goodwill HK\$'M	Total HK\$'M
Cost:			
At 1 January 2012	381	1,507	1,888
Additions	165	_	165
Disposals and write-offs	(65)		(65)
At 31 December 2012	481	1,507	1,988
Accumulated amortisation:			
At 1 January 2012	147	_	147
Charge for the year (note 4(g))	85	-	85
Attributable to intangible assets sold or written off	(65)		(65)
At 31 December 2012	167	_	167
			
Carrying amount:			
At 31 December 2012	<u>314</u>	1,507	1,821
		2011	
	Capitalised		
	software and other		
	intangible assets	Goodwill	Total
		1.11/01/11	
	HK\$'M	HK\$'M	HK\$'M
Cost:	НК\$'М		
At 1 January 2011	373	1,507	1,880
At 1 January 2011 Additions	373 115		1,880 115
At 1 January 2011	373		1,880
At 1 January 2011 Additions	373 115		1,880 115
At 1 January 2011 Additions Disposals and write-offs	373 115 (107)	1,507 - -	1,880 115 (107)
At 1 January 2011 Additions Disposals and write-offs At 31 December 2011	373 115 (107)	1,507 - -	1,880 115 (107)
At 1 January 2011 Additions Disposals and write-offs At 31 December 2011 Accumulated amortisation:	373 115 (107) ————————————————————————————————————	1,507 - -	1,880 115 (107) ————————————————————————————————————
At 1 January 2011 Additions Disposals and write-offs At 31 December 2011 Accumulated amortisation: At 1 January 2011	373 115 (107) ————————————————————————————————————	1,507 - -	1,880 115 (107)
At 1 January 2011 Additions Disposals and write-offs At 31 December 2011 Accumulated amortisation: At 1 January 2011 Charge for the year (note 4(g))	373 115 (107) ————————————————————————————————————	1,507 - -	1,880 115 (107) 1,888 159 93
At 1 January 2011 Additions Disposals and write-offs At 31 December 2011 Accumulated amortisation: At 1 January 2011 Charge for the year (note 4(g)) Attributable to intangible assets sold or written off	373 115 (107) 381 159 93 (105)	1,507 - -	1,880 115 (107) 1,888 159 93 (105)
At 1 January 2011 Additions Disposals and write-offs At 31 December 2011 Accumulated amortisation: At 1 January 2011 Charge for the year (note 4(g)) Attributable to intangible assets sold or written off	373 115 (107) 381 159 93 (105)	1,507 - -	1,880 115 (107) 1,888 159 93 (105)

(Expressed in millions of Hong Kong dollars)

22 Goodwill and intangible assets (continued)

Bank

	Capitalised software and other	2012	
	intangible assets HK\$'M	Goodwill HK\$'M	Total HK\$'M
Cost:			
At 1 January 2012	298	729	1,027
Additions	165	_	165
Disposals and write-offs	(65)		(65)
At 31 December 2012	398	729	1,127
Accumulated amortisation:			
At 1 January 2012	106	_	106
Charge for the year	75	_	75
Attributable to intangible assets sold or written off	(65)		(65)
At 31 December 2012	116	_	116
Carrying amount:			
At 31 December 2012	282	729	1,011
		2011	
	Capitalised		
	software		
	software and other		Total
	software	Goodwill HK\$'M	Total HK\$'M
Cost:	software and other intangible assets		
	software and other intangible assets		HK\$'M
Cost: At 1 January 2011 Additions	software and other intangible assets HK\$'M	HK\$'M	
At 1 January 2011	software and other intangible assets HK\$'M	HK\$'M	<i>нк\$'м</i> 1,009
At 1 January 2011 Additions	software and other intangible assets HK\$'M	HK\$'M	нк\$'М 1,009 115
At 1 January 2011 Additions Disposals and write-offs At 31 December 2011	software and other intangible assets HK\$'M 280 115 (97)	НК\$'M 729 — —	1,009 115 (97)
At 1 January 2011 Additions Disposals and write-offs At 31 December 2011 Accumulated amortisation:	software and other intangible assets HK\$'M 280 115 (97)	НК\$'M 729 — —	1,009 115 (97) 1,027
At 1 January 2011 Additions Disposals and write-offs At 31 December 2011	software and other intangible assets HK\$'M 280 115 (97)	НК\$'M 729 — —	1,009 115 (97)
At 1 January 2011 Additions Disposals and write-offs At 31 December 2011 Accumulated amortisation: At 1 January 2011	software and other intangible assets HK\$'M 280 115 (97) 298	НК\$'M 729 — —	1,009 115 (97) 1,027
At 1 January 2011 Additions Disposals and write-offs At 31 December 2011 Accumulated amortisation: At 1 January 2011 Charge for the year	software and other intangible assets HK\$'M 280 115 (97) 298	НК\$'M 729 — —	1,009 115 (97) 1,027
At 1 January 2011 Additions Disposals and write-offs At 31 December 2011 Accumulated amortisation: At 1 January 2011 Charge for the year Attributable to intangible assets sold or written off	software and other intangible assets HK\$'M 280 115 (97) 298 123 80 (97)	НК\$'M 729 — —	1,009 115 (97) 1,027 1,027
At 1 January 2011 Additions Disposals and write-offs At 31 December 2011 Accumulated amortisation: At 1 January 2011 Charge for the year Attributable to intangible assets sold or written off	software and other intangible assets HK\$'M 280 115 (97) 298 123 80 (97)	НК\$'M 729 — —	1,009 115 (97) 1,027 1,027

(Expressed in millions of Hong Kong dollars)

22 Goodwill and intangible assets (continued)

Impairment tests for cash-generating units containing goodwill

Goodwill is allocated to the Bank and its subsidiaries' cash-generating units ("CGUs") as follows:

	Consolidated		Bank	
	2012	2011	2012	2011
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Lending	611	611	611	611
Private Banking	118	118	118	118
Standard Chartered Securities (Hong Kong) Limited	253	253	_	_
Prime Credit Limited ("PCL")	525	525		
	1,507	1,507	729	729

The recoverable amounts of the CGUs are determined based on value in use calculations. The key assumptions and approach to determining value in use calculations, as set out below, are solely estimates for the purpose of assessing impairment on acquired goodwill. These calculations use cash flow projections based on budgets and forecasts approved by management covering one year and extrapolated for a further 19 years using steady growth rates of 4.2 per cent (2011: 4.3 per cent).

In assessing impairment of goodwill, the Bank and its subsidiaries assumed growth at a steady rate in line with long-term forecast GDP growth. A discount rate of 11.8 per cent (2011: 18.0 per cent) was used.

23 Other assets

	Consolidated		Bank	
	2012	2011	2012	2011
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Prepayments and accrued income	3,012	2,480	2,921	2,306
Sundry debtors	3,190	2,222	2,965	1,990
Acceptances and endorsements	4,839	4,777	4,839	4,777
Positive fair values of hedging derivatives	_	56	_	56
Unsettled trades and others	5,960	2,431	3,681	1,849
	17,001	11,966	14,406	10,978

(Expressed in millions of Hong Kong dollars)

24 Deposits from customers

		Consolidated		Bank	
		2012	2011	2012	2011
		HK\$'M	HK\$'M	HK\$'M	HK\$'M
0.	www.nt.aaaa.unta	101 101	06 500	101 101	06 500
	urrent accounts	101,131	96,528	101,131	96,528
	avings accounts	373,620	318,359	373,620	318,359
	me, call and notice deposits	257,669	252,626	256,567	252,111
De	eposits and balances of central banks	24,169	5,427	24,169	5,427
		756,589	672,940	755,487	672,425
25 De	ebt securities in issue				
				Consolida	ted and Bank
				2012	2011
				HK\$'M	HK\$'M
Ce	ertificates of deposit, measured at amortised co	st		10,006	13,265
26 Fir	nancial liabilities designated at fair value				
				Consolida	ted and Bank
				2012	2011
				HK\$'M	HK\$'M
Stı	ructured customer deposits			3,574	2,615
De	ebt securities issued			38	872
				2 612	2 197
				=======================================	
Ce 26 Fir Str	ertificates of deposit, measured at amortised co nancial liabilities designated at fair value cructured customer deposits	st		2012 HK\$'M 10,006 ——————————————————————————————————	20 HK\$ 13,26 ted and Bar 20 HK\$

The Bank designates certain financial liabilities at fair value where either the liabilities:

- have fixed rates of interest and interest rate swaps or other interest related derivatives have been transacted with the intention of significantly reducing interest rate risk; or
- are exposed to equity price risk or foreign currency risk and derivatives have been transacted with the intention of significantly reducing exposure to market changes;

At 31 December 2012, the contractual amount payable at maturity of these financial liabilities exceeded the carrying amount by HK\$30 million (2011: HK\$56 million). This change is attributable to changes in market rates.

(Expressed in millions of Hong Kong dollars)

27 Taxation in the balance sheet

Deferred tax assets and liabilities:

The components of gross deferred tax (assets)/liabilities recognised in the balance sheet and the movements during the year are as follows:

Consolidated

	Depreciation allowances in excess of related depreciation HK\$'M	Impairment losses on financial assets HK\$'M	Available- for-sale securities HK\$'M	Others HK\$'M	Total HK\$'M
Deferred tax arising from:					
At 1 January 2012	53	(103)	(167)	(97)	(314)
Charge/(release) to income statement					
(note 7(a))	168	2	_	(112)	58
Charge to reserves	_	_	207	3	210
At 31 December 2012	221	(101)	40	(206)	(46)
			2011		
At 1 January 2011	(3)	(78)	11	(263)	(333)
Charge/(release) to income statement	(0)	(10)		(200)	(000)
(note 7(a))	56	(25)	_	204	235
Release to reserves	_	(20)	(178)	(41)	(219)
Others	_	_	()	3	3
At 31 December 2011	53	(103)	(167)	(97)	(314)
ACOT DOGGINDOL ZOTT		(100)	(101)	(51)	(-110)

(Expressed in millions of Hong Kong dollars)

27 Taxation in the balance sheet (continued)

Deferred tax assets and liabilities (continued):

The components of gross deferred tax (assets)/liabilities recognised in the balance sheet and the movements during the year are as follows: (continued)

Bank

	Depreciation allowances in excess of related depreciation HK\$'M	Impairment losses on financial assets HK\$'M	Available- for-sale securities HK\$'M	Others HK\$'M	Total HK\$'M
Deferred tax arising from:					
At 1 January 2012	12	(74)	(167)	(46)	(275)
Charge/(release) to income statement	17	(1)	_	11	27
Charge to reserves			207	3	210
At 31 December 2012	29	(75)	40	(32)	(38)
			2011		
At 1 January 2011	(3)	(62)	11	(258)	(312)
Charge/(release) to income statement	15	(12)	_	252	255
Release to reserves			(178)	(40)	(218)
At 31 December 2011	12	(74)	(167)	(46)	(275)
		Consoli	dated	Ва	ank
		2012	2011	2012	2011
		HK\$'M	HK\$'M	HK\$'M	HK\$'M
Analysed by:					
Net deferred tax asset recognised on the balance sheet	ne	(89)	(319)	(38)	(275)
Net deferred tax liability recognised on	the				
balance sheet	_	43			
	_	(46)	(314)	(38)	(275)

(Expressed in millions of Hong Kong dollars)

28 Trading liabilities

29

	Conso	olidated	Б	Bank
	2012	2011	2012	2011
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Short positions in securities	22,229	23,855	22,229	23,855
Negative fair values of trading derivatives	839	783	836	783
	23,068	24,638	23,065	24,638
Other liabilities				
	Conso	olidated	Б	Bank
	2012	2011	2012	2011
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Accruals and deferred income	5,014	4,372	4,603	3,960
Provision for liabilities and charges	230	1,082	230	1,082
Acceptances and endorsements	4,839	4,777	4,839	4,777
Unsettled trades and others	8,121	9,544	7,533	9,168
	18,204	19,775	17,205	18,987

30 Employee retirement benefits

The Bank and its subsidiaries made contributions to two defined benefit retirement schemes, namely Standard Chartered Bank Hong Kong Retirement Scheme ("SCB Scheme") and Cazenove Hong Kong Retirement Scheme ("Cazenove Scheme") which covered 16% (2011: 18%) of the Bank and its subsidiaries' employees. The schemes are administered by trustees, with the assets held separately from those of the Bank and its subsidiaries.

In December 2011, the Bank closed the Cazenove Scheme. Members' benefits accrued under the Cazenove Scheme were transferred to the SCB Scheme in December 2011. The assets under the Cazenove Scheme were redeemed and also transferred to the SCB Scheme in December 2011.

(a) The amounts recognised in the consolidated balance sheet are as follows:

	SCR	Scheme	Cazenove Scheme
	2012	2011	2011
	HK\$'M	HK\$'M	HK\$'M
Fair value of plan assets	2,069	1,906	_
Present value of wholly or partly funded obligations	(2,309)	(2,129)	
Net liability recognised in the balance sheet (included in			
"Other liabilities")	(240)	(223)	

(Expressed in millions of Hong Kong dollars)

30 Employee retirement benefits (continued)

(b) Movements in the present value of the defined benefit obligations:

	SCB S	Scheme	Cazenove Scheme
	2012	2011	2011
	HK\$'M	HK\$'M	HK\$'M
At the beginning of the year	2,129	1,807	56
Current service cost	106	96	5
Interest cost	30	46	2
Benefits paid	(135)	(110)	(2)
Actuarial losses	179	222	7
Transfer in/(out)		68	(68)
At the end of the year	2,309	2,129	_

(c) Movements in the fair value of plan assets:

	SCB Sc	cheme	Cazenove Scheme
	2012	2011	2011
	HK\$'M	HK\$'M	HK\$'M
At the beginning of the year	1,906	1,927	75
Contributions	61	57	4
Expected return on assets	119	120	5
Benefits paid	(135)	(110)	(2)
Actuarial gains/(losses) on plan assets	118	(159)	(11)
Transfer in/(out)		71	(71)
At the end of the year	2,069	1,906	

(d) Movements in the net (liabilities)/assets recognised in the consolidated balance sheet are as follows:

	SCB	Scheme	Cazenove Scheme
	2012	2011	2011
	HK\$'M	HK\$'M	HK\$'M
At the beginning of the year	(223)	120	19
Contributions	61	57	4
Expense recognised in the income statement (note 4(g))	(17)	(22)	(2)
Actuarial losses to pension reserve	(61)	(381)	(18)
Transfer in/(out)		3	(3)
At the end of the year	(240)	(223)	

As at 31 December 2012, the Scheme did not invest in the Bank's own financial instruments and properties (2011: HK\$Nil). The Bank expects to contribute approximately HK\$62 million to the SCB Scheme in 2013.

The total cumulative amount of actuarial gains and losses recognised directly in consolidated other comprehensive income to date is a loss of HK\$610 million (2011: loss of HK\$549 million).

(Expressed in millions of Hong Kong dollars)

30 Employee retirement benefits (continued)

(e) The expense recognised in the consolidated income statement for the year is as follows:

	SCB S	cheme	Cazenove Scheme
	2012	2011	2011
	HK\$'M	HK\$'M	HK\$'M
Current service cost	106	96	5
Interest cost	30	46	2
Actuarial expected return on plan assets	(119)	(120)	(5)
	17	22	2

The actual return on plan assets (taking into account all changes in the fair value of plan assets) was a net income of HK\$237 million (2011: net losses of HK\$45 million (restated)).

(f) The principal actuarial assumptions used in the valuation are as follows:

	SCB S	cheme	Cazenove Scheme
	2012	2011	2011
	HK\$'M	HK\$'M	HK\$'M
Discount rate	0.70%	1.50%	1.50%
Expected rate of return on plan assets	6.50%	6.50%	6.50%
Future salary increases	3.50%	3.50%	3.50%

The expected return is based on market expectations at the beginning of the year, for the return net of administration costs, over the entire life of the related obligations.

(g) The major categories of assets as a percentage of total assets are as follows:

	SCR	Scheme	Cazenove Scheme
	2012	2011	2011
	HK\$'M	HK\$'M	HK\$'M
Equities	52%	47%	_
Bonds	45%	46%	_
Cash	3%	7%	
	100%	100%	

(h) Amounts for the current and previous years

SCB Scheme

	2012	2011	2010	2009	2008
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Fair value of plan assets Present value of defined benefit obligations	2,069	1,906	1,927	1,799	1,467
	(2,309)	(2,129)	(1,807)	(1,712)	(1,890)
Net (deficit)/surplus	(240)	(223)	120	87	(423)
Experience gains/(losses) on scheme assets Experience gains/(losses) on scheme liabilities	118	(159)	36	261	(623)
	(59)	(70)	(50)	(9)	(57)

(Expressed in millions of Hong Kong dollars)

30 Employee retirement benefits (continued)

(h) Amounts for the current and previous years (continued)

Cazenove Scheme

	2011 HK\$'M	2010 HK\$'M	30 January to 31 December 2009 HK\$'M
Fair value of plan assets Present value of defined benefit obligations		75 (56)	70 (54)
Net surplus/(deficit)		19	16
Experience (losses)/gains on scheme assets Experience (losses)/gains on scheme liabilities	(11) (2)	- 1	13 7
Subordinated liabilities			

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	Consolidated and Ba	
	2012	2011
	HK\$'M	HK\$'M
US\$300 million Floating Rate Step-Up Notes 2017 ⁽¹⁾	_	2,330
US\$750 million 5.875% Fixed Rate Notes 2020 ⁽²⁾	6,565	6,427
SGD750 million 4.15% Fixed Rate Notes 2021 ⁽³⁾	4,702	4,343
	11,267	13,100

All subordinated liabilities are unsecured and subordinated to the claims of other creditors.

- Interest rate at three-months US dollar LIBOR plus 0.25 per cent, payable quarterly, to the call option date on 13 April 2012. Thereafter, it will be reset to three-months US dollar LIBOR plus 0.75 per cent, payable quarterly. The Bank exercised its option to redeem the Notes in full on 13 April 2012.
- Interest rate at 5.875 per cent per annum, payable semi-annually, to the maturity date on 24 June
- Interest rate at 4.15 per cent per annum, payable semi-annually, to the maturity date on 27 October 2021.

32 Share capital

	2012 and 2011	
	No. of shares	
	in millions	HK\$'M
Authorised:		
'A' ordinary shares of HK\$0.05 each	780	39
'B' ordinary shares of HK\$0.05 each	1,231	62
	2,011	101
Preference shares of HK\$1.00 each	3,800	3,800
	5,811	3,901

(Expressed in millions of Hong Kong dollars)

32 Share capital (continued)

	2012 and 2011	
	No. of shares	
	in millions	HK\$'M
Issued and fully paid:		
'A' ordinary shares of HK\$0.05 each	706	35
'B' ordinary shares of HK\$0.05 each	1,231	62
	1,937	97
Preference shares of HK\$1.00 each	_	_
	1,937	97

The preference shares bear a non-cumulative preferential dividend at a rate of 8.25% per annum on their nominal amount and rank in priority to the 'A' ordinary shares and the 'B' ordinary shares with respect to the payment of dividends and any return of capital. The 'B' ordinary shares rank in priority to the 'A' ordinary shares with respect to any return of capital.

33 Reserves

Nature and purpose of reserves

(i) Share premium

The application of the share premium account is governed by Section 48B of the Hong Kong Companies Ordinance.

(ii) Capital redemption reserve

The capital redemption reserve represents the repurchase of the Bank's own shares.

(iii) Available-for-sale investment reserve

The available-for-sale investment reserve comprises the cumulative net change in the fair value of available-for-sale securities held at the balance sheet date and is dealt with in accordance with the accounting policy in note 2(i).

(iv) Cash flow hedge reserve

The cash flow hedge reserve comprises the effective portion of the cumulative net change in the fair value of hedging instruments used in cash flow hedges pending subsequent recognition of the hedged cash flow in accordance with the accounting policy adopted for cash flow hedges in note 2(j).

(v) Pension reserve

The pension reserve comprises the cumulative net effect of the actuarial gains and losses for the defined benefit plan.

(Expressed in millions of Hong Kong dollars)

33 Reserves (continued)

Nature and purpose of reserves (continued)

(vi) Exchange reserve

The exchange reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations. The reserve is dealt with in accordance with the accounting policy set out in note 2(s).

(vii) Revaluation reserve

The revaluation reserve comprises the share of the change in fair value of an associate's identifiable net assets prior to the Bank and its subsidiaries obtaining significant influence in a step-acquisition.

(viii) Share option equity reserve

The Group operates equity-settled share-based compensation plans in which the Bank and its subsidiaries' employees participate. The fair value of the employee services received in exchange for the grant of the share awards is recognized as an expense with the corresponding amount credited to the share option equity reserve.

(ix) Property revaluation reserve

The property revaluation reserve represents the revaluation surplus arising upon the reclassification of a property previously included in "Buildings and leasehold land held for own use" to "investment properties".

The HKMA requires the Bank and its subsidiaries to maintain a minimum level of impairment allowances which is in excess of the impairment allowances required under Hong Kong Financial Reporting Standards. Of the retained earnings as at 31 December 2012, an amount of HK\$5,561 million (2011: HK\$5,309 million) has been reserved for this purpose.

34 Cash and cash equivalents

(a)

	2012 HK\$'M	2011 HK\$'M
Components of cash and cash equivalents in the cash		
flow statement		
Cash and balances with banks, central banks and		
other financial institutions	20,492	21,777
Trading assets with original maturity within three months	2,599	14,856
Placements with banks and other financial institutions with		
original maturity within three months	60,270	67,301
Investment securities with original maturity within three months	10,609	_
Amounts due from immediate holding company and fellow		
subsidiaries with original maturity within three months	53,067	44,789
Less: Overdrafts included in "deposits and balances		
of banks and other financial institutions	(153)	(77)
Less: Overdrafts included in "amounts due to		
immediate holding company"	(5,736)	(121)
	141,148	148,525

(Expressed in millions of Hong Kong dollars)

34 Cash and cash equivalents (continued)

		2012 HK\$'M	2011 HK\$'M
(b)	Reconciliation with the consolidated balance sheet	ŕ	
(2)	Cash and balances with banks, central banks, and		
	other financial institutions	20,492	21,777
	Trading assets	28,414	35,377
	Placements with banks and other financial institutions	143,581	136,513
	Investment securities	174,379	135,090
	Amounts due from immediate holding company and	,-	,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,
	fellow subsidiaries	79,322	68,488
	Overdrafts included in "deposits and balances of		
	banks and other financial institutions"	(153)	(77)
	Overdrafts included in "amounts due to immediate		
	holding company"	(5,736)	(121)
	Amounts shown in the balance sheet	440,299	397,047
	Less: amounts with an original maturity of beyond three months	(299,151)	(248,522)
	Cash and cash equivalents in the consolidated cash flow statement	141,148	148,525

35 Derivative financial instruments

The use of derivatives for trading and their sale to customers as risk management products is an integral part of the Bank's business activities. These instruments are also used to manage the Bank's own exposures to market risk as part of its asset and liability management process. The principal derivative instruments used by the Bank are foreign exchange related and interest rate related contracts, which are primarily over-the-counter derivatives. Most of the Bank's derivative positions have been entered into to meet customer demand and to hedge these and other trading positions. For accounting purposes, derivatives are classified as either held for trading or held for hedging.

(a) Notional amounts of derivatives

Derivatives are financial instruments that derive their value in reference to changes in interest or exchange rates, credit risk, financial instrument prices and indices. The notional amounts of these instruments indicate the volume of transactions outstanding and do not represent amounts at risk.

(Expressed in millions of Hong Kong dollars)

35 Derivative financial instruments (continued)

(a) Notional amounts of derivatives (continued)

The following is a summary of the notional amounts of each significant type of derivative entered into by the Bank and its subsidiaries:

Consolidated

	Qualifying for hedge accounting HK\$'M	201: Managed in conjunction with financial instruments designated at fair value through profit or loss HK\$'M	Others, including held for trading HK\$'M	Total HK\$'M
Exchange rate contracts Forwards Cross currency swaps Options purchased Options written	- 36,264 - -	99 1,214 69 1,927	1,192,815 32,176 13,210 13,231	1,192,914 69,654 13,279 15,158
Interest rate contracts Swaps Options purchased Options written	103,927 - -	108 - 217	28,587 436 43	132,622 436 260
Other derivatives			2,442	2,442
	140,191	3,634	1,282,940	1,426,765
Exchange rate contracts Forwards Cross currency swaps Options purchased Options written	- 12,502 - -	795 1,372 382 2,233	690,004 20,756 15,177 15,600	690,799 34,630 15,559 17,833
Interest rate contracts Swaps Options purchased Options written	105,278 - -	593 416 480	11,924 350 350	117,795 766 830
Other derivatives		99	14,035	14,134
	117,780	6,370	768,196	892,346

(Expressed in millions of Hong Kong dollars)

35 Derivative financial instruments (continued)

(a) Notional amounts of derivatives (continued)

Bank

	2012			
	Managed			
		in conjunction with		
		financial instruments	Others,	
	Qualifying	designated at	including	
	for hedge	fair value through	held for	
	accounting	profit or loss	trading	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Exchange rate contracts				
Forwards	_	99	1,192,815	1,192,914
Cross currency swaps	36,264	1,214	32,176	69,654
Options purchased	, <u> </u>	69	13,210	13,279
Options written	_	1,927	13,231	15,158
		.,	,	,
Interest rate contracts				
Swaps	103,927	108	27,482	131,517
Options purchased	_	_	436	436
Options written	-	217	43	260
Other derivatives			2,270	2,270
	140,191	3,634	1,281,663	1,425,488
		2011		
Exchange rate contracts				
Forwards	_	795	690,004	690,799
Cross currency swaps	12,502	1,372	20,756	34,630
Options purchased	_	382	15,177	15,559
Options written	-	2,233	15,600	17,833
Interest rate contracts				
Swaps	105,278	593	11,384	117,255
Options purchased	_	416	350	766
Options written	_	480	350	830
Other derivatives		99	14,035	14,134
	117,780	6,370	767,656	891,806

(Expressed in millions of Hong Kong dollars)

35 Derivative financial instruments (continued)

(b) Fair values and credit risk weighted amounts of derivatives

Consolidated

	2012			2011 Restated	
Fair value	Fair value	Credit risk	Fair value	Fair value	Credit risk
assets	liabilities	weighted	assets	liabilities	weighted
		amount			amount
HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
0.407	0.050	4 507	0.044	0.000	4 405
					1,135
1,079	1,749	360	872	1,549	295
120	73	90	903	909	7
7,666	8,475	2,047	4,419	5,546	1,437
	2012			2011 Postatod	
Fair value		Cradit rick	Fair value		Credit risk
					weighted
accord	naomeroo	amount	accoto	nasmass	amount
HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
0.407	0.050	4 505	0.044		4 405
6,467	6,653	1,597		3,088	1,135
1,075	1,749	357	869	1,549	294
116	70	34	903	909	7
7,658 =====	8,472	1,988	4,416	5,546	1,436
	assets HK\$'M 6,467 1,079 120 7,666 Fair value assets HK\$'M 6,467 1,075	assets liabilities HK\$'M HK\$'M 6,467 6,653 1,079 1,749 120 73 7,666 8,475 Fair value assets liabilities HK\$'M HK\$'M 6,467 6,653 1,075 1,749 116 70	Fair value assets Fair value liabilities Credit risk weighted amount HK\$'M 6,467 6,653 1,597 1,079 1,749 360 120 73 90 7,666 8,475 2,047 Fair value assets liabilities Weighted amount HK\$'M HK\$'M HK\$'M HK\$'M 6,467 6,653 1,597 1,075 1,749 357 116 70 34	Fair value assets Fair value liabilities Credit risk weighted amount HK\$'M Fair value Amount HK\$'M Fair value HK\$'M Fair value Amount HK\$'M HK\$'M\$ HK\$'M HK\$'M <td>Fair value assets Fair value liabilities Credit risk weighted amount HK\$'M Fair value HK\$'M Fair value assets Fair value liabilities HK\$'M HK\$'M HK\$'M HK\$'M HK\$'M HK\$'M 6,467 6,653 1,597 2,644 3,088 1,079 1,749 360 872 1,549 120 73 90 903 909 7,666 8,475 2,047 4,419 5,546 Fair value assets liabilities Weighted amount HK\$'M HK\$'M</td>	Fair value assets Fair value liabilities Credit risk weighted amount HK\$'M Fair value HK\$'M Fair value assets Fair value liabilities HK\$'M HK\$'M HK\$'M HK\$'M HK\$'M HK\$'M 6,467 6,653 1,597 2,644 3,088 1,079 1,749 360 872 1,549 120 73 90 903 909 7,666 8,475 2,047 4,419 5,546 Fair value assets liabilities Weighted amount HK\$'M HK\$'M

Credit risk weighted amount refers to the amount as computed in accordance with the Banking (Capital) Rules of the Hong Kong Banking Ordinance. The amount calculated is dependent upon the status of the counterparty and maturity characteristics of each type of contract.

The fair values and credit risk weighted amounts do not take into account any bilateral netting arrangements entered into during the year and accordingly these amounts are shown on a gross basis.

(c) Fair value of derivative financial instruments designated as hedging instruments

The following is a summary of the fair values of derivatives held for hedging purposes by product type entered into by the Bank and its subsidiaries as at 31 December 2012:

Consolidated and Bank

	2012	?
	Assets	Liabilities
	(Included in Amounts	(Included in
	due from immediate holding company	Amounts due to immediate holding
	and fellow subsidiaries)	company and fellow subsidiaries)
	HK\$'M	HK\$'M
Exchange rate contracts	16	355
Interest rate contracts	895	1,563
	911	1,918

(Expressed in millions of Hong Kong dollars)

35 Derivative financial instruments (continued)

(c) Fair value of derivative financial instruments designated as hedging instruments (continued)

Consolidated and Bank

	2011	
	Assets	Liabilities
	(Included in Other assets and Amounts	(Included in
	due from immediate holding company	Amounts due to immediate holding
	and fellow subsidiaries)	company and fellow subsidiaries)
	HK\$'M	HK\$'M
Exchange rate contracts	269	30
Interest rate contracts	688	1,344
	957	1,374

Fair value hedges

The fair value hedges principally consist of interest rate swaps and cross currency swaps. The interest rate swaps are used to protect against changes in the fair value of certain fixed rate assets and liabilities due to movements in market interest rates. The cross currency swaps are used to manage foreign exchange exposures. At 31 December 2012, the net negative fair value of derivatives held as fair value hedges was HK\$705 million (2011: negative HK\$338 million) comprising assets of HK\$827 million (2011: HK\$917 million) and liabilities of HK\$1,532 million (2011: HK\$1,255 million). The losses on the hedging instruments for the year were HK\$330 million (2011: losses of HK\$501 million). The gains on the hedged item attributable to the hedged risk were HK\$330 million (2011: gains of HK\$501 million).

Cash flow hedges

The cash flow hedges principally consist of interest rate swaps and cross currency swaps that are used to hedge against the variability in cash flows of certain floating rate assets and liabilities. At 31 December 2012, the net negative fair value of derivatives held as cash flow hedges was HK\$302 million (2011: negative HK\$79 million) comprising assets of HK\$84 million (2011: HK\$40 million) and liabilities of HK\$386 million (2011: HK\$119 million). The derivatives will mature within 5 years (2011: within 5 years) from the balance sheet date. During the year, there was no ineffectiveness recognised in the income statement that arose from cash flow hedges (2011: HK\$ Nil).

(Expressed in millions of Hong Kong dollars)

36 Contingent liabilities and commitments

(a) The following is a summary of the contractual amounts of each significant contingent liability and commitment:

	Consolidated			Bank	
		Restated		Restated	
	2012	2011	2012	2011	
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	
Direct credit substitutes	7,963	16,520	7,963	16,615	
Transaction-related contingencies	10,786	13,755	10,790	13,755	
Trade-related contingencies	23,009	22,054	23,088	22,086	
Forward asset purchases	140	622	140	622	
Other commitments:					
which are not unconditionally cancellable:					
with original maturity of not more than one year	8,649	11,479	7,741	10,096	
with original maturity of more than one year	18,425	13,436	17,639	13,309	
which are unconditionally cancellable	368,461	303,223	382,477	323,993	
	437,433	381,089	449,838	400,476	
Credit risk weighted amount	34,779	30,891	34,597	31,057	

Contingent liabilities and commitments are credit-related instruments, which include letters of credit, guarantees and commitments to extend credit. The risk involved is similar to the credit risk involved in extending loan facilities to customers. These transactions are, therefore, subject to the same credit application, portfolio maintenance and collateral requirements as for customers applying for loans. The contractual amounts represent the amounts at risk should the contract be fully drawn upon and the client defaults. As the facilities may expire without being drawn upon, the contracted amounts do not represent expected future cash flows.

(b) Capital commitments

Capital commitments outstanding at 31 December in respect of fixed asset purchases not provided for in the financial statements were as follows:

	Consolida	Consolidated and Bank	
	2012	2011	
	HK\$'M	HK\$'M	
Contracted for	63	66	
Authorised but not contracted for	61	76	
	124	142	

(Expressed in millions of Hong Kong dollars)

36 Contingent liabilities and commitments (continued)

(c) Lease commitments

The Bank and its subsidiaries lease a number of properties under operating leases. The leases typically run for an initial period of two to ten years, with an option to renew the lease when all terms are renegotiated. At 31 December, total future minimum lease payments under non-cancellable operating leases are payable as follows:

	Consc	olidated	Bank	
	2012	2011	2012	2011
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Within 1 year	759	710	737	691
After 1 year but within 5 years	1,531	1,433	1,519	1,425
After 5 years	1,094	931	1,094	931
	3,384	3,074	3,350	3,047

During the year HK\$744 million (2011: HK\$707 million) was recognised as an expense in the income statement in respect of operating leases. The Bank and its subsidiaries lease various premises and equipment under non-cancellable operating lease agreements.

(d) Contingencies

The Bank and its subsidiaries are named in and are defending a number of legal actions arising from its banking activities. Management of the Bank believes that the resolution of these actions and proceedings will not be material to the financial position of the Bank and its subsidiaries.

37 Risk management

The management of risk lies at the heart of the Bank's business. One of the principal risks the Bank incurs arises from extending credit to customers through its trading and lending operations. Beyond credit risk, the Bank is also exposed to a range of other risk types such as cross-border country, market, liquidity, operational, pensions, reputational and other risks that are inherent to the Bank's strategy, product range and business coverage.

Risk management framework

Effective risk management is fundamental to being able to generate profits consistently and sustainably – and is thus a central part of the financial and operational management of the Bank.

Through its risk management framework the Bank manages enterprise-wide risks, with the objective of maximising risk-adjusted returns while remaining within its risk appetite.

As part of this framework, the Bank uses a set of principles that describe the risk management culture the Bank wishes to sustain:

• Balancing risk and return: risk is taken in support of the requirements of the Bank's stakeholders, in line with the Bank's strategy and within its risk appetite;

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

Risk management framework (continued)

- Responsibility: it is the responsibility of all employees to ensure that risk-taking is disciplined and focused. The Bank takes account of its social responsibilities, and its commitment to customers in taking risk to produce a return;
- Accountability: risk is taken only within agreed authorities and where there is appropriate infrastructure and resource. All risk-taking must be transparent, controlled and reported;
- Anticipation: the Bank seeks to anticipate future risks and ensure awareness of all known risks;
 and
- Competitive advantage: the Bank seeks competitive advantage through efficient and effective risk management and control.

The Risk function

The Country Chief Risk Officer ("CCRO") directly manages a Risk function that is separate from and independent of the origination, trading and sales functions of the businesses. The CCRO chairs the Risk Committee.

The role of the Risk function is:

- To maintain the Risk Management Framework, ensuring it remains appropriate to the Bank's activities, is effectively communicated and implemented across the Bank and for administering related governance and reporting processes.
- To uphold the overall integrity of the Bank's risk/return decisions, and in particular for ensuring that
 risks are properly assessed, that risk/return decisions are made transparently on the basis of this
 proper assessment, and are controlled in accordance with the Bank's standards.
- To exercise direct Risk Control Ownership for Credit, Market, Country Cross-Border, Short-term Liquidity and Operational risk types.

(a) Credit risk

Credit risk is the potential for loss due to the failure of a counterparty to meet its obligations to pay in accordance with agreed terms. Credit exposures may arise from both the banking and trading books.

Credit risk is managed through a framework that sets out policies and procedures covering the measurement and management of credit risk. There is a clear segregation of duties between transaction originators in the businesses and the approvers in the Risk function. All credit exposure limits are approved within a defined credit approval authority framework.

Group-wide credit policies and standards are considered and approved by the Group Risk Committee ("GRC"), which also oversees the delegation of credit approval and loan impairment provisioning authorities.

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(a) Credit risk (continued)

The Bank's Risk Committee is responsible for the management of all risks, except those for which the Asset and Liability Committee and the Pensions Executive Committee have direct responsibility. The Risk Committee approves policies and standards based on those approved by GRC, risk limits and risk exposure delegated approval authority frameworks. When approving risk policies and standards, the Risk Committee takes into account the requirements of the Hong Kong Banking Ordinance and the guidelines issued by the HKMA with respect to large exposures and provisioning requirements.

Credit rating and measurement

Risk measurement plays a central role, along with judgement and experience, in informing risk-taking and portfolio management decisions. It is a primary area for sustained investment and senior management attention.

Since 1 January 2008, the Bank has used the advanced Internal Ratings Based (IRB) approach under the Basel II regulatory framework to calculate credit risk capital.

For IRB portfolios, a standard alphanumeric credit risk-grading system is used in both Wholesale and Consumer Banking. The grading is based on the Group's internal estimate of probability of default over a one year horizon, with customers or portfolios assessed against a range of quantitative and qualitative factors. The numeric grades run from 1 to 14 and some of the grades are further sub-classified A, B or C. Lower credit grades are indicative of a lower likelihood of default. Credit grades 1A to 12C are assigned to performing customers or accounts, while credit grades 13 and 14 are assigned to non-performing or defaulted customers.

The Bank's credit grades in Wholesale Banking are not intended to replicate external credit grades, and ratings assigned by external ratings agencies are not used in determining the Bank's internal credit grades. Nonetheless, as the factors used to grade a borrower may be similar, a borrower rated poorly by an external rating agency is typically assigned a worse internal credit grade.

Advanced IRB models cover a substantial majority of the Bank's loans and are used extensively in assessing risks at customer and portfolio level, setting strategy and optimising the Bank's risk-return decisions.

IRB risk measurement models are approved by the Risk Committee, on the recommendation of the Group Model Assessment Committee ('MAC') and the Bank's MAC. The Bank's MAC supports the Risk Committee in ensuring risk identification and measurement capabilities are objective and consistent, so that risk control and risk origination decisions are properly informed. Prior to review by the MAC, all IRB models are validated in detail by a model validation team, which is separate from the teams which develop and maintain the models. Models undergo a detailed annual review. Reviews are also triggered if the performance of a model deteriorates materially against predetermined thresholds during the ongoing model performance monitoring process.

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(a) Credit risk (continued)

Credit Approval

The Bank has been locally incorporated since 1 July 2004. Since then, the approval process reflects that strategic decisions are being made in accordance with individual managers' delegated authorities and the terms of reference of the appropriate committees. It is recognised that, as a major part of the Group, all significant risk decisions emanating from Hong Kong will have an impact to the Group, be it regulatory, concentration, strategic, etc. It is therefore recognised that it is essential for the Group to consider such transactions to ensure that these Group issues are included as part of the decision making process. Delegated authorities approved by the Risk Committee of the Bank are delegated to the key risk managers to ensure that all risk decisions are made within the Bank. Where proposals fall outside of the individual's authorities, the advice and guidance of the Group is sought. In such cases, the relevant Group entity, whether an individual or a committee (including but not limited to the GRC), will review the proposal from a Group perspective and give their recommendation. On receipt of such recommendation, the Bank's Excess Approval Committee, being a sub-committee of the Risk Committee, will meet to consider such advice and reach a suitable decision. All the credit applications approved by the Excess Approval Committee will be reported at each Risk Committee meeting for noting.

Concentration risk

Credit concentration risk is managed within concentration caps set by counterparty or groups of connected counterparties, by country and industry in Wholesale Banking; and tracked by product in Consumer Banking (and also by industry for the small and medium-sized enterprise business (SME)). Additional targets are set and monitored for concentrations by credit rating.

Credit concentrations are monitored by the Risk Committee and concentration limits that are material to the Bank are reviewed and approved at least annually by the Risk Committee.

Credit monitoring

The Bank and its subsidiaries regularly monitor credit exposures, portfolio performance, and external trends that may impact risk management outcomes.

Internal risk management reports are presented to risk committees, containing information on key environmental, political and economic trends across major portfolios and countries; portfolio delinquency and loan impairment performance; as well as IRB portfolio metrics including credit grade migration.

The Bank's Wholesale Banking Credit Issues Forum (which is a sub-committee of the Risk Committee) meets regularly to assess the impact of external events and trends on the Wholesale Banking credit risk portfolio and to define and implement the Bank's response in terms of appropriate changes to portfolio shape, portfolio and underwriting standards, risk policy and procedures.

Client accounts are placed on Early Alert when they display signs of actual or potential weakness. For example where there is a decline in the clients' position within the industry, a financial deterioration, a breach of covenants, non-performance of an obligation, or there are issues relating to ownership or management.

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(a) Credit risk (continued)

Such accounts and portfolios are subjected to a dedicated process overseen by an Early Alert Committee. Client account plans and credit grades are re-evaluated and remedial actions are agreed and monitored. Remedial actions include, but are not limited to, exposure reduction, security enhancement, exiting the account or immediate movement of the account into the control of Group Special Assets Management (GSAM), the Bank's specialist recovery unit.

In Consumer Banking, portfolio delinquency trends are monitored continuously at a detailed level. Individual customer behaviour is also tracked and is considered for lending decisions. Accounts that are past due are subject to a collections process, managed independently by the Risk function. Charged-off accounts are managed by a specialist recovery team.

The SME business is managed within Consumer Banking in two distinct customer sub-segments: small businesses and medium enterprises, differentiated by the annual turnover of the counterparty. The credit processes are further refined based on exposure at risk. Larger exposures are managed through the Discretionary Lending approach, in line with Wholesale Banking procedures, and smaller exposures are managed through Programmed Lending, in line with Consumer Banking procedures. Discretionary Lending and Private Banking past due accounts are managed by GSAM.

Credit mitigation

Potential credit losses from any given account, customer or portfolio are mitigated using a range of tools such as collateral, netting agreements, credit insurance, credit derivatives and other guarantees. The reliance that can be placed on these mitigants is carefully assessed in light of issues such as legal enforceability, market value and counterparty risk of the guarantor.

Risk mitigation policies determine the eligibility of collateral types. Collateral types which are eligible for risk mitigation include: cash; residential, commercial and industrial property; fixed assets such as motor vehicles, aircraft, plant and machinery; marketable securities; commodities; bank guarantees; and letters of credit. Risk mitigation policies control the approval of collateral types.

Collateral is valued in accordance with the Bank's risk mitigation policy, which prescribes the frequency of valuation for different collateral types. The valuation frequency is driven by the level of price volatility of each type of collateral and the nature of the underlying product or risk exposure.

In Wholesale Banking the effectiveness of credit mitigation is ensured by policies which govern eligibility criteria such as monitoring of concentration of collateral, correlation of the collateral to underlying assets, adjustments for currency fluctuations for collateral. For all credit risk mitigation that meets the policy criteria, a clear set of procedures are applied to ensure that the value of the underlying collateral is appropriately recorded and updated regularly.

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(a) Credit risk (continued)

In Consumer Banking effective use of collateral is a key tool by which credit risk is mitigated. All eligible collateral accepted by Consumer Banking is covered by a product proposal approved by senior credit officers delegated with the relevant authority. New collateral types have to be vetted through a stringent 'New Business Approval' process and are approved in accordance with the delegated authorities within Consumer Banking Risk or by the Excess Approval Committee under advice of the Bank's Consumer Banking Risk Committee as appropriate. In order to be recognized as security and for the loan to be classified as secured, all items pledged must be valued and an active secondary resale market must exist for the collateral. Documentation must be held to enable Consumer Banking to realize the asset without the cooperation of the asset owner in the event that this is necessary. Regular valuation of collateral is required in accordance with the Group's risk mitigation policy, which prescribes both the process of valuation and the frequency of valuation for different collateral types. The valuation frequency is driven by the level of price volatility of each type of collateral and the nature of the underlying product or risk exposure. Stress tests are performed on changes in collateral values for key portfolios to assist senior management in managing the risks in those portfolios. Physical collateral is required to be insured at all times and against all risks, with the Bank as the loss payee under the insurance policy.

Detailed procedures over collateral management must be in place for each business.

Traded Products

Credit risk from traded products is managed within the overall credit risk appetite for corporates and financial institutions.

The credit risk exposure from traded products is derived from the positive mark-to-market value of the underlying instruments, and an additional component to cater for potential market movements.

For derivative contracts, the Bank limits its exposure to credit losses in the event of default by entering into master netting agreements with certain counterparties. As required by HKAS 32/IAS 32, exposures are presented on a gross basis in the financial statements as such transactions are not intended to be settled net in the ordinary course of business.

In addition, the Bank enters into Credit Support Annexes ('CSA') with counterparties where collateral is deemed a necessary or desirable mitigant to the exposure. Under a variation margin process, additional collateral is called from the counterparty if total uncollateralised mark-to-market exposure exceeds the threshold and minimum transfer amount specified in the CSA. With certain counterparties, the CSA is reciprocal and requires the Bank to post collateral if the overall mark-to-market value of positions is in the counterparty's favour and exceeds an agreed threshold.

Securities

Within Wholesale Banking, the Excess Approval Committee under advice of the Group's Underwriting Committee (as approved by the Bank's Board) approves the portfolio limits and parameters for the underwriting and purchase of all pre-defined securities assets to be held for sale. The Underwriting Committee is established under the authority of the Risk Committee under advice of the Group. Wholesale Banking operates within set limits, which include country, single issuer, holding period and credit grade limits.

Day to day credit risk management activities for traded securities are carried out by Traded Credit Risk Management whose activities include oversight and approval within the levels delegated by the Underwriting Committee. Issuer credit risk, including settlement and pre-settlement risk, is controlled by Wholesale Banking Risk, while price risk is controlled by Market Risk.

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(a) Credit risk (continued)

The Underwriting Committee approves individual proposals to underwrite new corporate security issues for clients. Where an underwritten security is held for a period longer than the target sell-down period, the final decision on whether to sell the position rests within the Risk function.

Maximum exposure to credit risk

The maximum exposures to credit risk of on-balance sheet financial instruments, before taking account of any collateral or other credit enhancements is the carrying amount reported on the balance sheet. For off-balance sheet instruments, the maximum exposure to credit risk excludes loan commitments which are unconditionally cancellable is the contractual nominal amounts as set out below:

	Consolidated		Bank	
		Restated		Restated
	2012	2011	2012	2011
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Financial guarantees and other				
credit related contingent liabilities Loan commitments and other	41,758	52,329	41,841	52,456
credit related commitments	27,214	25,537	25,520	24,027
	68,972	77,866	67,361	76,483

Collateral

Collateral is held to mitigate credit risk exposures and risk mitigation policies determine the eligibility of collateral types.

For certain types of lending – typically mortgages and asset financing – the right to take charge over physical assets is significant in terms of determining appropriate pricing and recoverability in the event of default.

Collateral is valued in accordance with our risk mitigation policy, which prescribes the frequency of valuation for different collateral types, based on the level of price volatility of each type of collateral and the nature of the underlying product or risk exposure. Where appropriate, collateral values are adjusted to reflect current market conditions, probability of recovery and the period of time to realise the collateral in the event of possession. The collateral values reported below reflect this conservative basis and are also adjusted for the effects of over-collateralisation.

(i) Loans and advances

The requirement for collateral is not a substitute for the ability to pay, however, which is the primary consideration for any lending decisions. In determining the financial effect of collateral held against loans neither past due nor impaired, we have assessed the significance of the collateral held in relation to the type of lending.

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(a) Credit risk (continued)

Loans neither past due nor impaired

At 31 December 2012, the Bank and its subsidiaries have HK\$173,846 million (2011: HK\$153,707 million) of mortgage loans in Consumer Banking that are neither past due nor impaired. These are generally fully secured exposures (2011: fully secured).

In Wholesale Banking, the Bank and its subsidiaries have HK\$159,310 million (2011: HK\$178,402 million) of corporate exposures that are neither past due nor impaired. Based on the fair value of the collateral held (Note), 20% (2011: 24%) of these exposures are secured by tangible collaterals.

The Bank and its subsidiaries also undertake collateralised lending and borrowing (reverse repo and repo) arrangements, and the collateral held against these types of loans are set out in note 39 to the financial statements.

Non-tangible collateral – such as guarantees and letters of credit – may also be held against corporate exposures although the financial effect of this type of collateral is less significant in terms of recoveries. It is not practicable to quantify the effect of this collateral as the value of the collateral is conditional on circumstances at the time of default and other credit related factors.

Loans past due or impaired

The fair value of collateral held against past due or impaired loans is detailed in the table below as at 31 December:

Consolidated

	2012		2011	
	Advances to	Advances to	Advances to	Advances to
	customers	banks	customers	banks
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Estimated fair value of collateral (Note):				
Held against impaired advances	307	_	249	_
Held against past due but not impaired advances	6,407	_	2,650	_

Bank

	2012		2011	
	Advances to	Advances to	Advances to	Advances to
	customers	banks	customers	banks
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Estimated fair value of collateral (Note):				
Held against impaired advances	298	_	249	_
Held against past due but not impaired advances	6,297	_	2,510	_

(Note) The fair value of the collateral held represents fair value, after taking into account the effects of over-collateralisation where it is not available for offset against other loans.

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(a) Credit risk (continued)

Repossessed Collateral

As at 31 December, the amounts of assets obtained by taking possession of collateral held as security were as follows:

	Consolidated		Bank	
	2012	2011	2012	2011
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Property, plant and equipment	32	48	26	31

Loan collateral acquired from borrowers due to restructuring or their inability to repay, continues to be recorded as "Advances to customers" in the balance sheet at the lower of fair value (less costs to sell) and the carrying amount of the loan (net of any impairment allowances), until the collateral is realised.

Repossessed collaterals obtained are intended to be realised in an orderly fashion to repay the impaired loans and are not held for the own use of the Bank and its subsidiaries.

(ii) Off-balance sheet exposures

For certain types of exposures such as letters of credit and guarantees, the Bank and its subsidiaries obtain collateral such as cash depending on internal credit risk assessments. However, for trade finance products such as letters of credit, the Bank and its subsidiaries will also hold legal title to the underlying assets should a default takes place.

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(a) Credit risk (continued)

Credit quality

(i) Analysis of the loan portfolio

Consolidated

Consolidated	2012		2011	
	Advances to customers HK\$'M	Advances to banks HK\$'M	Advances to customers HK\$'M	Advances to banks HK\$'M
Loans and advances				
 neither past due nor impaired 	398,645	143,525	386,145	135,967
 past due but not impaired 	9,082	13	3,781	485
- impaired, net of individually assessed				
impairment charges	858	43	391	61
Less: collectively assessed				
impairment charges	(567)		(554)	
	408,018	143,581	389,763	136,513
Rank				

Bank

	2012		2011	
	Advances to customers HK\$'M	Advances to banks HK\$'M	Advances to customers HK\$'M	Advances to banks HK\$'M
Loans and advances				
- neither past due nor impaired	386,169	143,515	374,011	135,931
past due but not impairedimpaired, net of individually assessed	8,835	13	3,526	485
impairment charges Less: collectively assessed	836	43	384	61
impairment charges	(454)		(444)	
	395,386	143,571	377,477	136,477

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(a) Credit risk (continued)

(i) Analysis of the loan portfolio (continued)

The following tables set out an analysis of the internal credit gradings for advances which are not past due and for which no individual impairment provision has been raised. The credit gradings set out in the tables below are based on a probability of default measure as set out on page 74.

Consolidated				
	2	012	2011	
	Advances to	Advances to	Advances to	Advances to
	customers	banks	customers	banks
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Credit grades:				
1 to 5	238,341	142,449	225,102	134,828
6 to 8	115,727	953	115,332	1,095
9 to 11	43,194	123	44,226	44
12	1,383		1,485	
	398,645	143,525	386,145	135,967
Bank				
	2	012	2	011
	Advances to	Advances to	Advances to	Advances to
	customers	banks	customers	banks
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Credit grades:				
1 to 5	233,993	142,439	223,420	134,792
6 to 8	112,022	953	108,114	1,095
9 to 11	38,976	123	41,374	44
12	1,178		1,103	
	386,169	143,515	374,011	135,931

The following tables set out the ageing of advances which are past due and for which no individual impairment provision has been raised. A loan is considered to be past due when the counterparty has failed to make a principal or interest payment when contractually due. Past due does not necessarily mean that the counterparty is impaired.

Consolidated

Consolidated	2	012	2011	
	Advances to customers HK\$'M	Advances to banks HK\$'M	Advances to customers HK\$'M	Advances to banks HK\$'M
Past due				
up to 30 days	7,903	13	3,474	485
- 31-60 days	200	_	176	_
- 61-90 days	844	_	55	_
- 91-120 days	45	_	13	_
- 121-150 days	90		63	
	9,082	13	3,781	485

(Expressed in millions of Hong Kong dollars)

Net impaired securities

Securities neither past due nor impaired

37 Risk management (continued)

(a) Credit risk (continued)

(i) Analysis of the loan portfolio (continued)

Bank

Barik	2012		2011	
	Advances to customers HK\$'M	Advances to banks HK\$'M	Advances to customers HK\$'M	Advances to banks HK\$'M
Past due				
- up to 30 days	7,705	13	3,274	485
- 31-60 days	174	_	138	_
- 61-90 days	821	_	38	_
- 91-120 days	45	_	13	_
- 121-150 days	90		63	
	8,835	13	3,526	485

(ii) Analysis of debt securities (including certificates of deposit), equity shares and treasury bills

Consolidated		2012	2			
	Treasury bills HK\$'M	Debt securities HK\$'M	Equity shares HK\$'M	Total HK\$'M		
Impaired securities Impairment provisions		26 (26)	6 (6)	32 (32)		
Net impaired securities Securities neither past due nor impaired	42,209	_ 163,419 	1,021	206,649		
	2011					
	Treasury bills HK\$'M	Debt securities HK\$'M	Equity shares HK\$'M	Total HK\$'M		
Impaired securities Impairment provisions		(34)	6 (6)	50 (40 <u>)</u>		
Net impaired securities Securities neither past due nor impaired	48,254	10 127,412	427	10 176,093		
Bank		2012	2			
	Treasury bills HK\$'M	Debt securities HK\$'M	Equity shares HK\$'M	Total HK\$'M		
Impaired securities Impairment provisions	<u>-</u>	26 (26)	6 (6)	32 (32)		

42,209

163,352

1,021

206,582

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(a) Credit risk (continued)

(ii) Analysis of debt securities (including certificates of deposit), equity shares and treasury bills (continued)

Bank (continued)

	2011							
	Treasury	Debt	Equity					
	bills	securities	shares	Total				
	HK\$'M	HK\$'M	HK\$'M	HK\$'M				
Impaired securities	_	36	6	42				
Impairment provisions		(30)	(6)	(36)				
Net impaired securities		6		6				
Securities neither past due nor impaired	48,254	125,589	427	174,270				

The following table analyses debt securities (including certificates of deposit) and treasury bills which are neither past due nor impaired by external credit rating. The standard credit ratings used by the Bank are those used by Standard & Poors or their equivalent. Debt securities held which have a short-term rating are reported against the long-term rating of the issuer.

Consolidated

Consolidated					
	20	12	2011		
	Treasury	Debt	Treasury	Debt	
	bills	securities	bills	securities	
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	
AAA	_	19,122	_	12,704	
AA - to AA +	42,209	72,764	48,254	50,658	
A - to A +	_	65,339	_	58,012	
Lower than A-	_	1,487	_	890	
Unrated		4,707		5,148	
	42,209	163,419	48,254	127,412	

Bank

	20	112	2011		
	Treasury	Debt	Treasury	Debt	
	bills	securities	bills	securities	
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	
AAA	_	19,122	_	12,704	
AA - to AA +	42,209	72,764	48,254	50,658	
A - to A +	_	65,339	_	58,012	
Lower than A-	_	1,487	_	890	
Unrated		4,640		3,325	
	42,209	163,352	48,254	125,589	

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(b) Country cross-border risk

Country cross-border risk is the risk that the Bank will be unable to obtain payment from its customers or third parties on their contractual obligations as a result of certain actions taken by foreign governments, chiefly relating to convertibility and transferability of foreign currency.

The Risk Committee is responsible for our country cross-border risk limits.

Cross-border assets comprise loans and advances, interest-bearing deposits with other banks, trade and other bills, acceptances, amounts receivable under finance leases, derivatives, certificates of deposit and other negotiable paper, investment securities and formal commitments where the counterparty is resident in a country other than where the assets are recorded. Cross-border assets also include exposures to local residents denominated in currencies other than the local currency. Cross-border exposure also includes the value of commodity, aircraft and shipping assets owned by the Bank that are held in a given country.

(c) Market risk management

Market risk

The Bank recognises market risk as the potential loss of earnings or economic value due to adverse changes in financial market rates or prices. The Bank's exposure to market risk arises principally from customer-driven transactions. The objective of the Bank's market risk policies and processes is to obtain the best balance of risk and return whilst meeting customers' requirements.

The Bank transacts in the money market, foreign exchange markets, equity markets, and capital markets giving rise to market risk exposures. Financial instruments transacted include debt and other securities and certain off-balance sheet ("derivatives") financial instruments. Derivatives are contracts with characteristics and value derived from underlying financial instruments, interest and exchange rates or indices. They include futures, forwards, swaps, and options transactions in the foreign exchange and interest rate markets. The Bank enters into derivative contracts in the normal course of business to meet customer demand and for hedging purposes. Derivative contracts entered into by the Bank are primarily over-the-counter derivatives which the mark-to-market values are readily determinable by reference to independent prices and valuation quotes.

The Bank has established a market risk management framework and policies, including limits setting, monitoring and reporting and control procedures, which are reviewed regularly by the Risk Committee. Market risk limits are proposed by the business within the terms of agreed policy and reviewed by the Market Risk department. The Risk Committee approves the limits and the Market Risk department monitors exposure against these limits and approves temporary limits within the delegated authorities. Additional limits are placed on specific instruments and position concentrations where appropriate. Sensitivity measures are used in addition to using value-at-risk ("VaR") as risk management tools. For example, interest rate sensitivity is measured in terms of exposure to a one basis point increase in yields.

Value at Risk

VaR, in general, is a quantitative measure of market risk that applies recent historical market conditions to estimate the potential future loss in market value that will not be exceeded in a set time period at a set statistical confidence level. VaR provides a consistent measure that can be applied across trading businesses and products over time and can be set against actual daily trading profit and loss outcome.

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(c) Market risk management (continued)

Value at Risk (continued)

VaR is calculated for expected movements over a minimum of one business day and to a confidence level of 97.5 per cent. This confidence level suggests that potential daily losses, in excess of the VaR measure, are likely to be experienced six times per year.

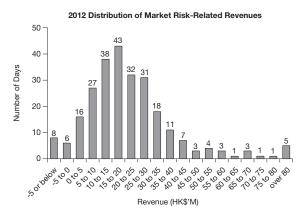
The Bank applies two VaR methodologies, historic simulation and Monte Carlo simulation, with a historical observation period of one year. Historic simulation is applied for general market risk factors. This approach involves the revaluation of all existing positions to reflect the effect of historically observed changes in market risk factors on the valuation of the current portfolio. Monte Carlo simulation is applied for credit spread VaR of the banking book. This approach is similar to historic simulation but with considerably more input risk factor observations. These are generated by random sampling techniques, but the results retain the essential variability and correlations of historically observed risk factor changes.

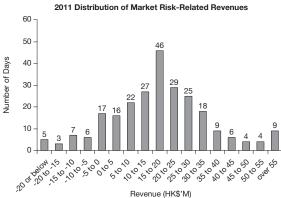
Stress Testing

Losses beyond the confidence interval are not captured by a VaR calculation, which therefore gives no indication of the size of unexpected losses in these situations.

VaR and other risk measures are complemented by weekly stress testing of market risk exposures to highlight potential risk that may arise from extreme market events that are rare but plausible. Stress testing is an integral part of the market risk management framework and considers both historical market events and forward looking scenarios. A consistent stress testing methodology is applied to trading and non-trading books. The stress testing methodology assumes that scope for management action would be limited during a stress event, reflecting the decrease in liquidity that often occurs.

Stress scenarios are regularly updated to reflect changes in risk profile and economic events. The Risk Committee reviews stress test results on a regular basis. Ad hoc scenarios are also prepared reflecting specific market conditions and for particular concentrations of risk that arise within the business.





(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(c) Market risk management (continued)

Trading and Non-trading (VaR at 97.5%, 1 day)*

Trading and Non-trading (VaF	R at 97.5%	5, 1 day)*								
Value at risk:		20	12			20	11			
	Average HK\$'M	High HK\$'M	Low HK\$'M	Actual** HK\$'M	Average HK\$'M	High HK\$'M	Low HK\$'M	Actual** HK\$'M		
Interest rate risk ^	75.3	116.9	52.2	52.2	45.2	54.2	35.8	51.7		
Foreign exchange risk	4.8	9.2	2.2	3.4	3.5	6.6	0.9	1.8		
Total ^^	76.3	117.2	53.5	53.7	45.4	54.3	36.0	51.7		
Trading (VaR at 97.5%, 1 day)									
Value at risk:		201	12		20			011		
	Average HK\$'M	High HK\$'M	Low HK\$'M	Actual** HK\$'M	Average HK\$'M	High HK\$'M	Low HK\$'M	Actual** HK\$'M		
Interest rate risk	13.6	26.7	8.5	11.9	12.3	16.6	9.1	9.2		
Foreign exchange risk	4.8	9.2	2.2	3.4	3.5	6.6	0.9	1.8		
Total ^^	14.9	26.3	8.9	11.7	13.0	18.6	9.3	10.1		
Non-trading (VaR at 97.5%, 1	day)									
Value at risk:		20	12			20	11			
	Average HK\$'M	High HK\$'M	Low HK\$'M	Actual** HK\$'M	Average HK\$'M	High HK\$'M	Low HK\$'M	Actual** HK\$'M		
Interest rate risk ^	74.1	109.2	51.2	51.2	43.4	52.8	34.0	50.8		
Average daily income earned	from mar	ket risk re	elated ac	tivities***	are as fol	lows:				
						2	012	2011		

	2012	2011
	HK\$'M	HK\$'M
Trading		
Interest rate risk	5.1	3.8
Foreign exchange risk	10.0	9.8
Total	15.1	13.6
Non-Trading		
-	0.5	4.0
Interest rate risk	6.5	4.0

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(c) Market risk management (continued)

The highest and lowest VaR are independent and usually occur on different days.

- * VaR is representative of SCB HK onshore portfolios only.
- ** This represents the actual one day VaR as at 31 December.
- *** P/L includes profits coming from offshore portfolios.
- ^ Interest rate risk VaR includes credit spread risk arising from securities held by the Financial Markets' Asset and Liability Management desk ("ALM").
- ^^ The total VaR shown in the table above is not a sum of the component risks due to offsets between them.

(d) Foreign exchange risk

The foreign exchange positions of the Bank and its subsidiaries arise from foreign exchange trading and commercial banking operations. Foreign exchange trading exposures are principally derived from customer driven transactions. The Market Risk department approves foreign exchange limits within delegated authorities and monitors exposures against these limits. The net option position is calculated on the basis of the delta-weighted positions of all foreign exchange option contracts.

Foreign exchange risk on the non-trading book portfolios is minimised by match funding assets and liabilities in the same currency.

The Bank and its subsidiaries had the following non-structural foreign currency positions which exceeded 10% of the net non-structural position in all foreign currencies:

	Consc	olidated	Bank			
	2012 2011		2012	2011		
	HK\$'M	HK\$'M	HK\$'M	HK\$'M		
HO dellare company						
US dollars exposure						
Spot assets	320,683	311,090	320,680	311,090		
Spot liabilities	(279,069)	(262,066)	(279,069)	(262,066)		
Forward purchases	608,542	328,649	608,542	328,649		
Forward sales	(644,729)	(378,787)	(644,729)	(378,787)		
Net option position	_	_	_	_		
Net long/(short) non-structural position	5,427	(1,114)	5,424	(1,114)		

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(d) Foreign exchange risk (continued)

	Consolidat	ted and Bank
	2012	2011
	HK\$'M	HK\$'M
Chinese renminbi exposure		
Spot assets	98,441	87,053
Spot liabilities	(86,732)	(63,195)
Forward purchases	382,433	162,096
Forward sales	(393,558)	(185,047)
Net option position	_	_
Net long non-structural position	584	907
	Consolidat	ted and Bank
	2012	2011
	HK\$'M	HK\$'M
Australian dollars exposure		
	7,239	6,800
Spot assets	7,239 (13,599)	6,800 (15,005)
Spot assets Spot liabilities	(13,599)	(15,005)
Spot assets	(13,599) 12,433	(15,005) 10,833
Spot assets Spot liabilities Forward purchases Forward sales	(13,599)	(15,005)
Spot assets Spot liabilities Forward purchases	(13,599) 12,433	(15,005) 10,833
Spot assets Spot liabilities Forward purchases Forward sales	(13,599) 12,433	(15,005) 10,833

The Bank and its subsidiaries had the following structural foreign currency positions which exceeded 10% of the net structural position in all foreign currencies:

	Consol	Bank Restated		
	2012	2011	2012	2011
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Chinese Renminbi	5,085	4,163	5,085	4,163
United Arab Emirates Dirham	503	531	503	531
Vietnamese Dong	764	740	317	307
US dollars	318	363	318	363
	6,670	5,797	6,223	5,364

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(e) Interest rate risk

The Bank's interest rate exposures comprise trading exposures and non-trading structural interest rate exposures. Structural interest rate risk generally arises from the differing re-pricing characteristics of commercial banking assets and liabilities.

Interest rate risk from the non-trading book portfolios is transferred to Financial Markets . Financial Markets manages these risks with oversight by the Asset and Liability Committee ("ALCO") and within limits approved by the Market Risk department. VaR and stress tests are applied to non-trading book interest rate exposures in the same way as for the trading book.

The Bank has established principles, policies and techniques for managing interest rate risk. Interest rate risk management is governed by the ALCO.

(f) Liquidity risk

The Bank defines liquidity risk as the risk that it either does not have sufficient financial resources available to meet all its obligations and commitments as they fall due, or can only secure them at excessive cost.

The Bank has established standards, principles, policies and techniques for managing liquidity risk. Liquidity risk management is governed by the ALCO. It is the policy of the Bank to maintain adequate liquidity at all times and hence to be in a position to meet all obligations as they fall due. The tools used for the management of liquidity risk range from key balance sheet ratios and medium-term funding requirements for ensuring balance sheets are not developing structural imbalances, to short term cash flow limits, controls on borrowing in the wholesale markets and guidelines on commitments. They are supplemented by the establishment of regular stress testing of liquidity positions and a liquidity crisis contingency plan.

The Bank has significant levels of marketable securities, principally government securities and bank paper, which can be realised in the event that there is a need for liquidity in a crisis. The Bank also prescribes a liquidity stress scenario that assumes accelerated withdrawal of deposits over a period of time and needs to ensure that cash inflows exceed outflows under such a scenario. The liquidity crisis management plan lays out trigger points and actions in the event of a liquidity crisis to ensure that there is an effective response by senior management in case of such an event.

Financial Markets is responsible for the day-to-day management of all the liquidity risk in the Bank, executing liquidity directives and operating within the liquidity policy and approved limits. Liquidity limits are regularly monitored by a Market Risk function that is independent from the business. Liquidity profiles are reviewed by the ALCO on a regular basis.

Customer deposits form a significant part of the Bank's overall funding. Its composition has remained relatively diversified and stable. The ALCO monitors trends in the balance sheet and ensures that any concerns that might impact the stability of these deposits are addressed effectively. The ALCO also reviews balance sheet plans to ensure that asset growth plans are matched by growth in the stable funding base. Moreover, professional markets are accessed for the purposes of providing additional funding, maintaining a presence in local money markets and optimising asset and liability maturities.

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(f) Liquidity risk (continued)

(i) Contractual maturity

The following maturity profile is based on the remaining period to the contractual maturity date as at the balance sheet date, on a discounted basis. The disclosure does not imply that the assets will be held to maturity or that the liabilities will be withdrawn on maturity.

Consolidated

				20	112			
			Due	Due	Due			
		Due	between	between	between	Due		
	Repayable	within	1 month to	3 months to	1 year to	after		
	on demand	1 month	3 months	1 year	5 years	5 years	Undated	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Assets								
Cash and balances with banks, central								
banks and other financial institutions	20,492	-	-	-	-	-	_	20,492
Placements with banks and								
other financial institutions	537	46,669	47,572	47,582	1,222	_	(1)	143,581
Hong Kong SAR Government								
certificates of indebtedness	_	_	_	_	_	_	32,481	32,481
Trading assets	_	1,513	4,173	9,273	8,851	4,103	501	28,414
Financial assets designated at		,-	,	,	-,	,		-,
fair value	_	_	_	_	110	3,106	_	3,216
Advances to customers	16,228	62,269	30,857	56,102	113,699	129,924	(1,061)	408,018
Investment securities	67	18,306	32,919	56,861	59,158	6,548	520	174,379
Amounts due from group companies	14,986	35,131	10,090	12,635	5,602	2,463	(1,585)	79,322
Others	350	4,515	10,796	733	554	86	32,737	49,771
Culore								
Total Assets	52,660	168,403	136,407	183,186	189,196	146,230	63,592	939,674
Liabilities								
Hong Kong SAR currency								
notes in circulation	_	_	_	_	_	_	32,481	32,481
Deposits and balances of banks							,	,
and other financial institutions	10,798	494	217	772	_	_	_	12,281
Deposits from customers	487,710	97,913	87,138	81,955	1,831	42	_	756,589
Trading liabilities	_	21,601	110	447	50	86	774	23,068
Financial liabilities designated at		,						,
fair value	_	818	924	1,372	468	30	_	3,612
Debt securities in issue	_	320	3,586	6,100	-	-	_	10,006
Amounts due to group companies	10,031	3,253	4,825	3,325	1,247	2,042	_	24,723
Subordinated liabilities		- 0,200	.,020	-	- 1,217	11,267	_	11,267
Others	6,395	5,025	5,528	1,309	48	244	327	18,876
2.1.5.0								
Total Liabilities	514,934	129,424	102,328	95,280	3,644	13,711	33,582	892,903
	====	====	====	====	====	====		====

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(f) Liquidity risk (continued)

(i) Contractual maturity (continued)

Consolidated (continued)

				20	12			
	Repayable on demand	Due within 1 month	Due between 1 month to 3 months	Due between 3 months to 1 year	Due between 1 year to 5 years	Due after 5 years	Undated	Total
Of which:								
Certificates of deposit held - included in Trading assets - included in Investment securities	-	4	452	590	33	-	-	1,079
as available-for-sale securities		6,603	11,663	10,634	2,856			31,756
		6,607	12,115	11,224	2,889			32,835
Treasury bills (including Exchange Fund Bills)								
included in Trading assets included in Investment securities	-	1,341	3,348	3,988	25	-	-	8,702
as available-for-sale securities		4,994	15,007	13,506				33,507
		6,335	18,355	17,494	25			42,209
Debt securities			004	4.070	0.705	4.075		47.000
included in Trading assetsincluded in Financial assets	-	-	291	4,278	8,725	4,075	-	17,369
designated at fair value - included in Investment securities classified as:	-	-	-	-	110	3,106	-	3,216
 available-for-sale securities 	-	6,116	6,249	28,611	52,182	6,548	-	99,706
 loans and receivables included in Amounts due from fellow subsidiaries classified as: 	67	593	-	4,110	4,120	-	-	8,890
available-for-sale securities financial assets designated at	-	-	-	-	-	1,305	-	1,305
fair value						98		98
	67	6,709	6,540	36,999	65,137	15,132		130,584

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(f) Liquidity risk (continued)

(i) Contractual maturity (continued)

Consolidated (continued)

				20	111			
			Due	Due	Due			
	Repayable	Due within	between	between 3 months to	between 1 year to	Due after		
	on demand	1 month	3 months	1 year	5 years	5 years	Undated	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Assets								
Cash and balances with banks, central								
banks and other financial institutions	21,777	_	_	_	_	_	_	21,777
Placements with banks and	21,777							21,111
other financial institutions	510	53,304	36,128	45,070	1,504	_	(3)	136,513
Hong Kong SAR Government	0.10	00,001	00,120	10,010	1,001		(0)	100,010
certificates of indebtedness	_	_	_	_	_	_	31,401	31,401
Trading assets	_	6,406	4,531	10,294	10,109	4,027	10	35,377
Financial assets designated at		,	,	,	,	,-		/ -
fair value	_	_	-	38	344	3,893	_	4,275
Advances to customers	9,476	57,041	42,141	57,247	109,954	115,038	(1,134)	389,763
Investment securities	1,827	12,021	25,611	45,430	48,144	1,640	417	135,090
Amounts due from group companies	6,519	33,642	12,287	4,984	8,051	3,005	_	68,488
Others	322	3,789	6,739	510	326	56	19,428	31,170
Total Assets	40,431	166,203	127,437	163,573	178,432	127,659	50,119	853,854
Liabilities								
Hong Kong SAR currency								
notes in circulation	_	_	-	-	_	-	31,401	31,401
Deposits and balances of banks								
and other financial institutions	11,156	3,584	256	13	720	_	_	15,729
Deposits from customers	415,667	130,939	85,872	39,022	1,422	18	_	672,940
Trading liabilities	-	23,972	109	543	13	1	-	24,638
Financial liabilities designated at								
fair value	-	194	1,329	1,353	611	-	_	3,487
Debt securities in issue	-	8,634	2,930	1,701	-	-	-	13,265
Amounts due to group companies	2,882	2,738	5,166	3,248	2,366	1,696	-	18,096
Subordinated liabilities	_	_	-	-	_	13,100	_	13,100
Others	5,521	3,618	8,820	2,358	27	130	223	20,697
Total Liabilities	40E 006	170 670	104 400	40.000	E 1E0	14.045	21 624	010 050
Total Liabilities	435,226	173,679	104,482	48,238	5,159	14,945	31,624	813,353

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(f) Liquidity risk (continued)

(i) Contractual maturity (continued)

Consolidated (continued)

	Repayable on demand	Due within 1 month	Due between 1 month to 3 months	Due between 3 months to 1 year	Due between 1 year to 5 years	Due after 5 years	Undated	Total
Of which:								
Certificates of deposit held - included in Trading assets - included in Investment securities	-	52	54	1,502	412	100	-	2,120
as available-for-sale securities		4,532	6,861	7,979	4,415			23,787
		4,584	6,915	9,481	4,827	100		25,907
Treasury bills (including Exchange								
Fund Bills) - included in Trading assets - included in Investment securities	-	5,828	3,183	4,727	-	-	-	13,738
as available-for-sale securities		1,418	15,833	17,265				34,516
		7,246	19,016	21,992				48,254
Debt securities								
included in Trading assetsincluded in Financial assets	-	280	979	3,706	9,640	3,908	-	18,513
designated at fair value - included in Investment securities classified as:	-	-	-	38	344	3,893	-	4,275
available-for-sale securities	_	5,801	2,567	19,546	38,406	_	_	66,320
 loans and receivables included in Amounts due from immediate holding company 	1,827	270	350	640	5,323	1,640	-	10,050
as trading securities - included in Amounts due from	-	-	-	-	2	15	-	17
fellow subsidiaries classified as: - available-for-sale securities - financial assets designated at	-	-	-	-	-	2,119	-	2,119
fair value						221		221
	1,827	6,351	3,896	23,930	53,715	11,796		101,515

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(f) Liquidity risk (continued)

(i) Contractual maturity (continued)

Bank

			Due	20 Due	112 Due			
		Due	between	between	between	Due		
	Repayable	within		3 months to	1 year to	after	l la data d	T-4-1
	on demand HK\$'M	1 month HK\$'M	3 months HK\$'M	1 year HK\$'M	5 years HK\$'M	5 years HK\$'M	Undated HK\$'M	Total HK\$'M
	πψινι	Iπψw	IIIΨW	πιφινι	πφιν	πφπ	πψπ	πφν
Assets								
Cash and balances with banks, central								
banks and other financial institutions	20,331	-	-	-	_	-	-	20,331
Placements with banks and other								
financial institutions	537	46,660	47,572	47,581	1,222	-	(1)	143,571
Hong Kong SAR Government								
certificates of indebtedness	-	-	-	-	-	-	32,481	32,481
Trading assets	-	1,510	4,172	9,273	8,851	4,103	501	28,410
Financial assets designated at								
fair value	-	-	-	-	110	3,106	-	3,216
Advances to customers	16,148	61,801	29,937	52,964	109,656	125,823	(943)	395,386
Investment securities	-	18,306	32,919	56,861	59,158	6,548	520	174,312
Amounts due from group companies	14,388	36,383	12,929	16,978	18,500	14,306	(1,585)	111,899
Others	337	4,096	9,364	540	38		9,069	23,444
Total Assets	51,741	168,756	136,893	184,197	197,535	153,886	40,042	933,050
Liabilities								
Hong Kong SAR currency notes in								
circulation	_	_	_	_	_	_	32,481	32,481
Deposits and balances of banks and							,	,
other financial institutions	10,798	444	62	52	_	-	-	11,356
Deposits from customers	487,709	97,610	86,704	81,596	1,826	42	_	755,487
Trading liabilities	_	21,599	109	447	50	86	774	23,065
Financial liabilities designated at								
fair value	-	818	924	1,372	468	30	-	3,612
Debt securities in issue	-	320	3,586	6,100	-	-	-	10,006
Amounts due to group companies	10,754	3,414	5,715	3,081	1,143	2,042	-	26,149
Subordinated liabilities	-	-	-	-	-	11,267	-	11,267
Others	6,395	4,939	5,222	1,010			235	17,801
Total Liabilities	515,656	129,144	102,322	93,658	3,487	13,467	33,490	891,224

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(f) Liquidity risk (continued)

(i) Contractual maturity (continued)

Bank (continued)

				20	12			
	Repayable on demand	Due within 1 month	Due between 1 month to 3 months	Due between 3 months to 1 year	Due between 1 year to 5 years	Due after 5 years	Undated	Total
Of which:								
Certificates of deposit held - included in Trading assets - included in Investment securities as	-	4	452	590	33	-	-	1,079
available-for-sale securities		6,603	11,663	10,634	2,856			31,756
		6,607	12,115	11,224	2,889			32,835
Treasury bills (including Exchange Fund Bills)								
included in Trading assets included in Investment securities as	-	1,341	3,348	3,988	25	-	-	8,702
available-for-sale securities		4,994	15,007	13,506				33,507
		6,335	18,355	17,494	25			42,209
Debt securities - included in Trading assets	_	_	291	4,278	8,725	4,075	_	17,369
included in Financial assets designated at fair value		_		-,	110	3,106	_	3,216
included in Investment securities classified as:					110	0,100		0,210
available-for-sale securitiesloans and receivables	-	6,116 593	6,249 -	28,611 4,110	52,182 4,120	6,548 -	-	99,706 8,823
 included in Amounts due from fellow subsidiaries classified as: 				,	•			·
available-for-sale securitiesfinancial assets designated at	-	-	-	-	-	1,305	-	1,305
fair value						98		98
		6,709	6,540	36,999	65,137	15,132		130,517

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(f) Liquidity risk (continued)

(i) Contractual maturity (continued)

Bank (continued)

				20	11			
			Due	Due	Due			
	Danayahla	Due within	between	between 3 months to	between	Due after		
	Repayable on demand	witnin 1 month	3 months	3 months to 1 year	1 year to 5 years	aner 5 years	Undated	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Assets								
Cash and balances with banks, central								
banks and other financial institutions	21,676	-	-	-	_	-	-	21,676
Placements with banks and other								
financial institutions	474	53,304	36,128	45,070	1,504	-	(3)	136,477
Hong Kong SAR Government								
certificates of indebtedness	-	-	-	-	_	-	31,401	31,401
Trading assets	-	6,406	4,531	10,294	10,109	4,027	10	35,377
Financial assets designated at								
fair value	-	-	-	38	344	3,893	-	4,275
Advances to customers	9,384	56,002	40,464	54,663	106,539	111,447	(1,022)	377,477
Investment securities	-	12,021	25,611	45,430	48,144	1,640	417	133,263
Amounts due from group companies	6,335	43,052	16,279	6,213	11,512	3,439	-	86,830
Others	322	3,789	6,349	404	275	56	9,808	21,003
Total Assets	20 101	17/57/	100.060	160 110	170 /07	104 500	40.611	047 770
Total Assets	38,191	174,574	129,362	162,112	178,427	124,502	40,611	847,779
Liabilities								
Hong Kong SAR currency notes in								
circulation	_	_	_	_	_	_	31,401	31,401
Deposits and balances of banks and							,	- 1, 1-1
other financial institutions	11,156	3,484	81	13	_	_	_	14,734
Deposits from customers	415,659	130,851	85,580	38,898	1,419	18	_	672,425
Trading liabilities	_	23,972	109	543	13	1	_	24,638
Financial liabilities designated at		,						,
fair value	_	194	1,329	1,353	611	-	-	3,487
Debt securities in issue	_	8,634	2,930	1,701	_	_	_	13,265
Amounts due to group companies	3,333	3,028	6,104	1,782	1,916	1,696	-	17,859
Subordinated liabilities	_	· _	-	-	_	13,100	_	13,100
Others	5,510	3,515	8,535	1,922	_	44	223	19,749
Total Liabilities	435,658	173,678	104,668	46,212	3,959	14,859	31,624	810,658

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(f) Liquidity risk (continued)

(i) Contractual maturity (continued)

Bank (continued)

				20	11			
			Due	Due	Due			
		Due	between	between	between	Due		
	Repayable on demand	within 1 month	1 month to 3 months	3 months to	1 year to 5 years	after 5 voors	Undated	Total
	on demand	i illolitli	3 IIIOIIIIIS	1 year	o years	5 years	Unualeu	TOTAL
Of which:								
Certificates of deposit held								
 included in Trading assets 	_	52	54	1,502	412	100	_	2,120
 included in Investment securities as 				.,				_, v
available-for-sale securities	_	4,532	6,861	7,979	4,415	_	_	23,787
	_	4,584	6,915	9,481	4,827	100	_	25,907
		====	====	====	====			====
Treasury bills (including Exchange								
Fund Bills)								
- included in Trading assets	-	5,828	3,183	4,727	-	-	-	13,738
- included in Investment securities as			45.000	47.005				0.4.54.0
available-for-sale securities		1,418	15,833	17,265				34,516
		7,246	19,016	21,992				48,254
Debt securities								
- included in Trading assets	-	280	979	3,706	9,640	3,908	-	18,513
- included in Financial assets								
designated at fair value	-	-	-	38	344	3,893	-	4,275
- included in Investment securities								
classified as: - available-for-sale securities		E 001	0.567	10.546	00.406			66 000
available-for-sale securitiesloans and receivables	_	5,801 270	2,567 350	19,546 640	38,406 5,323	1,640	_	66,320 8,223
 included in Amounts due from 	_	210	330	040	3,323	1,040	_	0,220
immediate holding company as								
trading securities	_	_	_	_	2	15	_	17
 included in Amounts due from fellow 					_	10		.,
subsidiaries classified as:								
 available-for-sale securities 	_	_	_	_	_	2,119	_	2,119
financial assets designated at						,		,
fair value	_	_	_	_	_	221	_	221
	_	6,351	3,896	23,930	53,715	11,796	_	99,688
		====	====	==,555	====	====		====

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(f) Liquidity risk (continued)

(ii) Behavioural maturity of financial liabilities on a discounted basis

The cash flows presented in note 37(f)(i) reflect the cash flows which will be contractually payable over the residual maturity of the instruments. In practice, however, liability instruments behave differently from their contractual terms and typically, short term customer accounts extend to a longer period than their contractual maturity. The Bank and its subsidiaries' expectation of when such liabilities are likely to become payable is provided in the table below. No information has been presented for financial liabilities which will become payable on their contractual due dates.

Consolidated

			2012		
		Between 3 months	Between 1 year		
	Within 3 months	and 1 year	and 5 years	After 5 years	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Deposits and balances of banks and					
other financial institutions	11,509	772	_	_	12,281
Deposits from customers	135,216	112,815	508,558		756,589
Total	146,725	113,587	508,558		768,870
			2011		
		Between 3 months	Between 1 year		
	Within 3 months	and 1 year	and 5 years	After 5 years	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Deposits and balances of banks and					
other financial institutions	14,996	13	720	_	15,729
Deposits from customers	132,251	118,875	421,814		672,940
Total	147,247	118,888	422,534		688,669

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(f) Liquidity risk (continued)

(ii) Behavioural maturity of financial liabilities on a discounted basis (continued)

Bank

	Within 3 months HK\$'M	Between 3 months and 1 year HK\$'M	2012 Between 1 year and 5 years HK\$'M	After 5 years HK\$'M	Total HK\$'M
Deposits and balances of banks and	44.004	50			44.050
other financial institutions	11,304	52	_	-	11,356
Deposits from customers	134,479	112,456	508,552		755,487
Total	145,783	112,508	508,552		766,843
	Within 3 months HK\$'M	Between 3 months and 1 year HK\$'M	2011 Between 1 year and 5 years HK\$'M	After 5 years HK\$'M	Total HK\$'M
	ΠΛΦ Ι۷Ι	ΠΚΦ Ι۷Ι	ΠΛΦ Ι۷Ι	ΠΛΦ Ι۷Ι	ΠΛΦ Ι۷Ι
Deposits and balances of banks and					
other financial institutions	14,721	13	-	-	14,734
Deposits from customers	131,864	118,750	421,811		672,425
Total	146,585	118,763	421,811		687,159

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(f) Liquidity risk (continued)

(iii) Financial liabilities excluding derivative financial instruments on an undiscounted basis

The following tables show the cash flows by remaining contractual maturity on an undiscounted basis for the Bank's financial liabilities. The financial liability balances in the tables will not agree to the balances reported in the balance sheets as the tables incorporate all contractual cash flows, on an undiscounted basis, relating to both principal and interest payments. The cash flows presented in the tables reflect the cash flows which will be contractually payable over the residual maturity of the instruments. In practice, however, the liability instruments behave differently from their contractual terms and typically, for short term customer accounts, extend to a longer period than their contractual maturity.

Consolidated

			Due	2012 Due			
			between	between	Due		
	Repayable		3 months to	1 year to	after		
	on demand	3 months	1 year	5 years	5 years	Undated	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Deposits and balances of banks							
and other financial institutions	10,798	715	772	_	_	_	12,285
Deposits from customers	487,710	185,600	83,138	2,005	84	_	758,537
Trading liabilities	_	20,818	_	_	_	774	21,592
Financial liabilities designated at							
fair value	_	1,777	1,390	497	28	_	3,692
Debt securities in issue	-	3,918	6,161	_	-	-	10,079
Amounts due to group companies	10,031	8,078	3,326	1,267	2,042	-	24,744
Subordinated liabilities	-	-	536	2,153	12,217	-	14,906
Others	5,744	9,750	1,114	11	244	33,095	49,958
	514,283	230,656	96,437	5,933	14,615	33,869	895,793
				2011			
			Due	Due			
			between	between	Due		
	Repayable	Due within	3 months to	1 year to	after	111-41	Takal
	on demand	3 months HK\$'M	1 year	5 years	5 years	Undated	Total
	HK\$'M			1 11/0/11/1	111/021/4	111/02/14	111/01/11
		Τ ΙΤΑΨ ΙΝΙ	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Deposits and balances of banks		ΠΨΨ	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Deposits and balances of banks and other financial institutions	11,156	3,845	нк\$'м	нк\$'м 720	HK\$'M -	HK\$'M –	<i>нк</i> \$'м 15,734
•	11,156 415,667				HK\$'M - 18	HK\$'M - -	
and other financial institutions		3,845	13	720	_	HK\$'M - - -	15,734
and other financial institutions Deposits from customers		3,845 217,161	13	720	_	HK\$'M - - -	15,734 673,778
and other financial institutions Deposits from customers Trading liabilities		3,845 217,161	13	720	_	HK\$'M - - -	15,734 673,778
and other financial institutions Deposits from customers Trading liabilities Financial liabilities designated at		3,845 217,161 23,137	13 39,481 -	720 1,451 –	_	HK\$*M - - - -	15,734 673,778 23,137
and other financial institutions Deposits from customers Trading liabilities Financial liabilities designated at fair value		3,845 217,161 23,137 1,593	13 39,481 - 1,336	720 1,451 –	_	HK\$*M	15,734 673,778 23,137 3,547
and other financial institutions Deposits from customers Trading liabilities Financial liabilities designated at fair value Debt securities in issue Amounts due to group companies Subordinated liabilities	415,667 - - - 2,882 -	3,845 217,161 23,137 1,593 11,570 7,913 2	13 39,481 - 1,336 1,712 3,297 528	720 1,451 - 618 - 2,449 2,187	- 18 - - - 1,696 14,943	- - - -	15,734 673,778 23,137 3,547 13,282 18,237 17,660
and other financial institutions Deposits from customers Trading liabilities Financial liabilities designated at fair value Debt securities in issue Amounts due to group companies	415,667 - - -	3,845 217,161 23,137 1,593 11,570 7,913	13 39,481 - 1,336 1,712 3,297	720 1,451 - 618 - 2,449	- 18 - - - 1,696	- - - -	15,734 673,778 23,137 3,547 13,282 18,237
and other financial institutions Deposits from customers Trading liabilities Financial liabilities designated at fair value Debt securities in issue Amounts due to group companies Subordinated liabilities	415,667 - - - 2,882 -	3,845 217,161 23,137 1,593 11,570 7,913 2	13 39,481 - 1,336 1,712 3,297 528	720 1,451 - 618 - 2,449 2,187	- 18 - - - 1,696 14,943	- - - -	15,734 673,778 23,137 3,547 13,282 18,237 17,660

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(f) Liquidity risk (continued)

(iii) Financial liabilities excluding derivative financial instruments on an undiscounted basis (continued)

Bank

			Due	2012 Due			
			between	between	Due		
	Repayable	Due within	3 months to	1 year to	after		
	on demand	3 months	1 year	5 years	5 years	Undated	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Deposits and balances of banks							
and other financial institutions	10,798	509	52	-	-	-	11,359
Deposits from customers	487,709	184,861	82,777	2,000	84	-	757,431
Trading liabilities	-	20,818	-	-	-	774	21,592
Financial liabilities designated at							
fair value	-	1,777	1,390	497	28	-	3,692
Debt securities in issue	-	3,918	6,161	-	-	-	10,079
Amounts due to group companies	10,754	9,132	3,081	1,165	2,042	-	26,174
Subordinated liabilities	_	-	536	2,153	12,217	_	14,906
Others	5,735	9,636	968			32,716	49,055
	514,996	230,651	94,965	5,815	14,371	33,490	894,288
				2011			
			Due	Due			
	Repayable	D	between	between	Due		
			3 months to	1 year to	after 5 vears	Undated	Total
	on demand HK\$'M	3 months HK\$'M	3 months to 1 year HK\$'M	5 years HK\$'M	after 5 years HK\$'M	Undated HK\$'M	Total HK\$'M
	on demand	3 months	1 year	5 years	5 years		
Deposits and balances of banks	on demand HK\$'M	3 months HK\$'M	1 year HK\$'M	5 years	5 years		HK\$'M
and other financial institutions	on demand HK\$'M	3 months HK\$'M 3,569	1 year HK\$'M	5 years HK\$'M	5 years HK\$'M -		нк\$ [*] М
and other financial institutions Deposits from customers	on demand HK\$'M	3 months HK\$'M 3,569 216,780	1 year HK\$'M	5 years	5 years		нк\$'м 14,738 673,261
and other financial institutions Deposits from customers Trading liabilities	on demand HK\$'M	3 months HK\$'M 3,569	1 year HK\$'M	5 years HK\$'M	5 years HK\$'M -		нк\$ [*] М
and other financial institutions Deposits from customers	on demand HK\$'M	3 months HK\$'M 3,569 216,780	1 year HK\$'M	5 years HK\$'M	5 years HK\$'M -		нк\$'м 14,738 673,261
and other financial institutions Deposits from customers Trading liabilities Financial liabilities designated at	on demand HK\$'M	3 months HK\$'M 3,569 216,780 23,137 1,593	1 year HK\$'M 13 39,356 — 1,336	5 years HK\$'M — 1,448 —	5 years HK\$'M -		14,738 673,261 23,137 3,547
and other financial institutions Deposits from customers Trading liabilities Financial liabilities designated at fair value Debt securities in issue	on demand HK\$'M 11,156 415,659 -	3 months HK\$'M 3,569 216,780 23,137 1,593 11,570	1 year HK\$'M 13 39,356 — 1,336 1,712	5 years HK\$'M - 1,448 - 618	5 years HK\$'M - 18 -		14,738 673,261 23,137 3,547 13,282
and other financial institutions Deposits from customers Trading liabilities Financial liabilities designated at fair value	on demand HK\$'M 11,156 415,659	3 months HK\$'M 3,569 216,780 23,137 1,593	1 year HK\$'M 13 39,356 — 1,336	5 years HK\$'M — 1,448 —	5 years HK\$'M -		14,738 673,261 23,137 3,547 13,282 17,866
and other financial institutions Deposits from customers Trading liabilities Financial liabilities designated at fair value Debt securities in issue Amounts due to group companies	on demand HK\$'M 11,156 415,659 -	3 months HK\$'M 3,569 216,780 23,137 1,593 11,570 9,136	1 year HK\$'M 13 39,356 - 1,336 1,712 1,785	5 years HK\$'M - 1,448 - 618 - 1,916	5 years HK\$'M - 18 - - - 1,696		14,738 673,261 23,137 3,547 13,282
and other financial institutions Deposits from customers Trading liabilities Financial liabilities designated at fair value Debt securities in issue Amounts due to group companies Subordinated liabilities	on demand HK\$'M 11,156 415,659 - - 3,333	3 months HK\$'M 3,569 216,780 23,137 1,593 11,570 9,136 2	1 year HK\$'M 13 39,356 - 1,336 1,712 1,785 528	5 years HK\$'M - 1,448 - 618 - 1,916	5 years HK\$'M - 18 1,696 14,943	HK\$'M	14,738 673,261 23,137 3,547 13,282 17,866 17,660

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(f) Liquidity risk (continued)

(iv) Derivative financial instruments on an undiscounted basis

The following tables show the maturity of derivative financial instruments including those net settled derivative contracts in a net liability position, together with the pay leg of gross settled contracts regardless of whether the overall contract is in an asset or liability position. The receiving leg is not shown in this table and as a result the derivative amounts in this table are inflated by their exclusion.

Consolidated

	Due within 3 months HK\$'M	Due between 3 months to 1 year HK\$'M	Due between 1 year to 5 years HK\$'M	Due after 5 years HK\$'M	Total HK\$'M
			2012		
Derivative financial instruments	731,255	532,200	26,824	6,061	1,296,340
			2011		
Derivative financial instruments	341,680	341,484	11,107	2,398	696,669
Bank					
	Due within	Due between 3 months to	Due between 1 year to	Due after	
	3 months HK\$'M	1 year HK\$'M	5 years HK\$'M	5 years HK\$'M	Total HK\$'M
			2012		
Derivative financial instruments	731,170	532,200	26,824	6,061	1,296,255
			2011		
Derivative financial instruments	341,680	341,484	11,107	2,398	696,669

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(g) Operational risk

Operational risk is the potential for loss arising from the failure of people, process or technology or the impact of external events. We seek to minimize our exposure to operational risk, subject to cost tradeoffs. Operational risk exposures are managed through a consistent set of management processes that drive risk identification, assessment, control and monitoring.

The Risk Committee (as delegated by the Board) oversees the management of operational risks across the Bank, supported by business and functional level committees. This formal structure of governance provides the Board with confidence that operational risks are being proactively identified and effectively managed.

The Risk Committee is responsible for setting and maintaining standards for operational risk management and measurement. In addition, specialist operational risk control owners have responsibility for the management of operational risk arising from the following Bank-wide activities: legal processes, people management, technology management, vendor management, property management, security management, accounting and financial control, tax management, corporate authorities and structure and regulatory compliance. Each risk control owner is responsible for identifying risks that are material to the Bank and for maintaining an effective control environment, which includes defining appropriate policies and procedures for approval by authorized risk committees.

The Country Operational Risk Committee ("CORC") is a sub-committee of the Risk Committee and is responsible for the supervision and management of operational risks across the Bank. CORC is also responsible for ensuring adequate and appropriate policies and procedures, and resources are in place for identification, assessment, monitoring, control and reporting of operational risks.

Compliance with operation risk policies and procedures is the responsibility of all managers within the Bank. Wholesale Bank and Consumer Bank have independent Operational Risk teams reporting to the Risk Function to ensure operational risk is effectively managed. These units are responsible for approving operational controls, ensuring compliance with policies and procedures in the business, monitoring material operational risk exposures, and providing guidance to the respective business areas on operational risk management.

(h) Reputational risk

Reputational risk is the potential for damage to the Bank's franchise, resulting in loss of earnings or adverse impact on market capitalisation as a result of stakeholders taking a negative view of the Bank or its actions.

Reputational risk could arise from the failure by the Bank to effectively mitigate the risks in its businesses including one or more of country, credit, liquidity, market, regulatory, legal or other operational risk. It may also arise from a failure to comply with environmental and social standards. Damage to the Bank's reputation could cause existing clients to reduce or cease to do business with the Bank and prospective clients to be reluctant to do business with the Bank. A failure to manage reputational risk effectively could materially affect the Bank's business, results of operations and prospects. All employees are responsible for day to day identification and management of reputational risk.

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(h) Reputational risk (continued)

The Risk Committee and its sub-committee, the Responsibility and Reputational Risk Committee, provides Bank-wide oversight on reputational risk, sets policy and monitors material risks. The Head of Corporate Affairs is the overall risk control owner for reputational risk. The Executive Committee ("EXCO") provide additional oversight of reputational risk on behalf of the Board.

The Head of Corporate Affairs as risk control owner is responsible for the protection of the Bank's reputation with the support of the country management team. The Head of Corporate Affairs and Chief Executive Officer must actively:

- Promote awareness and application of the Bank's policies and procedures regarding reputational risk.
- Encourage business and functions to take account of the Bank's reputation in all decision-making, including dealings with customers and suppliers.
- Implement effective in-country reporting systems to ensure they are aware of all potential issues in tandem with respective business committees.
- Promote effective, proactive stakeholder management through ongoing engagement.

(i) Pension risk

Pension risk is the potential for loss due to having to meet an actuarially assessed shortfall in the Bank's pension scheme. Pension risk exposure is not concerned with the financial performance of the Bank's pension scheme but is focused upon the risk to the Bank's financial position arising from the need to meet pension scheme funding obligations. The risk assessment is focused on our obligations towards the Bank's pension scheme, ensuring that our funding obligation is comfortably within our financial capacity. Pension risk is monitored on a quarterly basis taking account of the actual variations in asset values and updated expectations regarding the progression of the pension fund assets and liabilities.

The Pension Risk Committee is the body responsible for governance of pension risk and it receives its authority from EXCO.

(j) Capital management

The HKMA sets and monitors capital requirements for the Bank and certain of its subsidiaries specified by the HKMA. In implementing current capital requirements, the HKMA requires the Bank to maintain a prescribed ratio of total capital to total risk-weighted assets. The Bank calculates its capital adequacy ratios in accordance with the Banking (Capital) Rules of the Hong Kong Banking Ordinance.

In addition to meeting the regulatory requirements, the Bank's primary objectives when managing capital are to safeguard the Bank and its subsidiaries' ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders, by pricing products and services commensurately with the level of risk and by securing access to finance at a reasonable cost. The Bank actively and regularly reviews and manages its capital structure to maintain a balance between the higher shareholder returns that might otherwise be possible with greater gearing and the advantages and security afforded by a sound capital position, and makes adjustments to the capital structure in light of changes in economic conditions.

(Expressed in millions of Hong Kong dollars)

37 Risk management (continued)

(j) Capital management (continued)

The process of allocating capital to specific operations and activities is undertaken by the Asset and Liability Committee and is reviewed regularly by the Board of Directors.

Consistent with industry practice, the Bank monitors its capital structure on the basis of the capital adequacy ratio and there have been no material changes in the Bank's policy on the management of capital during the year.

The Bank and its subsidiaries have complied with all externally imposed capital requirements throughout the years ended 31 December 2012 and 2011.

For the capital ratios as at 31 December 2012 and 2011, the Bank uses both the advanced internal ratings-based approach and standardized approach to calculate its credit risk for non-securitization exposures. The Bank adopts the internal ratings-based (securitization) approach to calculate its credit risk for securitization exposures.

For the calculation of its capital charge for market risk, the Bank uses an internal models approach for two guaranteed funds and the standardized (market risk) approach for other exposures. In addition, the Bank adopts the standardized (operational risk) approach for operational risk.

The Bank's consolidated capital as at 31 December 2012 and 2011 consists of core capital after deductions of HK\$34,061 million (2011: HK\$28,612 million) and supplementary capital after deductions of HK\$10,441 million (2011: HK\$11,708 million). Supplementary capital includes subordinated debt, and collective impairment allowances for impaired assets.

38 Financial instruments

(a) Valuation of financial instruments carried at fair value

Valuation of financial assets and liabilities held at fair value are subject to a review independent of the business by Valuation Control. For those financial assets and liabilities whose fair value is determined by reference to externally quoted prices or market observable pricing inputs to valuation models, an assessment is made against external market data and consensus services. Financial instruments held at fair value in the balance sheet have been classified into a valuation hierarchy that reflects the significance of the inputs used in the fair value measurements.

Valuation methodologies

The valuation hierarchy, and the types of instruments classified into each level within that hierarchy, is set out below:

	Level 1	Level 2	Level 3
Fair value determined using:	Unadjusted quoted price in an active market for identical assets and liabilities	Valuation models with directly or indirectly market observable inputs	Valuation models using significant non-market observable inputs
Types of financial assets	Actively traded government and agency securities Listed equities Quoted derivative instruments	Corporate and other government bonds and loans Over-the-counter derivatives Asset backed securities	Asset backed securities Corporate bonds and loans in illiquid markets Unlisted equities
Types of financial liabilities	Short positions in actively traded government and agency securities Short positions in listed equities Quoted derivative instruments	Structured customer deposits Over-the-counter derivatives	Over-the-counter derivatives with unobservable parameters

(Expressed in millions of Hong Kong dollars)

38 Financial instruments (continued)

(a) Valuation of financial instruments carried at fair value (continued)

The tables below show the classification of financial instruments held at fair value into the valuation hierarchy set out above as at 31 December:

Consolidated

			2012	
	Level 1	Level 2	Level 3	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Trading assets				
Trading securities	24,871	2,780	_	27,651
Advances to customers	_ 1,07 1	186	_	186
 Positive fair values of trading derivatives 	2	567	8	577
•	2	307	O	377
Amounts due from immediate holding company	0	0.000	4	0.007
Positive fair values of trading derivatives	3	6,093	1	6,097
 Positive fair values of hedging derivatives 	_	911	_	911
Amounts due from fellow subsidiaries				
 Available-for-sale debt securities 	_	_	1,305	1,305
 Debt securities designated at fair value 	_	_	98	98
 Positive fair values of trading derivatives 	_	81	_	81
Financial assets designated at fair value				
 Debt securities 	_	2,668	548	3,216
Available-for-sale securities				
Treasury bills (including Exchange Fund				
Bills)	33,507	_	_	33,507
Certificates of deposit held	-	31,756	_	31,756
Debt securities	28,692	71,014	_	99,706
 Equity shares, net of impairment 	90	71,014	430	520
Equity shares, her of impairment				
	07.405	440.050	0.000	005.044
Total assets measured at fair value	87,165	116,056	2,390	205,611
Trading liabilities				
 Short positions in securities 	22,229	_	_	22,229
 Negative fair values of trading derivatives 		838	1	839
Financial liabilities designated at fair value				
Structured customer deposits	_	3,574	_	3,574
Debt securities issued	_	38	_	38
Amounts due to immediate holding company		00		00
		100		100
Structured deposits designated at fair value	_	186	_	186
 Negative fair values of trading derivatives 	2	5,632	8	5,642
 Negative fair values of hedging derivatives 	_	1,654	_	1,654
Amounts due to fellow subsidiaries				
 Negative fair values of trading derivatives 	_	76	_	76
 Negative fair values of hedging derivatives 	-	264	_	264
Total liabilities measured at fair value	22,231	12,262	9	34,502
				=====

There were no significant transfers between level 1 and level 2 instruments in 2012.

(Expressed in millions of Hong Kong dollars)

38 Financial instruments (continued)

(a) Valuation of financial instruments carried at fair value (continued)

Consolidated (continued)

		2011	Restated	
	Level 1	Level 2	Level 3	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Trading assets				
 Trading securities 	30,410	3,971	_	34,381
 Placement with banks and other financial 				
institutions	-	21	_	21
 Advances to customers 	_	185	_	185
 Positive fair values of trading derivatives 	45	745	_	790
Amounts due from immediate holding company				
 Trading debt securities 	_	17	_	17
 Positive fair values of trading derivatives 	6	2,563	_	2,569
 Positive fair values of hedging derivatives 	_	802	_	802
Amounts due from fellow subsidiaries				
 Available-for-sale debt securities 	_	_	2,119	2,119
 Debt securities designated at fair value 	-	_	221	221
 Positive fair values of trading derivatives 	-	103	_	103
 Positive fair values of hedging derivatives 	-	99	_	99
Financial assets designated at fair value				
 Debt securities 	_	2,659	1,616	4,275
Available-for-sale securities				
 Treasury bills (including Exchange Fund 				
Bills)	34,516	_	_	34,516
 Certificates of deposit held 	_	23,787	_	23,787
 Debt securities 	15,757	50,563	_	66,320
 Equity shares, net of impairment 	99	_	318	417
Other assets				
 Positive fair values of hedging derivatives 	_	56	_	56
Total assets measured at fair value	80,833	85,571	4,274	170,678
Trading liabilities				
 Short positions in securities 	23,855	_	_	23,855
 Negative fair values of trading derivatives 	6	777	_	783
Financial liabilities designated at fair value				
 Structured customer deposits 	_	2,615	_	2,615
 Debt securities issued 	_	872	_	872
Amounts due to immediate holding company				
 Negative fair values of trading derivatives 	2	3,375	_	3,377
 Negative fair values of hedging derivatives 	_	1,358	_	1,358
Amounts due to fellow subsidiaries		,		,
 Negative fair values of trading derivatives 	_	12	_	12
 Negative fair values of hedging derivatives 	_	16	_	16
Total liabilities measured at fair value	23,863	9,025		32,888
iotal nabilities illeasured at fall Value		=====		=====

There were no significant transfers between level 1 and level 2 instruments in 2011.

(Expressed in millions of Hong Kong dollars)

38 Financial instruments (continued)

(a) Valuation of financial instruments carried at fair value (continued)

Bank

			2012	
	Level 1	Level 2	Level 3	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Trading assets				
-	04 071	2 790		27.651
- Trading securities	24,871	2,780	_	27,651
- Advances to customers	_	186	_	186
Positive fair values of trading derivatives	2	563	8	573
Amounts due from immediate holding company				
 Positive fair values of trading derivatives 	3	6,089	1	6,093
 Positive fair values of hedging derivatives 	_	911	_	911
Amounts due from fellow subsidiaries				
 Available-for-sale debt securities 	_	_	1,305	1,305
 Debt securities designated at fair value 	_	_	98	98
 Positive fair values of trading derivatives 	_	81	_	81
Financial assets designated at fair value				
 Debt securities 	_	2,668	548	3,216
Available-for-sale securities				
 Treasury bills (including Exchange Fund 				
Bills)	33,507	_	_	33,507
 Certificates of deposit held 	· _	31,756	_	31,756
 Debt securities 	28,692	71,014	_	99,706
 Equity shares, net of impairment 	90		430	520
Equity Granos, flot of impairmont				
Total assets measured at fair value	87,165	116,048	2,390	205,603
Trading liabilities				
_	22,229			22,229
Short positions in securities	22,229	835	1	836
Negative fair values of trading derivatives Figure in line litities designed at fair value.	_	033	ı	030
Financial liabilities designated at fair value		0.574		0.574
Structured customer deposits	_	3,574	_	3,574
- Debt securities issued	_	38	_	38
Amounts due to immediate holding company				
 Structured deposits designated at fair value 	_	186	_	186
 Negative fair values of trading derivatives 	2	5,632	8	5,642
 Negative fair values of hedging derivatives 	_	1,654	_	1,654
Amounts due to fellow subsidiaries				
 Negative fair values of trading derivatives 	_	76	_	76
 Negative fair values of hedging derivatives 		264		264
Total liabilities measured at fair value	22,231	12,259	9	34,499
Total Habitato Historia de la Para				=====

There were no significant transfers between level 1 and level 2 instruments in 2012.

(Expressed in millions of Hong Kong dollars)

38 Financial instruments (continued)

(a) Valuation of financial instruments carried at fair value (continued)

Bank (continued)

	2011 Restated			
	Level 1	Level 2	Level 3	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Trading assets				
- Trading securities	30,410	3,971	_	34,381
 Placement with banks and other financial 	50,410	0,571		0-7,001
institutions	_	21	_	21
Advances to customers	_	185	_	185
 Positive fair values of trading derivatives 	45	745	_	790
Amounts due from immediate holding company				
 Trading debt securities 	_	17	_	17
 Positive fair values of trading derivatives 	6	2,560	_	2,566
 Positive fair values of hedging derivatives 	_	802	_	802
Amounts due from fellow subsidiaries				
 Available-for-sale debt securities 	_	_	2,119	2,119
 Debt securities designated at fair value 	_	_	221	221
 Positive fair values of trading derivatives 	_	103	_	103
 Positive fair values of hedging derivatives 	_	99	_	99
Financial assets designated at fair value				
 Debt securities 	_	2,659	1,616	4,275
Available-for-sale securities				
 Treasury bills (including Exchange Fund 				
Bills)	34,516	_	_	34,516
 Certificates of deposit held 	_	23,787	_	23,787
 Debt securities 	15,757	50,563	_	66,320
 Equity shares, net of impairment 	99	_	318	417
Other assets				
 Positive fair values of hedging derivatives 		56		56
Total assets measured at fair value	80,833	85,568	4,274	170,675
Trading liabilities				
Trading liabilities - Short positions in securities	23,855			22 055
 Negative fair values of trading derivatives 	23,655	- 777	_	23,855 783
Financial liabilities designated at fair value	O	111	_	700
Structured customer deposits	_	2,615	_	2,615
Debt securities issued	_	872	_	872
Amounts due to immediate holding company		0,2		012
Negative fair values of trading derivatives	2	3,375	_	3,377
 Negative fair values of hedging derivatives 	_	1,358	_	1,358
Amounts due to fellow subsidiaries		.,		.,000
Negative fair values of trading derivatives	_	12	_	12
Negative fair values of hedging derivatives	_	16	_	16
, g o				
Total liabilities measured at fair value	23,863	9,025	_	32,888
		=====		=====

There were no significant transfers between level 1 and level 2 instruments in 2011.

(Expressed in millions of Hong Kong dollars)

38 Financial instruments (continued)

(a) Valuation of financial instruments carried at fair value (continued)

The movements during the year for level 3 financial assets and liabilities are as follows:

Consolidated and Bank

	Financial assets designated at fair value HK\$'M	Amounts due from immediate holding company HK\$'M	Amounts due from fellow subsidiaries (Note) HK\$'M	2012 Available- for-sale securities HK\$'M	Derivatives financial instruments HK\$'M	Total level 3 assets HK\$'M
Financial assets At 1 January 2012 Total gains recognised in the	1,616	-	2,340	318	-	4,274
income statement	76	1	35	_	8	120
Total gains recognised in the available-for-sale investment reserve Purchases Sales Settlements Transferred into level 3	- - (700) 113	- - - -	8 - - (980)	30 217 (31) (104)	- - - -	38 217 (31) (1,784) 113
Transferred out of level 3	(557)	-	-	-	_	(557)
At 31 December 2012	548	1	1,403	430	8	2,390
Total gains/(losses) recognised in the income statement relating to assets held at 31 December 2012	5	1	(1)		8	13
			to im	holding	Derivatives financial astruments HK\$'M	Total level 3 liabilities HK\$'M
Financial liabilities At 1 January 2012 Total losses recognised in the inco	ome staten	nent		- 8	- 1	_ 9
At 31 December 2012				8	1	9
Total losses recognised in the incolliabilities held at 31 December 2		nent relating	to	8	1	9

(Expressed in millions of Hong Kong dollars)

38 Financial instruments (continued)

(a) Valuation of financial instruments carried at fair value (continued)

	2011			
	Financial	Amounts due		
	assets	from fellow	Available-	
	designated at	subsidiaries	for-sale	Total level
	fair value	(Note)	securities	3 assets
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Financial assets				
At 1 January 2011	2,385	3,309	277	5,971
Total gains recognised in the				
income statement	31	10	240	281
Total gains/(losses) recognised in the				
available-for-sale investment reserve	_	13	(38)	(25)
Purchases	_	_	526	526
Sales	_	_	(491)	(491)
Settlements	(1,133)	(992)	(196)	(2,321)
Transferred into level 3	824	_	_	824
Transferred out of level 3	(491)	_	_	(491)
At 31 December 2011	1,616	2,340	318	4,274
Total gains recognised in the income statement				
relating to assets held at 31 December 2011	6	18	_	24

Note: Amounts due from fellow subsidiaries included debt securities which are available for sale and designated at fair value.

Sensitivities in respect of the fair values of level 3 assets and liabilities are as follows:

Consolidated and Bank

2012						
Held at fair v	alue through	profit or loss	Availa	Available-for-sale securities		
Net	Favourable	Unfavourable	Net	Favourable	Unfavourable	
exposure	changes	changes	exposure	changes	changes	
HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	
1	1	1	_	_	_	
98	98	98	1,305	1,310	1,300	
548	554	542	_	_	_	
_	_	_	430	473	387	
7	7	7	_	_	_	
(8)	(8)	(8)	_	_	_	
646	652	640	1,735	1,783	1,687	
	Net exposure HK\$'M 1 98 548 - 7 (8)	Net exposure Favourable changes HK\$'M HK\$'M 1 1 98 98 548 554 - - 7 7 (8) (8)	Held at fair value through profit or loss Net exposure exposure HK\$'M Favourable changes changes hK\$'M Unfavourable changes changes hK\$'M 1 1 1 98 98 98 548 554 542 - - - 7 7 7 (8) (8) (8)	Held at fair value through profit or loss Availate Net exposure changes changes HK\$'M Favourable changes changes changes hK\$'M Net exposure exposure hK\$'M 1 1 1 - 98 98 98 1,305 548 554 542 - - - 430 7 7 7 - (8) (8) (8) -	Held at fair value through profit or loss Available-for-sale sectors Net exposure changes changes HK\$'M Favourable HK\$'M Net exposure changes changes exposure changes HK\$'M <	

(Expressed in millions of Hong Kong dollars)

38 Financial instruments (continued)

(a) Valuation of financial instruments carried at fair value (continued)

		2011				
	Held at fair	value through _l	profit or loss	Available-for-sale securities		
	Net exposure HK\$'M	Favourable changes HK\$'M	Unfavourable changes HK\$'M	Net exposure HK\$'M	Favourable changes HK\$'M	Unfavourable changes HK\$'M
Amounts due from fellow						
subsidiaries	221	222	220	2,119	2,126	2,112
Debt securities	1,616	1,631	1,601	_	_	_
Equity shares				318	350	286
	1,837	1,853	1,821	2,437	2,476	2,398

Where the fair value of financial instruments are measured using valuation techniques that incorporate one or more significant input which are based on unobservable market data, we apply stresses on these unobservable parameter inputs. A 10 per cent increase or decrease in correlation and credit sensitivities has been used to generate a range of reasonably possible alternative valuations. As of 31 December 2012, these stresses could have increased or decreased the fair values of financial instruments held at fair value by HK\$6 million (2011: HK\$16 million) and available-for-sale securities by HK\$48 million (2011: HK\$39 million).

(b) Valuation of financial instruments carried at amortized cost

All financial instruments are stated at fair value or amounts not materially different from their fair value as at 31 December 2012 and 2011.

The following sets out the Bank's basis of establishing the fair value of its financial assets and liabilities which are not carried at fair value. The basis for establishing the fair value of financial assets and liabilities held at fair value and of derivatives is set out in note 2(i) and note 2(j), respectively.

Cash and balances with banks, central banks and other financial institutions

The fair value of cash and balances with banks, central banks and other financial institutions is their carrying amounts.

(Expressed in millions of Hong Kong dollars)

38 Financial instruments (continued)

(b) Valuation of financial instruments carried at amortized cost (continued)

Placements with banks and other financial institutions

The fair value of floating rate placements and overnight deposits is their carrying amounts. The estimated fair value of fixed interest bearing deposits is based on discounted cash flows using the prevailing money market rates for debts with a similar credit risk and remaining maturity.

Advances to customers

Advances are net of provisions for impairment. The estimated fair value of advances represents the discounted amount of future cash flows expected to be received, including assumptions relating to prepayment rates and, where appropriate, credit spreads. Expected cash flows are discounted at current market rates to determine fair value.

Deposits and balances of banks, other financial institutions and customers

The estimated fair value of deposits with no stated maturity is the amount repayable on demand. The estimated fair value of fixed interest bearing deposits and other borrowings without quoted market prices is based on discounting cash flows using the prevailing market rates for debts with a similar credit risk and remaining maturity.

Debt securities in issue and subordinated liabilities

The aggregate fair values are calculated based on quoted market prices. For those securities where quoted market prices are not available, a discounted cash flow model is used based on a current market related yield curve appropriate for the remaining term to maturity.

(c) Transfers of financial assets

The Bank enters into collateralised repurchase agreements (repos). These transactions typically entitle the Bank and its counterparties to have recourse to assets similar to those provided as collateral in the event of a default. Securities sold subject to repos amounting to HK\$847 million continue to be recognised on the balance sheet as the Bank retains substantially the associated risk and rewards of these securities. The counterparty liability amounting to HK\$813 million is included in "Amounts due to immediate holding company".

39 Assets pledged as security for liabilities

Liabilities of the Bank amounting to HK\$23,043 million (2011: HK\$24,245 million) are secured by the deposit of assets, including assets pledged in respect of sale and repurchase agreements, to cover short positions and to facilitate settlement processes with clearing houses. The amount of assets pledged by the Bank to secure these liabilities is HK\$23,076 million (2011: HK\$24,247 million). These assets mainly comprise of debt securities and treasury bills.

(Expressed in millions of Hong Kong dollars)

39 Assets pledged as security for liabilities (continued)

In respect of reverse repurchase agreements and securities borrowing transactions, the fair value of collateral held by the Bank which was permitted to be sold or repledged amounted to HK\$3,333 million (2011: HK\$11,397 million). The fair value of such collateral actually sold or repledged by the Bank amounted to HK\$Nil million (2011: HK\$2,396 million).

These transactions are conducted under terms that are usual and customary to standard lending and stock borrowing activities.

40 Material related party transactions

In addition to the transactions and balances disclosed elsewhere in these financial statements, the Bank and its subsidiaries entered into the following material related party transactions. The transactions of the Bank are materially the same as those appearing in the consolidated financial statements in 2012 and 2011.

(a) Key management personnel remuneration

Remuneration for key management personnel of the Bank, including amounts paid to the directors as disclosed in note 8 is as follows:

		Restated
	2012	2011
	HK\$'M	HK\$'M
Short-term employee benefits	129	110
Post-employment benefits	12	11
Equity compensation benefits	48	33
	189	154

Total remuneration is included in staff costs (see note 4(g)).

(b) Credit facilities and loans to key management personnel

During the year, the Bank provided credit facilities to key management personnel of the Bank and their close family members and companies controlled or significantly influenced by them. The credit facilities were provided in the ordinary course of business and on substantially the same terms as for comparable transactions with persons of a similar standing or, where applicable, with other employees.

	2012 HK\$'M	Restated 2011 HK\$'M
Loan balances:		
At 1 January	441	1,240
At 31 December	124	441
A course to allow an elevision than constru	454	000
Average balance during the year	<u>454</u>	909
Income earned	4	8

(Expressed in millions of Hong Kong dollars)

40 Material related party transactions (continued)

(c) Share based payments

The Group operates a number of share based payment schemes for its directors and employees. The scheme lives referred to below relate to the remaining period in which options may be granted under the scheme by the Bank and its subsidiaries' ultimate holding company Standard Chartered PLC (SC PLC).

2011 Standard Chartered Share Plan (the 2011 Plan)

Approved by shareholders in May 2011, it is the Group's main share plan. The 2011 Plan is designed to deliver performance shares, deferred awards (share or cash) and restricted shares, giving the Group sufficient flexibility to meet the challenges of the changing regulatory and competitive environment. Discretionary share awards are a key part of both executive directors' and senior management's variable compensation and their significance as a proportion of potential total remuneration is one of the strongest indicators of the Group's commitment to pay for sustainable performance and aligning reward with the risk horizon. Performance and restricted share awards will generally be in the form of nil price options to acquire shares in SC PLC.

Performance shares

Awards of performance shares vest after a three-year period and are subject to a combination of three performance measures, Total Shareholder Return (TSR), Earnings per share (EPS) and Return on Risk Weighted Assets (RoRWA). The three performance measures are equally weighted with one third of the award depending on each measure, assessed independently. Performance share awards are subject to the Group's claw-back policy.

Restricted shares

Restricted share awards which are made outside of the annual performance process, as buy-out or retention mechanisms, are provided as restricted shares under the 2011 Plan. These awards vest in equal instalments on the second and the third anniversaries of the award date. In a few circumstances, some awards vest over a four-year period in equal tranches. This is in line with similar plans operated by the Group's competitors. Restricted share awards are not subject to an annual limit and do not have any performance conditions, although the Group's claw-back policy will apply.

1997/2006 Restricted Share Scheme (2006 RSS)/ 2007 Supplementary Restricted Share Scheme (2007 SRSS)

The Group's previous plans for delivering restricted shares were the 2006 RSS and 2007 SRSS, both of which are now replaced by the 2011 Plan. There are still unvested and vested awards outstanding under these plans which were previously used to deliver the deferred portion of annual performance awards and as an incentive to motivate and retain high performing employees. Awards will generally be in the form of nil cost options and do not have any performance conditions. Generally deferred restricted share awards vest equally over three years and for non-deferred awards half vests two years after the date of grant and the balance after three years. No further awards will be granted under the 2006 RSS and 2007 SRSS.

(Expressed in millions of Hong Kong dollars)

40 Material related party transactions (continued)

(c) Share based payments (continued)

2000 Executive Share Option Scheme (2000 ESOS)

The 2000 ESOS is designed to be internationally competitive and focus executive directors and their senior management teams on delivering long-term performance. An EPS performance criterion must be met before options can be exercised.

Executive share options to purchase ordinary shares in the ultimate holding company are exercisable after the third, but before the tenth anniversary of the date of grant. The exercise price per share is the share price at the date of grant and options can only be exercised if a performance condition is satisfied. No further awards may be granted to the employees of the Bank and its subsidiaries under the 2000 ESOS.

2001 Performance Share Plan (PSP)

The Group's previous plan for delivering performance shares was the PSP. Although the PSP was replaced in 2011, there are still outstanding vested and unvested awards under the plan.

Under the PSP, half the award is dependent upon TSR performance and the balance is subject to a target of defined EPS growth. Both measures use the same three-year period and are assessed independently. No further awards can be granted under the plan.

2004 Deferred Bonus Plan

Under the 2004 Deferred Bonus Plan, shares are conditionally awarded as part of the executive directors' annual performance award.

All Employee Sharesave Schemes (Sharesave)

Under the Sharesave schemes, employees have the choice of opening a three-year or five-year savings contract. Within a period of six months after the third or fifth anniversary, as appropriate, employees may purchase ordinary shares in the ultimate holding company. The price at which they may purchase shares is at a discount of up to 20 per cent on the share price at the date of invitation. There are no performance conditions attached to options granted under the Sharesave schemes.

2011 Standard Chartered Share Plan (the 2011 plan)

Performance Shares

Valuation

The fair value is based on the market value less an adjustment to take into account the expected dividends over the vesting period and the relevant performance condition applying to that portion of the award. The fair value of the TSR component is derived by discounting a third of the award that is subject to the TSR condition by the loss of expected dividends over the performance period together with the probability of meeting the TSR condition. The EPS fair value is derived by discounting one third of the award respectively by the loss of expected dividends over the performance period. The same approach is applied to calculate the RoRWA fair value for one third of the award. In respect of the EPS and RoRWA components only, the number of shares expected to vest is adjusted for actual performance when calculating the charge for the year. The same fair value is applied to awards made to both directors and employees of the Group.

(Expressed in millions of Hong Kong dollars)

40 Material related party transactions (continued)

(c) Share based payments (continued)

	201	2011		
Grant Date	21 December	13 March	20 September	6 May
Share price at grant date (£)	15.84	15.65	13.52	16.31
Shares granted	4,142	624,382	32,915	487,341
Vesting period (years)	3	3	3	3
Expected dividends (yield) (%)	3.7	3.5	4.0	3.7
Fair value (EPS) (£)	4.73	4.71	4.01	4.87
Fair value (RoRWA) (£)	4.73	4.71	4.01	4.87
Fair value (TSR) (£)	1.86	1.85	1.58	1.91

The expected dividend yield is based on the historical dividend yield over the three years prior to grant.

A reconciliation of movements for the year to 31 December 2012 and 2011 is shown below:

	2012	2011 No. of shares	
	No. of shares		
Outstanding at 1 January	503.484	_	
Granted	628,524	520,256	
Lapsed	(50,452)	(16,772)	
Outstanding at 31 December	1,081,556	503,484	
Weighted average remaining contractual life	8.83 years	9.45 years	
Exercisable at 31 December	_	_	

Restricted Share Awards

Valuation

The fair value is based on the market value less an adjustment to take into account the expected dividends over the vesting period. The same fair value is applied for awards made to both the directors and employees of the Group.

		2012				
Grant Date	21 December	19 September	20 June	13 March		
Share price at grant date (£)	15.84	14.82	14.17	15.65		
Shares granted	37,872	63,876	111,978	1,330,714		
Vesting period (years)	2/3, 1/2/3/4	2/3	2/3	2/3		
Expected dividends (yield) (%)	3.7	3.0	3.8	3.8		
Fair value (£)	14.46	13.76	12.91	14.26		

(Expressed in millions of Hong Kong dollars)

40 Material related party transactions (continued)

(c) Share based payments (continued)

	2011				
Grant Date	14 December	20 September	22 June		
Share price at grant date (£)	14.35	13.52	15.75		
Shares granted	19,642	65,422	51,941		
Vesting period (years)	2/3	2/3	2/3		
Expected dividends (yield) (%)	2.9	2.9	4.1		
Fair value (£)	13.36	12.59	14.25		

The expected dividend yield is based on the historical dividend yield for three years prior to grant.

A reconciliation of movements for the year to 31 December 2012 and 2011 is shown below:

	2012	2011
	No. of shares	
Outstanding at 1 January	127.005	
Outstanding at 1 January	137,005	107.005
Granted	1,544,440	137,005
Lapsed	(86,596)	
Outstanding at 31 December	1,594,849	137,005
Weighted average remaining contractual life	6.21 years	6.67 years
Exercisable at 31 December	_	

1997/2006 Restricted Share Scheme (2006 RSS)

No share awards were granted in 2012.

Valuation

The fair value is based on the market value less an adjustment to take into account the expected dividends over the vesting period.

	2011
Grant Date	10 March
Share price at grant date (£)	16.82
Shares granted	1,811,942
Vesting period (years)	1/2/3
Expected dividends (yield) (%)	4.1
Fair value (£)	16.82/15.22

The expected dividend yield is based on the historical dividend yield for three years prior to grant.

(Expressed in millions of Hong Kong dollars)

40 Material related party transactions (continued)

(c) Share based payments (continued)

A reconciliation of movements for the year ended 31 December 2012 and 2011 is shown below:

	2012	2011
	No. of shares	No. of shares
Outstanding at 1 January	4,393,297	3,479,217
Granted	-	1,811,942
Additional shares for SC PLC rights issue	53,801	_
Lapsed	(219,520)	(202,127)
Exercised	(1,851,537)	(695,735)
Outstanding at 31 December	2,376,041	4,393,297
Weighted average remaining contractual life	4.53 years	5.28 years
Exercisable at 31 December	1,120,469	665,964

2007 Supplementary Restricted Share Scheme (2007 SRSS)

No share awards were granted in 2012.

Valuation

The fair value is based on the market value less an adjustment to take into account the expected dividends over the vesting period.

	2011
Grant Date	10 March
Share price at grant date (£)	16.82
Shares granted	10,713
Vesting period (years)	2/3
Expected dividends (yield) (%)	4.1
Fair value (£)	15.22

The expected dividend yield is based on the historical dividend yield for three years prior to grant.

A reconciliation of movements for the year to 31 December 2012 and 2011 is shown below:

	2012	2011	
	No. of shares	No. of shares	
Outstanding at 1 January	1,525,196	2,516,214	
Granted	_	10,713	
Lapsed	(245,516)	(20,827)	
Exercised	(832,977)	(980,904)	
Outstanding at 31 December	446,703	1,525,196	
Weighted average remaining contractual life	4.18 years	4.76 years	
Exercisable at 31 December	292,095	602,907	

(Expressed in millions of Hong Kong dollars)

40 Material related party transactions (continued)

(c) Share based payments (continued)

2000 Executive Share Option Scheme (2000 ESOS)

No share awards were granted in 2012 and 2011.

A reconciliation of option movements for the year ended 31 December 2012 and 2011 is shown below:

		2012 2011		11	
	No	. of shares	Weighted average exercise price	No. of shares	Weighted average exercise price
Outstanding at 1 January		541,426	£6.74	728,821	£6.59
Lapsed	((225,621)	£6.58	_	_
Exercised	((243,071)	£6.62	(187,395)	£6.16
Outstanding at 31 December		72,734	£7.67	541,426	£6.74
Exercisable at 31 December		72,734	£7.67	541,426	£6.74
20	012			2011	
Weighted average exercise	No. of	Weighted average remaining contractua	e Weighted g average	•	Weighted average remaining contractual

Range of exercise price price shares life price shares life £5.82/£8.76 (2011: £5.82/£7.89) £7.67 72,734 1.07 years £6.74 541,426 1.07 years

2001 Performance Share Plan (PSP)

No share awards were granted in 2012 and 2011.

A reconciliation of movements for the year ended 31 December 2012 and 2011 is shown below:

	2012	2011
	No. of shares	No. of shares
Outstanding at 1 January	648,053	889,647
Lapsed	(180,974)	(87,807)
Exercised	(258,389)	(153,787)
Outstanding at 31 December	208,690	648,053
Weighted average remaining contractual life	6.44 years	7.05 years
Exercisable at 31 December	88,364	113,877

(Expressed in millions of Hong Kong dollars)

40 Material related party transactions (continued)

(c) Share based payments (continued)

2004 Deferred Bonus Plan

No share awards were granted in 2012 and 2011.

Under this plan, shares are issued directly to participants upon vesting.

A reconciliation of share movements for the year ended 31 December 2012 and 2011 is shown below:

	2012	No. of shares
	No. of shares	
Outstanding at 1 January	_	12,649
Shares exercised	_	(12,649)
Outstanding at 31 December	_	_

Notes:

Sharesave

Valuation

Options are valued using a binomial option-pricing model. The fair value per option granted and the assumptions used in the calculation are as follows:

	2012	2011
Grant Date	11 October	11 October
Share price at grant date (£)	13.95	14.11
Exercise price (£)	11.40	10.65
Shares granted	820,453	493,772
Vesting period (years)	3	3/5
Expected volatility (%)	29.8	45.8-53.8
Expected option life (years)	3.33	3.33-5.33
Risk free rate (%)	0.4	0.9-1.4
Expected dividends (yield) (%)	3.1	3.5-3.9
Fair value (£)	3.28	5.39-5.46

The expected volatility is based on historical volatility over the last three to five years or three to five years prior to grant. The expected life is the average expected period to exercise. The risk free rate of return is the yield on zero-coupon UK Government bonds of a term consistent with the assumed option life. The expected dividend yield is based on historical dividend yield for three years prior to grant. Where two amounts are shown for volatility, risk free rates, expected dividend yield and fair values, the first relates to a three years vesting period and the second to a five years vesting period.

a) The shares vest one year after the date of award.

b) A notional scrip dividend accrues on the shares held in the Trust. The dividend is normally delivered in the form of shares and is released on vesting.

(Expressed in millions of Hong Kong dollars)

40 Material related party transactions (continued)

(c) Share based payments (continued)

A reconciliation of option movements for the year ended 31 December 2012 and 2011 is shown below:

	2012		20	11
		Weighted average		Weighted average
	No. of shares	exercise price	No. of shares	exercise price
Outstanding at 1 January	1,703,989	£11.48	1,626,299	£11.50
Granted	820,453	£11.40	493,772	£10.65
Lapsed	(179,473)	£12.42	(199,673)	£11.29
Exercised	(595,149)	£10.80	(216,409)	£9.92
Outstanding at 31 December	1,749,820	£11.57	1,703,989	£11.48
Exercisable at 31 December	174,964	£10.96	114,945	£9.65

		2012			2011		
Range of exercise price	Weighted average exercise price	No. of shares	Weighted average remaining contractual life	Weighted average exercise price	No. of shares	Weighted average remaining contractual life	
£9.79/£14.63 (2011: £8.32/£14.63)	£11.57	1,749,820	2.57 years	£11.48	1,703,989	2.30 years	

(d) Loans to officers

Loans to officers of the Bank disclosed pursuant to section 161B of the Hong Kong Companies Ordinance are as follows:

	2012 HK\$'M	Restated 2011 HK\$'M
Aggregate amount of relevant loans by the Bank outstanding at 31 December	117	109
Maximum aggregate amount of relevant loans by the Bank outstanding during the year	131	121

(Expressed in millions of Hong Kong dollars)

40 Material related party transactions (continued)

(e) Related party transactions with associates and joint ventures of the Group

During the year, the Bank and its subsidiaries entered into transactions with associates and joint ventures of the Group in the ordinary course of its banking business. The amounts of material transactions during the year are set out below:

		Restated
	2012	2011
	HK\$'M	HK\$'M
Amounts due from associates and joint ventures	<u>474</u>	1,632
Deposits from associates and joint ventures	287	312
Operating income	42	19

41 Ultimate holding company

The Bank's ultimate holding company is Standard Chartered PLC, a company registered in England and Wales. Standard Chartered PLC has listings on the London Stock Exchange and the Stock Exchange of Hong Kong. In addition, Standard Chartered PLC is also listed on the Bombay and National Stock Exchanges of India in a form of Indian Depository Receipts.

42 Significant accounting estimates and judgements

In determining the carrying amounts of certain assets and liabilities, the Bank and its subsidiaries make assumptions about the effects of uncertain future events on those assets and liabilities at the balance sheet date. These estimations and assumptions are based on historical experience and expectation of future events and are reviewed periodically as actual results may differ from these estimates.

Pensions

Actuarial assumptions are made in valuing future defined pension obligations as set out in note 30 and are updated periodically.

Taxes

Determining income tax provisions involves judgement on the future tax treatment of certain transactions. Deferred tax liabilities are recognised on all temporary differences and deferred tax assets are recognised on temporary differences where it is probable that there will be taxable revenue against which these can be offset. Management has made judgements as to the probability of future taxable revenues being generated against which tax losses will be available for offset.

Fair value of financial instruments

Fair value is the amount for which an asset could be exchanged or a liability settled, between knowledgeable willing parties in an arm's length transaction. Notes 2(i) and 38 provide further information on the Bank's fair value accounting policy and process.

Impairment of financial assets

Policies on impairment of financial assets are set out in note 2(k).

(Expressed in millions of Hong Kong dollars)

42 Significant accounting estimates and judgements (continued)

Goodwill impairment

An annual assessment is made, as set out in note 22, as to whether the current carrying value of goodwill is impaired.

43 Possible impact of amendments, new standards and interpretations issued but not yet effective for the annual accounting period ended 31 December 2012

Up to the date of issue of the financial statements, the HKICPA/IASB has issued a number of amendments, new standards and interpretations which are not yet effective for the accounting year ended 31 December 2012 and which have not been adopted in these financial statements.

These include:

- Amendments to HKFRS 7/IFRS 7, Financial instruments: Disclosures Offsetting financial assets and financial liabilities
- Amendments to HKAS 1/IAS 1, Presentation of financial statements Presentation of items of other comprehensive income
- HKFRS 9/IFRS 9, Financial instruments
- HKFRS 10/IFRS 10, Consolidated financial statements
- HKFRS 11/IFRS 11, Joint arrangements
- HKFRS 12/IFRS 12, Disclosure of interests in other entities
- HKFRS 13/IFRS 13, Fair value measurement
- Revised HKAS 19/IAS 19, Employee benefits
- HKAS 27/IAS 27, Separate financial statements (2011)
- HKAS 28/IAS 28, Investments in associates and joint ventures
- HKAS 32/IAS 32, Financial Instruments: Presentation Offsetting financial assets and financial liabilities
- Annual Improvements to HKFRS 2009-2011

The Bank and its subsidiaries are in the process of making an assessment of what the impact of these amendments is expected to be in the period of initial application. So far it has concluded that the adoption of these standards is unlikely to have a significant impact on the Bank and its subsidiaries' results of operations and financial position except for HKFRS 9/IFRS 9 and HKFRS 13/IFRS 13 which may have an impact on the Bank and its subsidiaries' results and financial position arising from changes in the Bank and its subsidiaries' classification and measurement of financial instruments.

44 Comparative figures

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

Unaudited supplementary financial information

Disclosure on Remuneration for CG-5 Guideline on a Sound Remuneration System issued by the HKMA

Pursuant to section 3 of CG-5 on Guideline on a Sound Remuneration System of the Supervisory Policy manual issued by the Hong Kong Monetary Authority and the Pillar 3 disclosure requirements for remuneration by the Basel Committee on Banking Supervision, the following disclosures are made:

- a) Information relating to the governance structure of the remuneration system
- b) Information relating to the design and structure of the remuneration processes
- c) Description of the ways in which current and future risks are taken into account in the remuneration processes
- d) Description of the ways in which the Bank seeks to link performance during a performance measurement period with levels of remuneration
- e) Description of the ways in which the Bank seeks to adjust remuneration to take account of longer-term performance
- f) Description of the different forms of variable remuneration that the Bank utilizes and the rationale for using these different forms
- g) Number of meetings held by the Board Remuneration Committee during the financial year and remuneration paid to the staff

The Bank adopts the remuneration policy and systems of Standard Chartered PLC. Please refer to the Directors' Remuneration Report in the Annual Report of Standard Chartered PLC for details of the Board Remuneration Committee, the major characteristics of the remuneration system, and how risks are taken into account in the remuneration processes.

h) Aggregate quantitative information on remuneration for Senior Management and Key Personnel (note 1) for the year ended 31 December 2012 and 31 December 2011 are as follows:

Analysis of remuneration spilt between fixed and variable compensation

	2012		2011		
	Senior Management	Key Personnel	Senior Management	Key Personnel	
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	
Fixed compensation Variable compensation	18,699	9,911	17,761	8,782	
- Up front cash	15,779	12,072	13,508	4,150	
- Up front shares	1,314	_	_	_	
 Deferred cash 	3,467	568	-	_	
Deferred shares:					
 Restricted shares 	4,391	6,405	9,430	10,074	
 Performance shares 	9,278	951	10,484	884	
Total	52,928	29,907	51,183	23,890	
Number of staff at 31 December	7	4	7	4	

Unaudited supplementary financial information (continued)

Disclosure on Remuneration for CG-5 Guideline on a Sound Remuneration System issued by the HKMA (continued)

Analysis of deferred remuneration (note 2)

	2012		2011		
	Senior Management	Key Personnel	Senior Management	Key Personnel	
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	
At 1 January	35,525	14,443	38,074	5,126	
Awarded during the year	17,136	7,924	19,914	10,958	
Paid out during the year Not vested due to performance	(13,794)	(2,300)	(12,257)	(1,651)	
adjustment	(2,007)	(233)	(2,268)		
At 31 December	36,860	19,834	43,463	14,433	
Vested during the year	14,686	2,797	12,584	1,375	

Analysis of total amount of outstanding deferred remuneration

	2012		2011		
	Senior Management	Key Personnel	Senior Management	Key Personnel	
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	
At 31 December					
- Vested	1,003	497	678	_	
- Not-vested	35,857	19,337	42,785	14,433	
	36,860	19,834	43,463	14,433	
At 31 December					
- Cash	3,467	568	_	_	
- Shares	33,393	19,266	43,463	14,433	
	36,860	19,834	43,463	14,433	
Total amount of outstanding deferred remuneration exposed to ex post explicit and/or implicit					
adjustments (note 3)	36,860	19,834	43,463	14,433	

Unaudited supplementary financial information (continued)

Disclosure on Remuneration for CG-5 Guideline on a Sound Remuneration System issued by the HKMA (continued)

Analysis of adjustments of deferred remuneration

	2012		2011	
	Senior Management HK\$'000	Key Personnel HK\$'000	Senior Management HK\$'000	Key Personnel HK\$'000
Total amount of adjustments during the financial year due to				
 ex post explicit adjustments 	(2,007)	(233)	(2,268)	_
 ex post implicit adjustments 	3,463	1,996	(10,062)	(3,132)

Analysis of sign-on payments and severance payments awarded during the year

	2012		2011	
	Senior Management HK\$'000	Key Personnel HK\$'000	Senior Management HK\$'000	Key Personnel HK\$'000
Sign-on payments (including guaranteed performance awards)	_	_	_	11,673
Severance payments				

Note 1: As defined in the CG5 on Guideline on a Sound Remuneration System issued by the HKMA, senior management are those who are responsible for oversight of either the Bank's companywide strategy or activities or those of the Bank's material business lines. Key Personnel are individual employees whose duties or activities in the course of their employment involve the assumption of material risk or the taking on of material exposures on behalf of the Bank.

Note 2: The population of Senior Management and Key Personnel in 2012 differs from that of 2011.

Note 3: Ex post adjustments are adjustments made after the awards are granted.