Habib Bank Zurich (Hong Kong) Limited

Annual Report 2015

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Corporate information

Board of Directors

Mohamedali R. Habib	Chairman
Hilmar R. Hoch	Director
Clive Shaun O'Neill Wallis	Director
Paul Jeremy Brough	Independent Non-Executive Director
Eddie Wang	Independent Non-Executive Director
Ikram Quraishi	Executive Director

Management

Ikram Quraishi	Chief Executive
Jagrup Singh Dhillon	SEVP
Masud Abid	EVP
Alan Yeung	EVP
Meheryar Mavalvala	CFO

Auditors

KPMG, *Certified Public Accountants*

Parent company

Habib Bank AG Zurich, *Incorporated in Switzerland*

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 2015.

Principal place of business and principal activities

Habib Bank Zurich (Hong Kong) Limited ("the Bank") is incorporated and domiciled in Hong Kong and has its registered office and principal place of business at 17/F, Wing On House, 71 Des Voeux Road, Central, Hong Kong.

The principal activities of the Bank are the taking of deposits and financing of import/export and local trade.

At the start of the reporting period, the Bank operated as a deposit taking company under the Hong Kong Banking Ordinance. Subsequently, on 27 February 2015, the Hong Kong Monetary Authority approved the upgrading of the Bank to a Restricted Licence Bank.

Change of name

Pursuant to the Bank's new status as a Restricted Licence Bank, the Bank changed its name on 11 March 2015 from HBZ Finance Limited to Habib Bank Zurich (Hong Kong) Limited.

Operating results

The Hong Kong economy grew moderately in 2015 with GDP growing by 2.4%, down from 2.6% in 2014. This was mainly due to the global economy which grew at its slowest pace since 2009, impacting Hong Kong exports. The slowdown in inbound tourism also added pressure. Domestic demand remained the key force supporting economic growth. Exports of goods witnessed their first annual decline since 2009, contracting by 1.7% in comparison with growth of 0.8% in 2014. The labour market remained largely stable. Underlying inflation witnessed continuing easing for the fourth year in a row averaging 2.5% down from 3.5% in 2014.

As at 31 December 2015, the Bank's capital adequacy ratio stood at 36% while maintaining a capital base above HK$500 million. The Bank's customer deposit base, including imprest accounts and margin deposits on letters of credit and trade bills stood at HK$1.63 billion (2014: HK$1.72 billion). Based on the balance sheet strength, the Bank prudently managed its lending portfolio. As at the year end, total advances to customers including trade bills were HK$1.12 billion (2014: HK$1.40 billion).

Report of the directors (continued)

Operating results (continued)

Liquidity was managed on a prudent basis. A portion of surplus liquidity was invested in short and medium term debt securities. During the year, average liquidity was maintained at 144% (2014: 114%).

During the year, export bills totalling HK$6.07 billion (2014: HK$7.81 billion) and import bills of HK$2.22 billion (2014: HK$2.74 billion) were processed. Import letters of credit for HK$1.76 billion (2014: HK$2.32 billion) were opened. Profit after tax was HK$16.02 million (2014: HK$37.20 million).

In 2016, Hong Kong's economy is expected to expand at a slower pace than that experienced in 2015, mainly due to concerns over expected slower growth of the Mainland China economy, interest rate normalisation in the U.S., increase in global financial markets volatility and an uncertain external economic environment. Business activities will be undertaken in line with the Bank's risk appetite and strategy, while keeping abreast of developments on the economic front in 2016.

Risk management

The Bank has established policies and procedures to identify and analyse key risks facing the Bank, to set appropriate risk limits and to devise controls, and to monitor such risks and limits continually by means of reliable and up-to-date management and information systems. The Bank continually modifies and enhances its risk management policies and systems to reflect changes in markets, products and best practice risk management processes.

(i) Board level committees

The Board of Directors has established two board level committees, namely the Board Risk and Compliance Committee and the Board Audit Committee.

The Board Risk and Compliance Committee is responsible for, among other things, the Bank's risk profile, risk appetite and tolerance, effectiveness of the risk management framework and systems of internal control and compliance. The Committee comprises two non-executive directors and one executive director.

The main purpose of the Board Audit Committee is to represent and assist the Board of Directors in providing independent review and monitoring of financial reporting process, internal control system, the internal and external audit process and compliance with regulatory requirements. The Committee comprises of one independent non-executive director and two non-executive directors.

Report of the directors (continued)

Risk management (continued)

(ii) Specialized management committees

The Board of Directors has also established several specialised management committees, namely the Risk and Compliance Management Committee, Credit Committee, Asset and Liability Committee and IT Steering Committee.

The Risk and Compliance Management Committee is entrusted with the task of putting in place systems and procedures that address the prevention of risks emerging or likely to emerge. The Committee identifies all quantifiable and material risk factors and evaluates the adequacy of organisational policies and procedures to manage the risks effectively. The Committee is also responsible for monitoring and reviewing regulatory compliance within the institution. The Committee comprises the Chief Executive, Alternate Chief Executives, Chief Risk Officer, Chief Financial Officer, Chief Compliance Officer and Executive.

The Credit Committee is responsible for building and maintaining an infrastructure that promotes growth of a quality loan portfolio and minimises losses within the constraints of established policies and relevant regulations. The Committee approves credit limits up to a defined threshold. It also determines and maintains adequate loan loss allowances. The Committee comprises the Chief Executive, Alternate Chief Executives, Chief Risk Officer, Credit Risk Manager and Executive.

The Asset and Liability Committee's principal responsibility is to maintain an effective risk control framework relating to balance sheet structure, liquidity and capital management and market risks while achieving an optimal return. The Committee recommends policy directives to the Board of Directors and provides analytical services relating to funding and investment strategies. The Committee comprises the Chief Executive, Alternate Chief Executives, Chief Risk Officer, Chief Financial Officer and Executive.

The IT Steering Committee is responsible for authorisation of system changes, review of computer hardware/software security and performance, overview of data integrity of transactions and information. The committee comprises the Chief Executive, Alternate Chief Executives, Head of IT, Chief Risk Officer, Chief Financial Officer and Chief Compliance Officer.

(a) Credit risk management

Credit risk arises from the possibility that the counterparty in a transaction may default. It arises from lending, trade finance, derivatives and other activities.

The Bank has policies and procedures in place to ensure that credit risk is properly addressed and managed at the transaction and portfolio levels. The Board of Directors formulates and updates the credit policies. The Bank's credit policies define credit extension criteria, credit sanctions, review and monitoring mechanisms, and the loan classification and provisioning policy.

Report of the directors (continued)

Risk management (continued)

(a) Credit risk management (continued)

To avoid large financial risk, the exposure to a single borrower or group of related borrowers is limited to a percentage of the capital base. Country risk concentration is managed by setting up country exposure limits and emphasising wide geographical spread of export markets.

The Bank holds collateral against advances to customers in the form of mortgages over property and cash deposits. Collateral held as security for financial assets other than advances to customers is determined by the nature of the instrument.

To mitigate credit risk, the Bank enters into netting arrangements with counterparties. Netting arrangements provide that, if an event of default occurs, all outstanding transactions with the counterparty will be terminated and all amounts outstanding will be settled on a net basis. Except for the event of default, all outstanding transactions with the counterparty are settled on a gross basis and generally do not result in offsetting the assets and liabilities in the balance sheet.

(b) Market risk management

Market risk is the risk that movements in interest rates or foreign exchange rates will result in losses in on and off balance sheet positions.

The Bank's policy is to take no proprietary trading positions. The Bank does not engage in speculative trading activities, and hence it is not exposed to market risk arising from the trading book.

Currency risk management

Currency risk is the risk to earnings or capital emanating from the movement of foreign exchange rates. Foreign exchange exposures originate mainly from the trade finance business. The risk thereof is largely eliminated by consciously devising policies that expressly prohibit speculation in currencies and mandate that trade finance related currency transactions are covered simultaneously and aggregate net open positions are managed within limits. All exposures are monitored by the Chief Financial Officer on a daily basis and reviewed periodically by the Asset and Liability Management Committee.

The Bank does not trade in foreign currencies, nor takes any other exposures on account of its clients. The Bank's foreign currency transactions primarily relate to discounting of foreign currency export and import bills. The exchange positions arising from trade bills as well as customers' foreign currency deposit-related transactions are covered in the local market. From time to time the Bank enters into foreign exchange forward transactions to mitigate currency risk.

Report of the directors (continued)

Risk management (continued)

Currency risk management (continued)

As the majority of the Bank's assets and liabilities are denominated in either Hong Kong dollars ("HK$") or United States dollars ("US$") and the US$ is pegged to the HK$, management does not consider there to be any significant currency risk associated with them.

Interest rate risk management

The Bank's interest rate risk positions arise from trade finance, lending and deposit taking activities. Interest rate risk primarily results from the timing difference in the repricing of interest-bearing assets and liabilities. It also relates to positions from non-interest bearing liabilities including shareholders' funds, as well as from certain fixed rate trade finance transactions and liabilities.

The Bank monitors interest rate movements by applying a weighting to assets and liabilities on the balance sheet. Management monitors the weighted average rates on deposits, lending, placements and investments to identify any mismatched exposures and alters the interest rate strategy accordingly. Interest bearing deposits from customers are for a fixed maturity mostly for a three month period and are generally utilised for a similar period. Surplus liquidity is placed in the interbank market and investments. A greater portion of the loans and trade advances is repriceable on a per-transaction basis. Hence the risk element is contained swiftly and the magnitude of the risk posed by interest rates movement is low.

(c) Liquidity risk management

Liquidity relates to the ability of a Bank to meet its obligations as they fall due. Liquidity and funding risk is the risk that the Bank is unable to meet its payment obligations when due, or that it is unable, on an on-going basis, to borrow funds in the market on an unsecured, or even secured, basis at an acceptable price to fund actual or proposed commitments.

The Bank manages the liquidity structure of its assets, liabilities and commitments so as to ensure that liquidity sources match funding needs and that the statutory liquidity maintenance ratio is complied with.

The finance department reviews the current and prospective funding requirements for all operations through monitoring of the liquidity maintenance ratio and the maturity mismatch profile. Liquidity risk is managed by holding sufficient liquid assets (e.g. cash and short term funds) of appropriate quality to ensure that short term funding requirements are covered within prudent limits. Customer deposits form a significant part of the Bank's overall funding and they have remained relatively diversified and stable. Adequate standby facilities are maintained to provide strategic liquidity to meet unexpected and material cash outflows in the ordinary course of business. The Asset and Liability Management Committee measures the liquidity and adequacy of funds periodically and evaluates the overall risks and mitigation. The Committee also manages the funds and investments within the internal and regulatory framework.

Report of the directors (continued)

Risk management (continued)

(d) Operational risk management

Operational risk is the risk of potential loss arising from inadequate or a failure in internal processes, people and systems or from external events. It arises from matters such as non-adherence to systems and procedures or from frauds resulting in financial or reputational loss.

The Board of Directors and senior management are responsible for approving and reviewing the overall business strategies and the policies for each major area of operations. A Risk and Compliance Management Committee is in place to manage operational risks.

The Bank recognises the importance of managing operational risk in a pro-active manner. Operational risk management tools and mechanisms adopted include operational risk incidents reporting, key risk indicators, operation manuals, accounting controls, business continuity planning, insurance policies etc.

The Bank attaches great importance to conducting its business in a safe and sound manner. Strict control is exercised at every level of operations. Additionally, an internal audit system plays an essential role in ensuring due adherence to policies, various internal and statutory limits, and regulatory requirements thus limiting operational risk.

(e) Capital management

The Bank's primary objectives when managing capital are to safeguard the Bank's 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 commensurate with the level of risk being taken 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.

(f) Compliance

Compliance is an integral part of the Bank's risk management function taking care of risks associated with regulatory non-compliance and financial crime risks. The Bank places high importance on the potential risks arising out of non-compliance including loss of reputation, supervisory actions or other regulatory measures including monetary penalties.

Report of the directors (continued)

Risk management (continued)

(f) Compliance (continued)

The compliance function in the Bank has been given the responsibility of supervising and mitigating compliance risk. Its mandate includes assimilation and dissemination of regulatory requirements relating to the business of the Bank, compliance advisory for implementation of relevant regulations and guidelines to various functions and conducting periodic self-assessments and other regulatory compliance reviews on a risk based approach. It also manages the framework and governance of anti-money laundering and counter-terrorist financing activities to be prevented by the Bank.

The compliance function is tasked to regularly report compliance matters to Senior Management. It also reports significant issues through the Risk and Compliance Committee to the Board of Directors.

Financial statements

The profit of the Bank for the financial year ended 31 December 2015 and the state of the Bank's affairs as at that date are set out in the financial statements on pages 13 to 65.

The directors recommend the payment of a dividend of HK$12.0 million (2014: HK$24.0 million) in respect of the year ended 31 December 2015.

Transfer to reserves

Profit attributable to shareholders, before dividends, of HK$16.0 million (2014: HK$37.2 million) has been transferred to reserves. Other movements in reserves are set out on page 15 and note 24.

Compliance with the Banking (Disclosure) Rules

The financial statements for the financial year ended 31 December 2015 comply fully with the applicable disclosure provisions of the Banking (Disclosure) Rules.

Share capital

Details of the share capital of the Bank are set out in note 23 to the financial statements.

Charitable donations

Donations made by the Bank during the year amounted to HK$155,064 (2014: HK$155,278).

Report of the directors (continued)

Directors

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

Mr Mohamedali R. Habib	
Mr Ikram Quraishi	
Dr Hilmar R. Hoch	
Mr A. R. Wadiwala	(deceased on 27 December 2015)
Mr Paul Jeremy Brough	
Mr Clive Shaun O'Neill Wallis	
Mr Eddie Wang	(appointed on 16 December 2015)

At no time during the financial year was the Bank, its holding company or a fellow subsidiary a party to any 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.

Indemnity of directors

A permitted indemnity provision (as defined in section 469 of the Hong Kong Companies Ordinance) for the benefit of the directors of the Bank is currently in force and was in force throughout this year.

Directors' interests in transactions, arrangements or contracts

No contract of significance to which the Bank, or any of its holding company 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.

Auditors

KPMG retire and, being eligible, offer themselves for reappointment. A resolution for the reappointment of KPMG as auditor of the Bank is to be proposed at the forthcoming annual general meeting.

By order of the Board

Mohamedali R. Habib
Chairman

Hong Kong,
11 April 2016

Independent auditor's report to the members of Habib Bank Zurich (Hong Kong) Limited

(Incorporated in Hong Kong with limited liability)

We have audited the financial statements of Habib Bank Zurich (Hong Kong) Limited ("the Bank") set out on pages 13 to 65, which comprise the statement of financial position as at 31 December 2015, the statement of comprehensive income, statement of changes in equity and 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 financial statements that give a true and fair view in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the Hong Kong Companies Ordinance and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. This report is made solely to you, as a body, in accordance with section 405 of the Hong Kong Companies Ordinance, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

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 financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the 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 financial statements.

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

Independent auditor's report to the members of Habib Bank Zurich (Hong Kong) Limited (continued)

(Incorporated in Hong Kong with limited liability)

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Bank as at 31 December 2015 and of its financial performance and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

KPMG
Certified Public Accountants

8th Floor, Prince's Building
10 Chater Road
Central, Hong Kong
28 April 2016

Statement of comprehensive income for the year ended 31 December 2015

(Expressed in Hong Kong dollars)

	Note	2015	2014
Interest income	2(a)	70,990,245	85,138,975
Interest expense	2(b)	(22,684,338)	(23,761,910)
Net interest income		**48,305,907**	**61,377,065**
Fee and commission income	3	28,107,898	33,050,980
Fee and commission expense		(525,271)	(544,470)
Net fee and commission income		**27,582,627**	**32,506,510**
Other net income	4	21,253,657	26,461,581
Operating income		**97,142,191**	**120,345,156**
Operating expenses	5	(68,802,941)	(65,701,244)
		28,339,250	**54,643,912**
Impairment losses on trade bills and advances to customers	7	(7,603,000)	(8,478,870)
Profit before taxation		**20,736,250**	**46,165,042**
Income tax	8(a)	(4,718,252)	(8,961,480)
Profit for the year		**16,017,998**	**37,203,562**
Other comprehensive income	9		
Item that may be reclassified subsequently to profit or loss:			
Available-for-sale financial assets - net movement in the available-for-sale financial assets revaluation reserve		(881,626)	(68,668)
Total comprehensive income for the year		**15,136,372**	**37,134,894**

The notes on pages 18 to 65 form part of these financial statements.

Balance sheet at 31 December 2015

(Expressed in Hong Kong dollars)

	Note	2015	2014
Assets			
Cash and balances with banks	10	165,228,116	224,733,230
Placements with banks	11	453,850,877	360,323,159
Investments	12	323,157,387	171,015,464
Trade bills	13(a)	580,358,779	702,653,557
Advances to customers	14(a)	535,293,274	696,490,670
Tax paid in advance	20(a)	3,614,799	387,575
Deferred tax assets	20(b)	1,234,151	1,132,151
Fixed assets	15	112,916,625	118,110,230
Other assets	16	91,696,784	101,177,372
Total assets		**2,267,350,792**	**2,376,023,408**
Liabilities			
Deposits and balances from banks	17	4,161,518	6,744,500
Deposits from customers	18	1,434,046,960	1,459,506,207
Other liabilities	19	285,999,278	357,766,037
Total liabilities		**1,724,207,756**	**1,824,016,744**
Equity			
Share capital	23	300,000,000	300,000,000
Reserves		243,143,036	252,006,664
Total equity		**543,143,036**	**552,006,664**
Total equity and liabilities		**2,267,350,792**	**2,376,023,408**

The notes on pages 18 to 65 form part of these financial statements.

Approved and authorised for issue by the Board of Directors on 11 April 2016

Ikram Quraishi
Chief Executive
& Executive Director

Mohamedali R. Habib
Chairman

Statement of changes in equity for the year ended 31 December 2015

(Expressed in Hong Kong dollars)

	Share capital	Property revaluation reserve	Regulatory reserve	Available-for-sale financial assets revaluation reserve	Retained profits	Total
At 1 January 2015	300,000,000	11,243,741	16,000,000	(68,668)	224,831,591	552,006,664
Dividend approved and paid in respect of prior year	-	-	-	-	(24,000,000)	(24,000,000)
Profit for the year	-	-	-	-	16,017,998	16,017,998
Other comprehensive income for the year	-	-	-	(881,626)	-	(881,626)
At 31 December 2015	**300,000,000**	**11,243,741**	**16,000,000**	**(950,294)**	**216,849,589**	**543,143,036**
At 1 January 2014	300,000,000	11,243,741	16,000,000	-	211,628,029	538,871,770
Dividend approved and paid in respect of prior year	-	-	-	-	(24,000,000)	(24,000,000)
Profit for the year	-	-	-	-	37,203,562	37,203,562
Other comprehensive income for the year	-	-	-	(68,668)	-	(68,668)
At 31 December 2014	**300,000,000**	**11,243,741**	**16,000,000**	**(68,668)**	**224,831,591**	**552,006,664**

The notes on pages 18 to 65 form part of these financial statements.

Cash flow statement
for the year ended 31 December 2015

(Expressed in Hong Kong dollars)

	2015	2014
Operating activities		
Profit before taxation	20,736,250	46,165,042
Adjustments for non-cash items:		
Depreciation	5,488,056	4,665,353
Charge for impairment losses	7,728,000	8,478,870
Advances written off net of recoveries	(3,098,001)	(9,803,817)
Loss/(gain) on disposal of fixed assets	2,516	(10,419)
Amortisation of bond premium	3,715,819	2,814,305
Exchange revaluation of bonds	(516,589)	(47,363)
	34,056,051	**52,261,971**
Decrease/(increase) in placements with banks with original maturity beyond 3 months	12,727,382	(20,265,403)
Decrease in trade bills	116,695,799	10,002,175
Decrease in advances to customers	162,199,140	99,572,956
Increase/(decrease) in deposits and placements from banks	435,068	(317,979)
(Decrease)/increase in deposits from customers	(25,459,247)	21,923,499
(Decrease)/increase in other liabilities	(71,766,759)	63,886,981
Decrease/(increase) in other assets	9,480,588	(69,895,748)
Cash generated from operations	**238,368,022**	**157,168,452**
Income tax paid		
– Hong Kong profits tax paid	(7,873,262)	(9,391,801)
Net cash generated from operating activities	**230,494,760**	**147,776,651**
Investing activities		
Payments for purchase of fixed assets	(335,731)	(61,936,903)
Proceeds from sales of fixed assets	6,000	25,000
Payments for purchase of investments	(187,402,494)	(30,962,664)
Proceeds from redemption of investments	31,005,500	-
Net cash used in investing activities	**(156,726,725)**	**(92,874,567)**

Cash flow statement for the year ended 31 December 2015 (continued)

(Expressed in Hong Kong dollars)

	2015	2014
Financing activity		
Dividends paid	(24,000,000)	(24,000,000)
Net cash used in financing activity	**(24,000,000)**	**(24,000,000)**
Net increase in cash and cash equivalents	**49,768,035**	**30,902,084**
Cash and cash equivalents at 1 January	556,321,284	525,419,200
Cash and cash equivalents at 31 December	**606,089,319**	**556,321,284**
Analysis of the balances of cash and cash equivalents		
Cash and balances with banks	165,228,116	224,733,230
Overdraft	(1,967,903)	(4,985,953)
Placements with banks with original maturity of three months or less	442,829,106	336,574,007
	606,089,319	**556,321,284**
Cash flows from operating activities include:		
Interest received	74,786,742	86,988,899
Interest paid	(22,431,500)	(22,689,168)

The notes on pages 18 to 65 form part of these financial statements.

Notes to the financial statements

(Expressed in Hong Kong dollars)

1 Significant accounting policies

Habib Bank Zurich (Hong Kong) Limited (the "Bank") is incorporated and domiciled in Hong Kong and has its registered office and principal place of business at 17/F, Wing On House, 71 Des Voeux Road, Central, Hong Kong.

At the start of the reporting period, the Bank operated as a deposit taking company under the Hong Kong Banking Ordinance. Subsequently, on 27 February 2015, the Hong Kong Monetary Authority approved the upgrading of the Bank to a Restricted Licence Bank.

Pursuant to the Bank's new status as a Restricted Licence Bank, the Bank changed its name on 11 March 2015 from HBZ Finance Limited to Habib Bank Zurich (Hong Kong) Limited.

(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 individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards (HKASs) and Interpretations issued by the Hong Kong Institute of Certified Public Accountants (HKICPA) and accounting principles generally accepted in Hong Kong and the requirements of the Hong Kong Companies Ordinance.

The HKICPA has issued several amendments to HKFRSs that are first effective for the current accounting period of the Bank. Of these, the following developments are relevant to the Bank's financial statements:

- *Annual Improvements to HKFRSs 2010-2012 Cycle*
- *Annual Improvements to HKFRSs 2011-2013 Cycle*

The above developments have had no material impact on the Bank's financial statements as they were consistent with policies already adopted by the Bank.

The Bank has not applied any new standard or interpretation that is not yet effective for the current accounting period.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(b) Basis of preparation of the financial statements

The measurement basis used in the preparation of the financial statements is the historical cost basis modified by the revaluation of a residential apartment and certain financial instruments as explained in the accounting policies set out below.

The preparation of financial statements in conformity with HKFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of HKFRSs that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in note 31.

(c) Revenue recognition

Interest income for all interest-bearing financial instruments is recognised in the statement of comprehensive income on an accruals basis using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating the interest income over the relevant period. The effective interest rate is the rate which exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument (for example, prepayment, call and similar options) but does not consider future credit losses. The calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

For impaired loans, the accrual of interest income based on the original terms of the loan is discontinued, but any increase of the present value of impaired loans due to the passage of time is reported as interest income.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(c) Revenue recognition (continued)

Net income from financial instruments designated at fair value through profit or loss and net trading income comprises all gains and losses from changes in fair value (net of accrued coupon) of such financial assets and financial liabilities, together with interest income and expense and dividend income attributable to those financial instruments.

Fee and commission income is recognised in profit or loss on an accruals basis in accordance with terms of the relevant agreements.

Origination or commitment fees received/paid by the Bank which result in the creation or acquisition of a financial asset are deferred and recognised as an adjustment to the effective interest rate. When a loan commitment is not expected to result in the draw-down of a loan, loan commitment fees are recognised on a straight-line basis over the commitment period.

(d) Intangible assets

Intangible assets comprise a club membership acquired by the Bank which is stated in the balance sheet at cost less impairment losses (see note 1(f)).

Intangible assets are not amortised while their useful lives are assessed to be indefinite. Any conclusion that the useful life of an intangible asset is indefinite is reviewed annually to determine whether events and circumstances continue to support the indefinite useful life assessment for that asset. If they do not, the change in the useful life assessment from indefinite to finite is accounted for prospectively from the date of change and in accordance with the policy for amortisation of intangible assets with finite lives as set out above.

(e) Financial instruments

(i) Initial recognition

The Bank classifies its financial instruments into different categories at inception, depending on the purpose for which the assets were acquired or the liabilities were incurred. The categories used by the Bank are: loans and receivables, held-to-maturity investments, available-for-sale investments, fair value through profit or loss and other financial liabilities.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(e) Financial instruments (continued)

(i) Initial recognition (continued)

Financial instruments are measured initially at fair value, which normally will be equal to the transaction price plus, in case of a financial asset or financial liability not held at fair value through profit or loss, transaction costs that are directly attributable to the acquisition of the financial asset or issue of the financial liability. Transaction costs on financial assets and financial liabilities at fair value through profit or loss are expensed immediately.

The Bank recognises financial assets and financial liabilities on the date it becomes a party to the contractual provisions of the instrument. A regular way purchase or sale of financial assets and financial liabilities at fair value through profit and loss is recognised using trade date accounting.

(ii) Categorisation

Fair value through profit or loss

This category comprises derivatives. Derivatives are held at fair value with changes in fair value recognised through profit or loss.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than (a) those that the Bank intends to sell immediately or in the near term, which will be classified as held for trading; (b) those that the Bank, upon initial recognition, designates as at fair value through profit or loss or as available-for-sale; or (c) those where the Bank may not recover substantially all of its initial investment, other than because of credit deterioration, which will be classified as available for sale. Loans and receivables mainly comprise advances to customers, trade bills and placements with banks and financial institutions.

Loans and receivables are carried at amortised cost using the effective interest method, less impairment losses, if any (see note 1(f)).

Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity for which the Bank has the positive intention and ability to hold to maturity, other than (a) those that the Bank, upon initial recognition, designates as at fair value through profit or loss or as available for sale; and (b) those that meet the definition of loans and receivables.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(e) Financial instruments (continued)

(ii) Categorisation (continued)

Held-to-maturity investments are carried at amortised cost using the effective interest method less impairment losses, if any (see note 1(f)).

Available-for-sale investments

Investments in securities which do not fall into any of the above categories are classified as available-for-sale securities. At the end of each reporting period the fair value is remeasured, with any resultant gain or loss being recognised in other comprehensive income and accumulated separately in equity in the fair value reserve.

Interest income from debt securities calculated using the effective interest method is recognised in profit or loss in accordance with the policy set out in note 1(c).

When the investments are derecognised or impaired (see note 1(f)), the cumulative gain or loss recognised in equity is reclassified to profit or loss.

Other financial liabilities

Financial liabilities are measured at amortised cost using the effective interest method.

(iii) Fair value measurement principles

The fair value of financial instruments is based on their quoted market prices at the balance sheet date without any deduction for estimated future selling costs. Financial assets are priced at current bid prices, while financial liabilities are priced at current asking prices.

If there is no publicly available latest traded price nor a quoted market price on a recognised stock exchange or a price from a broker/dealer for non-exchange-traded financial instruments, or if the market for it is not active, the fair value of the instrument is estimated using valuation techniques that provide a reliable estimate of prices which could be obtained in actual market transactions.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate used is a market rate at the balance sheet date applicable for an instrument with similar terms and conditions. Where other pricing models are used, inputs are based on market data at the balance sheet date.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(e) Financial instruments (continued)

(iv) Derecognition

A financial asset is derecognised when the contractual rights to receive the cash flows from the financial asset expire, or where the financial asset together with substantially all the risks and rewards of ownership have been transferred.

A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or expires.

(v) Offsetting

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

(f) Impairment of assets

The carrying amounts of the Bank's assets are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such evidence exists, the carrying amount is reduced to the estimated recoverable amount by means of a charge to profit or loss.

Impairment losses are written off against the corresponding assets directly, except for impairment losses recognised in respect of loans and receivables and held-to-maturity investments, which are measured at amortised cost, whose recovery is considered doubtful but not remote. In this case, the impairment losses are recorded using an allowance account. When the Bank is satisfied that recovery is remote, the amount considered irrecoverable is written off against loans and receivables or held-to-maturity investments directly and any amounts held in the allowance account relating to that borrower/investment are reversed. Subsequent recoveries of amounts previously charged to the allowance account are reversed against the allowance account. Other changes in the allowance account and subsequent recoveries of amounts previously written off directly are recognised in profit or loss.

(i) Loans and receivables

Impairment losses on loans and receivables are measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate (i.e. the effective interest rate computed on initial recognition of these assets). Receivables with a short duration are not discounted if the effect of discounting is immaterial.

1 Significant accounting policies (continued)

(f) Impairment of assets (continued)

(i) Loans and receivables (continued)

The total allowance for credit losses consists of two components: individual impairment allowances and collective impairment allowances.

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

The individual impairment allowance is based upon management's best estimate of the present value of the cash flows which are expected to be received discounted at the original effective interest rate. In estimating these cash flows, management makes judgements about the borrower's financial situation and the net realisable value of any underlying collateral or guarantees in favour of the Bank. Each impaired asset is assessed on its own merits.

In assessing the need for a collective impairment allowance, management uses statistical modelling and considers historical trends of factors such as credit quality, portfolio size, concentrations, and economic factors. In order to estimate the required allowance, the Bank makes assumptions both to define the way the Bank models inherent losses and to determine the required input parameters, based on historical experience and current economic conditions.

The accuracy of the impairment allowances the Bank makes depends on how well the Bank can estimate future cash flows for individually assessed impairment allowances and the model assumptions and parameters used in determining collective impairment allowances. While this necessarily involves judgement, the Bank believes that the impairment allowances on loans and advances to customers are reasonable and supportable.

Any subsequent changes to the amounts and timing of the expected future cash flows compared to the prior estimates that can be linked objectively to an event occurring after the write-down, will result in a change in the impairment allowances on loans and receivables and be charged or credited to the statement of comprehensive income. A reversal of impairment losses is limited to the loans and receivables' carrying amount that would have been determined had no impairment loss been recognised in prior years.

When there is no reasonable prospect of recovery, the loan and the related interest receivable are written off.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Impairment of assets (continued)

(i) Loans and receivables (continued)

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 has made concessions that it would not otherwise consider. Renegotiated loans and receivables are subject to ongoing monitoring to determine whether they remain impaired or past due.

(ii) Held-to-maturity investments

Impairment on held-to-maturity investments is considered at both an individual and collective level. The individual impairment allowance is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the asset's original effective interest rate, where the effect of discounting is material.

All significant assets found not to be individually impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Assets that are not individually significant are then collectively assessed for impairment by grouping together financial assets with similar risk characteristics.

If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the impairment loss was recognised, the impairment loss is reversed through the income statement. A reversal of impairment losses shall not result in the asset's carrying amount exceeding that which would have been determined had no impairment loss been recognised in prior years.

(iii) Available-for-sale investments

For available-for-sale securities, the cumulative loss that has been recognised in the fair value reserve is reclassified to profit or loss. The amount of the cumulative loss that is recognised in profit or loss is the difference between the acquisition cost (net of any principal repayment and amortisation) and current fair value, less any impairment loss on that asset previously recognised in profit or loss.

Impairment losses in respect of available-for-sale debt securities are reversed if the subsequent increase in fair value can be objectively related to an event occurring after the impairment loss was recognised. Reversals of impairment losses in such circumstances are recognised in profit or loss. Impairment losses recognised in profit or loss for an investment in an equity instrument classified as available-for-sale are not reversed through profit or loss.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Impairment of assets (continued)

(iv) Other assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired:

- Fixed assets (other than properties carried at revalued amounts); and
- Intangible assets.

If any such indication exists, the asset's recoverable amount is estimated. In addition, for intangible assets that have indefinite useful lives, the recoverable amount is estimated annually whether or not there is any indication of impairment.

- Calculation of recoverable amount

  The recoverable amount of an asset is the greater of its fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

- Recognition of impairment losses

  An impairment loss is recognised in profit or loss whenever the carrying amount of an asset, or the cash-generating unit to which it belongs, exceeds its recoverable amount. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating unit (or group of units) and then to reduce the carrying amount of the other assets in the unit (or group of units) on a pro rata basis, except that the carrying value of an asset will not be reduced below its individual fair value less costs to sell, or value in use, if determinable.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Impairment of assets (continued)

(iv) Other assets (continued)

- Reversals of impairment losses

  An impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount.

  A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. Reversals of impairment losses are credited to profit or loss in the year in which the reversals are recognised.

(g) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks and placements with banks with original maturity of three months or less for the purpose of the cash flow statement.

(h) Fixed assets

Fixed assets are held for own use and are stated at cost or valuation less accumulated depreciation and impairment losses (note 1(f)). A property is held at a revalued amount and was last revalued in 1994. In accordance with paragraph 80A of HKAS 16, "Property, plant and equipment", no further revaluation of the property is required.

Depreciation is calculated to write off the cost or valuation of fixed assets over their anticipated useful lives using the straight line method as follows:

– Residential apartment	40 years
– Office buildings	50 years
– Leasehold improvements	5 to 10 years
– Furniture, fixtures and office equipment	4 to 5 years
– Motor vehicles	5 years

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(i) Operating leases

Leases which do not transfer substantially all the risks and rewards of ownership to the lessee are classified as operating leases.

Where the Bank has the use of assets held under operating leases, payments made under the leases are charged to profit or loss in equal instalments over the accounting periods covered by the lease term, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased asset. Lease incentives received are recognised in profit or loss as an integral part of the aggregate net lease payments made. Contingent rentals are charged to profit or loss in the accounting period in which they are incurred.

(j) Repossessed assets

In the recovery of impaired loans and advances, the Bank may take possession of assets held as collateral through court proceedings or voluntary delivery of possession by the borrowers. Where it is intended to achieve an orderly realisation of the impaired assets and the Bank is no longer seeking repayment from the borrower, repossessed assets are reported in "Other assets". The Bank does not hold the repossessed assets for its own use.

Repossessed assets are recorded at the lower of the amount of the related loans and advances and fair value less costs to sell at the date of exchange. They are not depreciated or amortised.

Impairment losses on initial classification and on subsequent remeasurement are recognised in profit or loss.

(k) Income tax

Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Current tax and movements in deferred tax assets and liabilities are recognised in profit or loss except to the extent that they relate to items recognised in other comprehensive income, in which case they are recognised in other comprehensive income.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(k) Income tax (continued)

Deferred tax assets and liabilities arise from deductible and taxable temporary differences respectively, being the differences between the carrying amounts of assets and liabilities for financial reporting purposes and their tax bases. Deferred tax assets also arise from unused tax losses and unused tax credits.

Apart from certain limited exceptions, all deferred tax liabilities, and all deferred tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilised, are recognised. Future taxable profits that may support the recognition of deferred tax assets arising from deductible temporary differences include those that will arise from the reversal of existing taxable temporary differences, provided those differences relate to the same taxation authority and the same taxable entity, and are expected to reverse either in the same period as the expected reversal of the deductible temporary difference or in periods into which a tax loss arising from the deferred tax asset can be carried forward. The same criteria are adopted when determining whether existing taxable temporary differences support the recognition of deferred tax assets arising from unused tax losses and credits, that is, those differences are taken into account if they relate to the same taxation authority and the same taxable entity, and are expected to reverse in a period, or periods, in which the tax loss or credit can be utilised.

The amount of deferred tax recognised is measured based on the expected manner of realisation or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are not discounted.

The carrying amount of a deferred tax asset is reviewed at each balance sheet date and is reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow the related tax benefit to be utilised. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profit will be available.

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 has the 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 intends 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 the same taxable entity.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(l) Provisions and contingent liabilities

Provisions are recognised for liabilities of uncertain timing or amount when the Bank has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditures expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

(m) Translation of foreign currencies

Foreign currency transactions during the year are translated into Hong Kong dollars at the foreign exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated into Hong Kong dollars at the foreign exchange rates ruling at the balance sheet date. Exchange gains and losses are recognised in profit or loss.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated into Hong Kong dollars using the foreign exchange rates ruling at the transaction dates. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated using the foreign exchange rates ruling at the dates the fair value was measured.

(n) Related parties

(1) A person, or a close member of that person's family, is related to the Bank if that person:

(i) has control or joint control over the Bank;

(ii) has significant influence over the Bank; or

(iii) is a member of the key management personnel of the Bank or the Bank's parent.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(n) Related parties (continued)

(2) An entity is related to the Bank if any of the following conditions applies:

(i) The entity and the Bank are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).

(ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a company of which the other entity is a member).

(iii) Both entities are joint ventures of the same third party.

(iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.

(v) The entity is a post-employment benefit plan for the benefit of employees of either the Bank or an entity related to the Bank.

(vi) The entity is controlled or jointly-controlled by a person identified in (1).

(vii) A person identified in (1)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

(viii) The entity, or any member of a group of which it is a part, provides key management personnel services to the Bank or to the Bank's parent.

Close members of the family of a person are those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity.

(o) Employee benefits

(i) Salaries, annual bonuses, paid annual leave, leave passage and the cost to the Bank of non-monetary benefits are accrued in the year in which the associated services are rendered by employees of the Bank. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.

(ii) The Bank operates a defined contribution scheme. Contributions to a provident fund under the Occupational Retirement Scheme Ordinance are recognised as an expense in profit or loss as incurred.

(iii) Termination benefits are recognised when, and only when, the Bank demonstrably commits itself to terminate employment or to provide benefits as a result of voluntary redundancy by having a detailed formal plan which is without realistic possibility of withdrawal.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

2 Interest income and interest expense

	2015	2014
(a) Interest income arising from		
Trade bills and advances to customers	62,004,441	78,026,815
Placements with banks	2,660,632	2,550,253
Investments	6,325,172	4,561,907
	70,990,245	**85,138,975**
(b) Interest expense arising from		
Deposits from customers	22,449,900	23,314,952
Deposits and balances from banks	234,438	446,958
	22,684,338	**23,761,910**

3 Fee and commission income

	2015	2014
Fee and commission income	28,107,898	33,050,980

Fee and commission income in 2015 and 2014 mainly comprised fee and commission income from L/C bills and export bills.

4 Other net income

	2015	2014
Net gains from dealing in foreign currencies	11,044,024	14,808,555
Others	10,209,633	11,653,026
	21,253,657	**26,461,581**

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

5 Operating expenses

	2015	2014
(a) Staff costs		
Salaries and other benefits	46,113,251	42,178,284
Contribution to defined contribution scheme	2,894,521	2,612,076
	49,007,772	**44,790,360**
(b) Depreciation	**5,488,056**	**4,665,353**
(c) Other operating expenses		
Premises and equipment expenses, excluding depreciation		
– rent and rates	1,294,536	2,631,542
– repairs and maintenance	407,855	529,751
Auditor's remuneration		
– audit services	718,300	724,950
– tax services	55,000	50,300
– other services	1,094,170	329,950
Others	10,737,252	11,979,038
	14,307,113	**16,245,531**
	68,802,941	**65,701,244**

6 Directors' emoluments

Directors' emoluments disclosed pursuant to section 383(1) of the Hong Kong Companies Ordinance and Part 2 of the Companies (Disclosure of Information about Benefits of Directors) Regulation are as follows:

	2015	2014
Directors' fees	311,907	385,554
Salaries, allowances and benefits in kind	2,585,232	2,527,428
Discretionary bonuses	262,958	254,066
Retirement scheme contributions	157,775	152,440
	3,317,872	**3,319,488**

Note: The benefits in kind are in the form of provision of the Bank's residential apartment to a director.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

7 Impairment charges on trade bills and advances to customers

	2015	2014
Impairment losses charged on trade bills and advances to customers (note 14(c))	7,728,000	8,478,870
Loan loss recovery	(125,000)	-
	7,603,000	**8,478,870**

8 Income tax in the statement of comprehensive income

(a) Taxation in the statement of comprehensive income represents:

	2015	2014
Current tax - provision for Hong Kong profits tax		
Tax for the year	4,656,368	8,261,497
(Over)/under-provision in respect of prior years	(10,330)	763,555
	4,646,038	**9,025,052**
Deferred tax		
Origination and reversal of temporary differences	72,214	(63,572)
	4,718,252	**8,961,480**

The provision for Hong Kong Profits Tax for 2015 is calculated at 16.5% (2014: 16.5%) of the estimated assessable profits for the year.

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

	2015	2014
Profit before tax	**20,736,250**	**46,165,042**
Notional tax on profit before taxation, calculated at 16.5%	3,421,481	7,617,232
Tax effect of non-deductible expenses	1,307,101	580,693
(Over)/under-provision in respect of prior years	(10,330)	763,555
Actual tax expense	**4,718,252**	**8,961,480**

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

9 Other comprehensive income

Tax effects relating to each component of other comprehensive income:

	2015			2014		
	Before-tax amount	Tax (charge)/ credit (note 20(b))	Net-of-tax amount	Before-tax amount	Tax (charge)/ credit (note 20(b))	Net-of-tax amount
Available-for-sale financial assets: net movement in available-for-sale financial assets revaluation reserve	(1,055,840)	174,214	(881,626)	(82,237)	13,569	(68,668)

10 Cash and balances with banks

	2015	2014
Cash in hand	135,266	108,328
Balances with banks	165,092,850	224,624,902
	165,228,116	**224,733,230**

11 Placements with banks

	2015	2014
Placements with banks	**453,850,877**	**360,323,159**
Remaining maturity		
– within one month	202,110,308	181,472,033
– between one month and three months	247,829,107	178,851,126
– between three months and one year	3,911,462	-
	453,850,877	**360,323,159**

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

12 Investments

	2015	2014
Held-to-maturity debt securities		
– Listed outside Hong Kong	133,868,213	106,729,692
– Listed in Hong Kong	85,000,406	31,455,999
– Unlisted	23,780,270	9,725,255
	242,648,889	**147,910,946**
Available-for-sale debt securities - at fair value		
– Listed outside Hong Kong	29,087,765	11,403,534
– Listed in Hong Kong	43,440,223	11,700,984
– Unlisted	7,980,510	-
Market value of listed debt securities	**80,508,498**	**23,104,518**
	323,157,387	**171,015,464**

13 Trade bills

(a) Trade bills less impairment:

	2015	2014
Gross trade bills	594,229,987	710,925,786
Less: Impairment allowances		
– individually assessed (note 14(c))	(7,875,000)	(795,000)
– collectively assessed (note 14(c))	(5,996,208)	(7,477,229)
	580,358,779	**702,653,557**

(b) Impaired trade bills:

	2015	2014
Gross impaired trade bills	38,110,938	7,318,467
Impairment allowance - individually assessed	(7,875,000)	(795,000)
	30,235,938	**6,523,467**

Impaired trade bills are individually assessed trade bills with objective evidence of impairment.

Individually assessed impairment allowances are made after taking into account the value of collateral in respect of such trade bills. For individually assessed impaired trade bills, the value of collateral is $24,524,602 (2014: $1,496,461).

The percentage of impaired trade bills to gross trade bills is 6.41% (2014: 1.03%).

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

14 Advances to customers

(a) Advances to customers less impairment:

	2015	2014
Gross advances to customers	550,739,274	712,905,650
Less: Impairment allowances		
– individually assessed (note 14(c))	(9,885,000)	(9,030,000)
– collectively assessed (note 14(c))	(5,561,000)	(7,384,980)
	535,293,274	**696,490,670**

(b) Impaired advances to customers:

	2015	2014
Gross impaired advances to customers	36,623,493	17,979,236
Impairment allowance - individually assessed	(9,885,000)	(9,030,000)
	26,738,493	**8,949,236**

Impaired advances are individually assessed advances with objective evidence of impairment.

Individually assessed impairment allowances are made after taking into account the value of collateral in respect of such advances to customers. For individually assessed impaired advances to customers, the value of collateral is $20,144,369 (2014: $7,277,356).

The percentage of impaired advances to gross advances to customers is 6.65% (2014: 2.52%).

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

14 Advances to customers (continued)

(c) Movement in impairment allowance on trade bills and advances to customers

	2015			2014		
	Individually assessed	Collectively assessed	Total	Individually assessed	Collectively assessed	Total
At 1 January	9,825,000	14,862,209	24,687,209	10,755,000	15,257,156	26,012,156
Impairment losses charged/(released) to statement of comprehensive income (note 7)	11,033,001	(3,305,001)	7,728,000	8,873,817	(394,947)	8,478,870
Amounts written off	(3,098,001)	-	(3,098,001)	(9,803,817)	-	(9,803,817)
At 31 December	**17,760,000**	**11,557,208**	**29,317,208**	**9,825,000**	**14,862,209**	**24,687,209**
Deducted from:						
Trade bills (note 13(a))	7,875,000	5,996,208	13,871,208	795,000	7,477,229	8,272,229
Advances to customers (note 14(a))	9,885,000	5,561,000	15,446,000	9,030,000	7,384,980	16,414,980
	17,760,000	**11,557,208**	**29,317,208**	**9,825,000**	**14,862,209**	**24,687,209**

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

15 Fixed assets

	2015			
	Leasehold improvements	Buildings	Furniture, fixtures, office equipment and motor vehicles	Total
Cost or valuation:				
At 1 January 2015	10,255,655	129,209,411	14,242,191	153,707,257
Additions	83,010	-	252,721	335,731
Disposals/written off	(1,685,877)	-	(659,200)	(2,345,077)
At 31 December 2015	8,652,788	129,209,411	13,835,712	151,697,911
Representing:				
Cost	8,652,788	114,709,411	13,835,712	137,197,911
Valuation	-	14,500,000	-	14,500,000
	8,652,788	**129,209,411**	**13,835,712**	**151,697,911**
Aggregate depreciation:				
At 1 January 2015	5,890,337	17,411,958	12,294,732	35,597,027
Charge for the year	1,736,291	2,782,143	969,622	5,488,056
Written back on disposals	(1,685,877)	-	(617,920)	(2,303,797)
At 31 December 2015	**5,940,751**	**20,194,101**	**12,646,434**	**38,781,286**
Net book value:				
At 31 December 2015	**2,712,037**	**109,015,310**	**1,189,278**	**112,916,625**

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

15 Fixed assets (continued)

	2014			
	Leasehold improvements	Buildings	Furniture, fixtures, office equipment and motor vehicles	Total
Cost or valuation:				
At 1 January 2014	7,392,449	71,183,079	14,155,907	92,731,435
Additions	3,011,806	58,026,332	898,765	61,936,903
Disposals/written off	(148,600)	-	(812,481)	(961,081)
At 31 December 2014	10,255,655	129,209,411	14,242,191	153,707,257
Representing:				
Cost	10,255,655	114,709,411	14,242,191	139,207,257
Valuation	-	14,500,000	-	14,500,000
	10,255,655	**129,209,411**	**14,242,191**	**153,707,257**
Aggregate depreciation:				
At 1 January 2014	4,570,768	15,211,466	12,095,940	31,878,174
Charge for the year	1,456,257	2,200,492	1,008,604	4,665,353
Written back on disposals	(136,688)	-	(809,812)	(946,500)
At 31 December 2014	**5,890,337**	**17,411,958**	**12,294,732**	**35,597,027**
Net book value:				
At 31 December 2014	**4,365,318**	**111,797,453**	**1,947,459**	**118,110,230**

The buildings are held in Hong Kong under a long term lease.

The Bank's residential apartment was purchased in 1984 for $1,362,270. It was revalued at $14,500,000 in 1994 on an open market value basis by an independent surveyor, Knight Frank Kan & Baillieu.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

16 Other assets

	2015	2014
Customer liabilities under acceptances	82,690,489	92,182,722
Interest receivable	7,973,466	7,435,108
Others	1,032,829	1,559,542
	91,696,784	**101,177,372**

Included in other assets are intangible assets of $225,000 (2014: $225,000) relating to club debentures held by the Bank. There has been no impairment of intangible assets in either the current or preceding year.

17 Deposits and balances from banks

	2015	2014
Deposits and balances from banks	4,161,518	6,744,500

18 Deposits from customers

	2015	2014
Staff provident fund	64,384,285	63,140,449
Time and call deposits	1,369,662,675	1,396,365,758
	1,434,046,960	**1,459,506,207**

19 Other liabilities

	2015	2014
Acceptances outstanding	82,690,489	92,182,722
Interest payable	4,831,209	4,713,783
Imprest accounts	106,299,499	108,580,332
Margin on L/Cs and trade bills	86,506,766	147,577,150
Interest received in advance	135,412	65,955
Others	5,535,903	4,646,095
	285,999,278	**357,766,037**

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

20 Income tax in the balance sheet

(a) Current taxation in the balance sheet represents:

	2015	2014
Provision for Hong Kong profits tax for the year	4,656,368	8,261,497
Provisional profits tax paid	(8,271,167)	(8,649,072)
	(3,614,799)	**(387,575)**

(b) Deferred tax assets and liabilities recognised

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

	Difference between depreciation allowances and related depreciation	Revaluation of properties	Collective impairment allowance for bad and doubtful debts	Fair value adjustment for available-for-sale financial assets	Total
Deferred tax arising from:					
At 1 January 2015	(521,535)	1,855,217	(2,452,264)	(13,569)	(1,132,151)
(Credited)/charged to statement of comprehensive income	(473,111)	-	545,325	-	72,214
Credited to available-for-sale financial assets revaluation reserve (note 9)	-	-	-	(174,214)	(174,214)
At 31 December 2015	**(994,646)**	**1,855,217**	**(1,906,939)**	**(187,783)**	**(1,234,151)**
At 1 January 2014	(392,796)	1,855,217	(2,517,431)	-	(1,055,010)
(Credited)/charged to statement of comprehensive income	(128,739)	-	65,167	-	(63,572)
Credited to available-for-sale financial assets revaluation reserve (note 9)	-	-	-	(13,569)	(13,569)
At 31 December 2014	**(521,535)**	**1,855,217**	**(2,452,264)**	**(13,569)**	**(1,132,151)**

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

21 Material related party transactions

(a) During the year, the Bank entered into transactions with related parties in the ordinary course of business including the taking and placing of inter-bank deposits. These transactions were priced at relevant market rates at the time of each transaction.

The amounts included in the financial statements arising from transactions with related parties are as follows:

	Parent company		Fellow subsidiaries		Affiliates		Key management personnel	
	2015	**2014**	**2015**	**2014**	**2015**	**2014**	**2015**	**2014**
Commission rebate	-	-	-	-	1,356,394	1,511,232	-	-
Interest expenses	227,120	388,837	-	-	2,082	-	-	-
IT maintenance	700,000	700,000	-	-	-	-	-	-
Other services	600,000	426,428	-	-	-	-	-	-
Head office expenses	1,099,532	1,100,000	-	-	-	-	-	-
Staff Provident Fund expense	-	-	-	-	2,894,521	2,612,076	-	-
Cash and balances with banks	3,972,722	3,243,899	471,600	615,006	22,945,724	-	-	-
Deposits and balances from banks	2,094,941	1,430,983	36,012	268,656	1,974,210	4,992,047	-	-
Time deposits	-	-	-	-	-	-	10,581,921	8,151,903
Imprest accounts	-	-	-	-	-	-	548,046	193,807
Staff Provident Fund deposit	-	-	-	-	64,384,285	63,140,449	-	-

The aggregate unsecured facilities granted to connected parties who are (i) individuals did not exceed $1,000,000 per person or 5% of the capital base and (ii) firms, partnerships or non-listed companies (as specified in section 83(4) of the Banking Ordinance) did not exceed 10% of the capital base. The maximum aggregate unsecured facilities to all connected parties did not exceed 10% of the capital base. The secured lending to connected parties follows the supervisory policy manual on connected lending (CR-G-9) clause 2.5 issued by the HKMA.

The Bank has entered into an agreement with its parent company for the provision of banking software and related IT services.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

21 Material related party transactions (continued)

(b) Key management personnel remuneration

	2015	2014
Short-term employee benefits	10,523,460	9,168,803
Post-employment benefits	574,406	440,457
	11,097,866	**9,609,260**

Total remuneration is included in staff costs (see note 5(a)).

22 Loans to directors and bodies corporate controlled by them

Loans to directors of the Bank, including loans to bodies controlled by them, disclosed pursuant to section 383(1)(d) of the Hong Kong Companies Ordinance and Part 3 of the Companies (Disclosure of Information about Benefits of Directors) Regulation are as follows:

	2015	2014
Loans made by a third party under a guarantee given by the Bank	-	-
Loans made by the Bank	-	-
	-	-

23 Share capital

	2015		2014	
	No. of shares (000)		No. of shares (000)	
Ordinary shares issued and fully paid:				
At 1 January and 31 December	3,000	300,000,000	3,000	300,000,000

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Bank. All ordinary shares rank equally with regard to the Bank's residual assets.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

24 Reserves and dividends

(a) Nature and purpose of reserves

(i) Available-for-sale financial assets revaluation reserve

The available-for-sale financial assets revaluation reserve comprises the cumulative net change in the fair value of available-for-sale financial assets until the financial assets are derecognised and is dealt with in accordance with the accounting policies in notes 1(e) and 1(f).

(ii) Property revaluation reserve

The revaluation reserve has been set up in accordance with the accounting policies adopted for land and buildings in note 1(h). The revaluation reserve is not available for distribution to shareholders.

(iii) Regulatory reserve

The regulatory reserve is an appropriation from retained earnings and is maintained for the purpose of paragraph 9 of the Seventh Schedule to the Hong Kong Banking Ordinance to set aside amounts in respect of losses which the Bank will or may incur on loans and advances in addition to impairment losses recognised under HKAS 39, "Financial instruments: Recognition and measurement". Transfer to and from the regulatory reserve are made directly through retained earnings and not the statement of comprehensive income.

(b) Distributability of reserves

At 31 December 2015, the aggregate amount of reserves available for distribution to equity shareholders of the Bank was $216,849,589 (2014: $224,831,591).

(c) Dividends

	2015	2014
Final dividend in respect of the current financial year proposed after the balance sheet date of $4.00 per ordinary share (2014: $8.00 per ordinary share)	12,000,000	24,000,000

The dividend proposed after the balance sheet date has not been recognised as a liability at the balance sheet date.

	2015	2014
Final dividend in respect of the previous financial year, approved and paid during the year, of $8.00 per ordinary share (2014: $8.00 per ordinary share)	24,000,000	24,000,000

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

25 Derivatives

(a) Notional amount of derivatives

Derivatives refer to financial contracts whose value depends on the value of one or more underlying assets or indices. The notional amounts of these instruments indicate the volume of outstanding transactions and do not represent amounts at risk.

	Non-trading book	
	2015	**2014**
Currency derivatives		
Forwards	-	**67,099,831**

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

The derivative financial instruments have a positive fair value of $nil (2014: $38,817) and negative fair value of $nil (2014: $35,292) and are expected to mature within one year from the balance sheet date. The fair value of financial instruments has been calculated using a Level 2 valuation methodology utilising market observable inputs.

26 Assets pledged as security

The following assets have been pledged as collateral:

	2015	**2014**
Balances with banks	2,497,749	3,059,934
Investments	59,845,430	88,366,212
	62,343,179	**91,426,146**

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

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

27 Contingent assets, liabilities and commitments

(a) Contingent assets, liabilities and commitments to extend credit

The following is a summary of the contractual amounts of each significant class of contingent liabilities and commitments:

	2015	2014
Trade-related contingencies	319,161,184	414,780,378
Credit risk weighted amounts	42,179,271	54,562,710

Contingent liabilities and commitments are credit-related instruments which include letters of credit, confirmation of letters of credit, guarantees and commitments to extend credit. The risk involved in these credit-related instruments is essentially the same as the credit risk involved in extending loan facilities to customers. The contractual amounts represent the amounts at risk should the contract be fully drawn upon and the client default. As the facilities may expire without being drawn upon, the contractual amounts do not represent expected future cash flows. The risk weights used in the computation of credit risk weighted amounts range from 0% to 100%.

(b) Lease commitments

At 31 December 2015, the total future minimum lease payments in respect of IT services and properties under non-cancellable operating leases are payable as follows:

	2015	2014
Within 1 year	198,034	192,534
After 1 year but within 5 years	-	-
	198,034	192,534

28 Ultimate and immediate holding company

As at 31 December 2015, the directors consider the Bank's immediate parent to be Habib Bank AG Zurich and ultimate holding company to be Gefan Finanz AG. Both the parent and ultimate holding company are incorporated in Switzerland.

29 Financial risk management

This section presents information about the Bank's exposure to and its management and control of risks, in particular, the primary risks associated with its use of financial instruments:

- credit risk: loss resulting from customer or counterparty default and arises on credit exposure in all forms, including settlement risk.
- market risk: exposure to market variables such as interest rates and exchange rates.
- liquidity and funding risk: the risk that the Bank is unable to meet its payment obligations when due, or that it is unable, on an ongoing basis, to borrow funds in the market on an unsecured, or even secured, basis at an acceptable price to fund actual or proposed commitments.
- operational risk: risk arising from matters such as non-adherence to systems and procedures or from frauds resulting in financial or reputational loss.

The Bank has established policies and procedures to identify and analyse these risks, to set appropriate risk limits and to devise controls, and to monitor such risks and limits continually by means of reliable and up-to-date management and information systems. The Bank continually modifies and enhances its risk management policies and systems to reflect changes in markets, products and best practice risk management processes. Introduction of new products and systems are approved by the Board of Directors after proper risk assessment. The internal auditors also perform regular audits to ensure compliance with the policies and procedures.

(a) Credit risk

Credit risk arises from the possibility that the counterparty in a transaction may default. It arises from lending, trade finance, derivatives and other activities.

The Bank has policies and procedures in place to ensure that credit risk is properly addressed and managed at the transaction and portfolio levels. The Board of Directors formulates and updates the credit policies. The Bank's credit policies define credit extension criteria, credit sanctions, review and monitoring mechanisms, and the loan classification and provisioning policy.

To avoid large financial risk, the exposure to a single borrower or group of related borrowers is limited to a percentage of the capital base. Country risk concentration is managed by setting up country exposure limits and emphasising wide geographical spread of export markets.

The Credit Committee, chaired by the Chief Executive, monitors compliance with statutory and internal limits on credit exposures. The internal auditor carries out regular audits to ensure compliance with the stated policies and procedures. To strengthen the independence of the audit function, the internal auditor of the Bank reports directly to the Audit Committee.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 Financial risk management (continued)

(a) Credit risk (continued)

(i) Maximum exposure

The maximum exposure to credit risk at the balance sheet date without taking into consideration of any collateral held or other credit enhancements is represented by the carrying amount of each financial asset in the balance sheet after deducting any impairment allowance. A summary of the maximum exposure is as follows:

	2015	2014
Cash and balances with banks	165,228,116	224,733,230
Placements with banks	453,850,877	360,323,159
Investments	323,157,387	171,015,464
Trade bills	580,358,779	702,653,557
Advances to customers	535,293,274	696,490,670
Other assets	91,696,784	101,177,372
Financial guarantees and other credit related contingent liabilities	319,161,184	414,780,378
	2,468,746,401	**2,671,173,830**

(ii) Credit quality of advances to customers and trade bills

The credit quality of advances to customers and trade bills can be analysed as follows:

	2015		2014	
	Gross amount of advances to customers	Gross amount of trade bills	Gross amount of advances to customers	Gross amount of trade bills
	'000	'000	'000	'000
Neither past due nor impaired	452,290	506,878	603,074	615,016
Past due but not impaired	61,826	49,241	91,852	88,591
Impaired	36,623	38,111	17,979	7,319
	550,739	**594,230**	**712,905**	**710,926**
Of which:				
Neither past due nor impaired				
– Grade 1: Pass	419,120	505,165	584,894	611,243
– Grade 2: Special Mention	33,170	1,713	18,180	3,773
	452,290	**506,878**	**603,074**	**615,016**

The Bank classifies the advances to customers and trade bills in accordance with the loan classification system required to be adopted for reporting to the HKMA.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 Financial risk management (continued)

(a) Credit risk (continued)

(ii) Credit quality of advances to customers and trade bills (continued)

The ageing analysis of advances to customers and trade bills to customers that are past due but not impaired is as follows:

	2015		2014	
	Gross amount of advances to customers	Gross amount of trade bills	Gross amount of advances to customers	Gross amount of trade bills
	'000	'000	'000	'000
Less than 1 month	31,281	34,180	39,395	58,912
3 months or less but over 1 month	13,944	10,995	30,908	21,183
6 months or less but over 3 months	6,066	103	19,769	7,734
1 year or less but over 6 months	10,535	3,963	1,780	762
Over 1 year	-	-	-	-
	61,826	**49,241**	**91,852**	**88,591**

(iii) Collateral and other credit enhancements

The Bank holds collateral against advances to customers in the form of mortgages over property and cash deposits. Collateral held as security for financial assets other than advances to customers is determined by the nature of the instrument.

An estimate of the fair value of collateral and other credit enhancements held against financial assets is as follows:

	2015	2014
	'000	'000
Fair value of collateral and other credit enhancements held against financial assets that are:		
– neither past due nor impaired	558,709	708,206
– past due but not impaired	102,317	145,464
	661,026	**853,670**

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 Financial risk management (continued)

(a) Credit risk (continued)

(iii) Collateral and other credit enhancements (continued)

To mitigate credit risk, the Bank enters into netting arrangements with counterparties. Netting arrangements provide that, if an event of default occurs, all outstanding transactions with the counterparty will be terminated and all amounts outstanding will be settled on a net basis. Except for the event of default, all outstanding transactions with the counterparty are settled on a gross basis and generally do not result in offsetting the assets and liabilities in the balance sheet.

		2015			2014		
	Note	Gross amounts of financial instruments in the balance sheet	Related financial instruments that have not been offset	Net amount	Gross amounts of financial instruments in the balance sheet	Related financial instruments that have not been offset	Net amount
		'000	'000	'000	'000	'000	'000
Financial assets							
Trade bills	13(a)	594,230	125,211	469,019	710,926	132,223	578,703
Advances to customers	14(a)	550,739	171,688	379,051	712,906	232,330	480,576
		1,144,969	**296,899**	**848,070**	**1,423,832**	**364,553**	**1,059,279**
Financial liabilities							
Deposit from customers	18	1,434,047	248,210	1,185,837	1,459,506	307,910	1,151,596
Imprest and margin accounts	19	192,806	48,689	144,117	256,157	56,643	199,514
		1,626,853	**296,899**	**1,329,954**	**1,715,663**	**364,553**	**1,351,110**

29 Financial risk management (continued)

(b) Market risk management

Market risk is the risk that movements in interest rates or foreign exchange rates will result in losses in on and off balance sheet positions.

The principal derivative instruments used by the Bank are foreign exchange rate contracts for hedging positions arising from commercial transactions.

The Bank's policy is to take no proprietary trading positions. The Bank does not engage in speculative trading activities, and hence it is not exposed to market risk arising from the trading book.

The Bank has been exempted under section 22(1) of the Banking (Capital) Rules from the calculation of market risk under section 17.

(i) Currency risk

Currency risk is the risk to earnings or capital emanating from the movement of foreign exchange rates. Foreign exchange exposures originate mainly from the trade finance business. The risk thereof has been largely eliminated by consciously devising policies that expressly prohibit speculation in currencies and mandate that trade finance related currency transactions are covered simultaneously and aggregate open positions exceeding amount equivalent to US$1 million cannot be left overnight in currencies other than US$. All exposures are managed by the Chief Financial Officer on a daily basis and reviewed periodically by the Asset and Liability Management Committee.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 Financial risk management (continued)

(b) Market risk management (continued)

(i) Currency risk (continued)

Foreign exchange exposures arising from non-trading and structural positions, with an individual currency constituting 10% or more of the total net position in all foreign currencies, are shown as follows:

	2015			2014		
	Total '000	United States Dollars '000	Other foreign currencies '000	Total '000	United States Dollars '000	Other foreign currencies '000
Assets						
Cash and balances with banks	102,417	73,423	28,994	132,603	79,508	53,095
Placements with banks	58,851	-	58,851	85,323	38,785	46,538
Investments	314,055	314,055	-	161,279	161,279	-
Trade bills	594,230	585,270	8,960	710,926	703,271	7,655
Advances to customers	423,972	418,795	5,177	543,028	540,267	2,761
Other assets	82,812	82,523	289	92,252	90,792	1,460
Spot assets	**1,576,337**	**1,474,066**	**102,271**	**1,725,411**	**1,613,902**	**111,509**
Liabilities						
Deposits and balances of banks	(2,668)	(2,668)	-	(5,650)	(5,650)	-
Deposits from customers	(1,273,707)	(1,189,308)	(84,399)	(1,279,205)	(1,187,901)	(91,304)
Other liabilities	(253,370)	(235,822)	(17,548)	(333,496)	(318,075)	(15,421)
Spot liabilities	**(1,529,745)**	**(1,427,798)**	**(101,947)**	**(1,618,351)**	**(1,511,626)**	**(106,725)**
Forward purchases	-	-	-	4,301	4,301	-
Forward sales	-	-	-	(67,100)	(62,799)	(4,301)
	-	-	-	**(62,799)**	**(58,498)**	**(4,301)**
Net non structural position	**46,592**	**46,268**	**324**	**44,261**	**43,778**	**483**

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 Financial risk management (continued)

(b) Market risk management (continued)

(i) Currency risk (continued)

The Bank does not trade in foreign currencies, nor takes any other exposures on account of its clients. The Bank's foreign currency transactions primarily relate to discounting of foreign currency export and import bills. The exchange positions arising from trade bills as well as customers' foreign currency deposit-related transactions are covered in the local market. From time to time the Bank enters into foreign exchange forward transactions to mitigate currency risk. Details of such transactions appear in the above table.

As the majority (95%) of the Bank's financial instruments at 31 December 2015 and 2014 were denominated in either Hong Kong dollars ("HK$") or United States dollars ("US$") and the US$ is pegged to the HK$, management does not consider there to be any significant currency risk associated with them.

(ii) Interest rate risk

The Bank's interest rate risk positions arise from trade finance, lending and deposit taking activities. Interest rate risk primarily results from the timing difference in the repricing of interest-bearing assets and liabilities. It also relates to positions from non-interest bearing liabilities including shareholders' funds, as well as from certain fixed rate trade finance transactions and liabilities.

The Bank monitors interest rate movements by applying a weighting to assets and liabilities on the balance sheet. Management monitors the weighted average rates on deposits, lending and placements to identify any mismatched exposures and alters the interest rate strategy accordingly. Interest bearing deposits from customers are for a fixed maturity mostly for a three month period and are generally utilised for a similar period. Surplus liquidity is placed in the interbank market and investments. A greater portion of the loans and trade advances is repriceable on a per-transaction basis. Hence the risk element is contained swiftly and the magnitude of the risk posed by interest rates movement is low.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 Financial risk management (continued)

(b) Market risk management (continued)

(ii) Interest rate risk (continued)

				2015			
Interest sensitivity of assets and liabilities	Effective interest rate	Total	3 months or less	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	Non-interest bearing
	%	'000	'000	'000	'000	'000	'000
Assets							
Cash and balances with banks	-	165,229	-	-	-	-	165,229
Placements with banks	0.76%	453,851	449,940	3,911	-	-	-
Investments	2.68%	323,157	34,008	15,621	273,528	-	-
Trade bills	4.77%	594,230	534,046	60,184	-	-	-
– Collective impairment allowance for trade bills	-	(5,996)	-	-	-	-	(5,996)
– Individual impairment allowance for trade bills	-	(7,875)	-	-	-	-	(7,875)
Advances to customers	5.04%	550,739	434,930	65,834	49,975	-	-
– Collective impairment allowance for advances to customers	-	(5,561)	-	-	-	-	(5,561)
– Individual impairment allowance for advances to customers	-	(9,885)	-	-	-	-	(9,885)
Tax paid in advance	-	3,615	-	-	-	-	3,615
Deferred tax assets	-	1,234	-	-	-	-	1,234
Fixed assets	-	112,917	-	-	-	-	112,917
Other assets	-	91,696	-	-	-	-	91,696
Total assets	-	**2,267,351**	**1,452,924**	**145,550**	**323,503**	-	**345,374**
Liabilities							
Deposits and balances of banks	-	4,162	-	-	-	-	4,162
Deposits from customers	1.67%	1,434,047	1,118,892	313,498	1,657	-	-
Other liabilities	-	285,999	-	-	-	-	285,999
Total liabilities	-	**1,724,208**	**1,118,892**	**313,498**	**1,657**	-	**290,161**
Net Re-Pricing gap	-	**543,143**	**334,032**	**(167,948)**	**321,846**	-	**55,213**

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 Financial risk management (continued)

(b) Market risk management (continued)

(ii) Interest rate risk (continued)

	2014						
Interest sensitivity of assets and liabilities	Effective interest rate	Total	3 months or less	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	Non-interest bearing
	%	'000	'000	'000	'000	'000	'000
Assets							
Cash and balances with banks	-	224,733	-	-	-	-	224,733
Placements with banks	1.03%	360,323	360,323	-	-	-	-
Investments	2.87%	171,015	-	31,432	139,583	-	-
Trade bills	4.95%	710,926	637,051	73,875	-	-	-
– Collective impairment allowance for trade bills	-	(7,477)	-	-	-	-	(7,477)
– Individual impairment allowance for trade bills	-	(795)	-	-	-	-	(795)
Advances to customers	4.97%	712,906	583,316	52,846	76,744	-	-
– Collective impairment allowance for advances to customers	-	(7,385)	-	-	-	-	(7,385)
– Individual impairment allowance for advances to customers	-	(9,030)	-	-	-	-	(9,030)
Tax paid in advance	-	388	-	-	-	-	388
Deferred tax assets	-	1,132	-	-	-	-	1,132
Fixed assets	-	118,110	-	-	-	-	118,110
Other assets	-	101,177	-	-	-	-	101,177
Total assets	-	**2,376,023**	**1,580,690**	**158,153**	**216,327**	-	**420,853**
Liabilities							
Deposits and balances of banks	-	6,745	-	-	-	-	6,745
Deposits from customers	1.66%	1,459,506	1,249,470	210,036	-	-	-
Other liabilities	-	357,766	-	-	-	-	357,766
Total liabilities	-	**1,824,017**	**1,249,470**	**210,036**	-	-	**364,511**
Net Re-Pricing gap	-	**552,006**	**331,220**	**(51,883)**	**216,327**	-	**56,342**

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 Financial risk management (continued)

(b) Market risk management (continued)

(ii) Interest rate risk (continued)

At 31 December 2015, it is estimated that a general increase/decrease of 50 basis points in interest rates (2014: 50 basis points in interest rates), with all other variables held constant, would not significantly impact the Bank's profit after taxation (2014: insignificant impact).

The sensitivity analysis above has been determined assuming that the change in interest rate had occurred at the balance sheet date and had been applied to the exposure to interest rate risk for non-derivative financial instruments in existence at that date. The 50 basis point increase or decrease represents management's assessment of a reasonable possible change in interest rates over the period until the next annual balance sheet date.

(c) Liquidity risk management

Liquidity relates to the ability of a company to meet its obligations as they fall due.

The Bank manages the liquidity structure of its assets, liabilities and commitments so as to ensure that liquidity sources match funding needs and that the statutory liquidity ratio is complied with. The Bank's average liquidity maintenance ratio in 2015 of 143.65% (2014: liquidity ratio of 114.27%) was well above the statutory minimum ratio of 25%.

The finance department reviews the current and prospective funding requirements for all operations through monitoring of the liquidity maintenance ratio and the maturity mismatch profile. Liquidity risk is managed by holding sufficient liquid assets (e.g. cash and short term funds) of appropriate quality to ensure that short term funding requirements are covered within prudent limits. Customer deposits form a significant part of the Bank's overall funding and they have remained relatively diversified and stable. Adequate standby facilities are maintained to provide strategic liquidity to meet unexpected and material cash outflows in the ordinary course of business. The Asset and Liability Management Committee measures the liquidity and adequacy of funds periodically and evaluates the overall risks and mitigation. The Committee also manages the funds and investments within the internal and regulatory framework.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 Financial risk management (continued)

(c) Liquidity risk management (continued)

Analysis of non derivative assets and liabilities by remaining maturity

The following maturity profile is based on the remaining period at the balance sheet date to the contractual maturity date.

	2015							
	Total	Repayable on demand	Within 1 month	Over 1 month but within 3 months	Over 3 months but within 1 year	Over 1 year but within 5 years	Over 5 years	Indefinite
	'000	'000	'000	'000	'000	'000	'000	'000
Assets								
Cash and balances with banks	165,228	165,228	-	-	-	-	-	-
Placements with banks	453,851	-	202,111	247,829	3,911	-	-	-
Investments	323,157	-	17,270	16,738	15,621	273,528	-	-
Trade bills	580,359	78,848	181,555	260,379	59,577	-	-	-
Advances to customers	535,293	81,928	109,682	229,044	65,169	49,470	-	-
Tax paid in advance	3,615	-	-	-	3,615	-	-	-
Deferred tax assets	1,234	-	-	-	-	-	-	1,234
Fixed assets	112,917	-	-	-	-	-	-	112,917
Other assets	91,697	1,033	20,511	61,208	8,945	-	-	-
Total assets	**2,267,351**	**327,037**	**531,129**	**815,198**	**156,838**	**322,998**	-	**114,151**
Liabilities								
Deposits and balances of banks	4,162	4,162	-	-	-	-	-	-
Deposits from customers	1,434,047	6,634	443,895	668,363	313,498	1,657	-	-
Other liabilities	285,999	197,612	18,234	61,208	8,945	-	-	-
Total liabilities	**1,724,208**	**208,408**	**462,129**	**729,571**	**322,443**	**1,657**	-	-
Net liability gap	**543,143**	**118,629**	**69,000**	**85,627**	**(165,605)**	**321,341**	-	**114,151**

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 Financial risk management (continued)

(c) Liquidity risk management (continued)

Analysis of non derivative assets and liabilities by remaining maturity

The following maturity profile is based on the remaining period at the balance sheet date to the contractual maturity date.

	2014							
	Total	Repayable on demand	Within 1 month	Over 1 month but within 3 months	Over 3 months but within 1 year	Over 1 year but within 5 years	Over 5 years	Indefinite
	'000	'000	'000	'000	'000	'000	'000	'000
Assets								
Cash and balances with banks	224,733	224,733	-	-	-	-	-	-
Placements with banks	360,323	-	181,472	178,851	-	-	-	-
Investments	171,015	-	-	-	31,432	139,583	-	-
Trade bills	702,654	99,908	195,554	334,094	73,098	-	-	-
Advances to customers	696,491	112,838	184,381	271,024	52,299	75,949	-	-
Tax paid in advance	388	-	-	-	388	-	-	-
Deferred tax assets	1,132	-	-	-	-	-	-	1,132
Fixed assets	118,110	-	-	-	-	-	-	118,110
Other assets	101,177	1,604	28,240	60,916	10,417	-	-	-
Total assets	**2,376,023**	**439,083**	**589,647**	**844,885**	**167,634**	**215,532**	-	**119,242**
Liabilities								
Deposits and balances of banks	6,745	6,745	-	-	-	-	-	-
Deposits from customers	1,459,506	-	448,942	800,528	210,036	-	-	-
Other liabilities	357,766	260,803	25,630	60,916	10,417	-	-	-
Total liabilities	**1,824,017**	**267,548**	**474,572**	**861,444**	**220,453**	-	-	-
Net liability gap	**552,006**	**171,535**	**115,075**	**(16,559)**	**(52,819)**	**215,532**	-	**119,242**

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 Financial risk management (continued)

(c) Liquidity risk management (continued)

The total gross undiscounted cash flows for the above liabilities are the same as shown above except for deposits and balances of banks and deposits from customers which are as follows:

	2015							
	Carrying amount	Total contractual undiscounted cash flows	Repayable on demand	Within 1 month	Over 1 month but within 3 months	Over 3 months but within 1 year	Over 1 year but within 5 years	Indefinite
	'000	'000	'000	'000	'000	'000	'000	'000
Deposits and balances of banks	4,162	4,162	4,162	-	-	-	-	-
Deposits from customers	1,434,047	1,443,952	6,680	445,695	672,395	317,521	1,661	-
	1,438,209	**1,448,114**	**10,842**	**445,695**	**672,395**	**317,521**	**1,661**	-

	2014							
	Carrying amount	Total contractual undiscounted cash flows	Repayable on demand	Within 1 month	Over 1 month but within 3 months	Over 3 months but within 1 year	Over 1 year but within 5 years	Indefinite
	'000	'000	'000	'000	'000	'000	'000	'000
Deposits and balances of banks	6,745	6,745	6,745	-	-	-	-	-
Deposits from customers	1,459,506	1,468,679	-	451,218	804,631	212,830	-	-
	1,466,251	**1,475,424**	**6,745**	**451,218**	**804,631**	**$212,830**	-	-

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 Financial risk management (continued)

(d) Operational risk

Operational risk is the risk of potential loss arising from inadequate or a failure in internal processes, people and systems or from external events.

The Board of Directors and senior management are responsible for approving and reviewing the overall business strategies and the policies for each major area of operations. A Risk and Compliance Management Committee is in place to manage operational risks.

The Bank recognises the importance of managing operational risk in a pro-active manner. Operational risk management tools and mechanisms adopted include operational risk incidents reporting, key risk indicators, operation manuals, accounting controls, business continuity planning, insurance policies etc.

The Bank attaches great importance to conducting its business in a safe and sound manner. Strict control is exercised at every level of operations. Additionally, an internal audit system plays an essential role in ensuring due adherence to policies, various internal and statutory limits, and regulatory requirements thus limiting operational risk.

(e) Capital management

The HKMA sets and monitors capital requirements for the Bank as a whole. In implementing current capital requirements the HKMA requires the Bank to maintain prescribed ratios of capital to total risk-weighted assets. The Bank's operations are categorised as banking book and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures.

In addition to meeting the regulatory requirements, the Bank's primary objectives when managing capital are to safeguard the Bank's 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 commensurate with the level of risk being taken 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. The Bank considers capital to include share capital and reserves.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 Financial risk management (continued)

(e) Capital management (continued)

The Bank monitors its capital adequacy ratios on a quarterly basis. The capital adequacy ratios are computed as specified by the HKMA for its regulatory purposes and are in accordance with the Banking (Capital) (Amendment) Rules 2012 and 2013 of the Hong Kong Banking Ordinance which came into effect from 1 January 2013 and 30 June 2013 respectively.

The Bank has complied with all capital requirements throughout the years ended 31 December 2015 and 2014 and is well above the minimum required ratio set by the HKMA.

30 Fair values of financial instruments

(a) Financial instruments carried at fair value

Fair value estimates are generally subjective in nature, and are made as of a specific point in time based on the characteristics of the financial instruments and relevant market information. Where available, the most suitable measure for fair value is the quoted market price. In the absence of organised secondary markets for most financial instruments, and in particular for loans, deposits and unlisted derivatives, direct market prices are not available. The fair value of such instruments was therefore calculated on the basis of well-established valuation techniques using current market parameters. In particular, the fair value is a theoretical value applicable at a given reporting date, and hence can only be used as an indicator of the value realisable in a future sale.

The Bank measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

- Level 1 - Quoted market price (unadjusted) in an active market for an identical instrument.
- Level 2 - Observable inputs which fail to meet Level 1, and not using significant unobservable inputs. Unobservable inputs are inputs for which market data are not available.
- Level 3 - Fair value measured using significant unobservable inputs.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

30 Fair values of financial instruments (continued)

(b) Fair value

The table below analyses financial instruments, measured at fair value at the end of the reporting period, by the level in the fair value hierarchy into which the fair value treatment is categorised:

	2015				2014			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets								
Available-for-sale financial assets: – Debt securities	-	80,508,498	-	80,508,498	-	23,104,518	-	23,104,518
Derivative financial instruments: – Forward exchange contracts	-	-	-	-	-	38,817	-	38,817
	-	80,508,498	-	80,508,498	-	23,143,335	-	23,143,335
Liabilities								
Derivative financial instruments: – Forward exchange contracts	-	-	-	-	-	35,292	-	35,292

During the year there were no significant transfers of financial instruments between Level 1 and Level 2 of the fair value hierarchy.

31 Accounting estimates and judgements

Key sources of estimation uncertainty

Note 30 contains information about the assumptions and their risk factors relating to fair value of financial instruments. Another key source of estimation uncertainty is as follows:

Impairment losses - Loans and advances

Loan portfolios are reviewed periodically to assess whether impairment losses exist. The Bank makes judgements as to whether there is any objective evidence that a loan is impaired. Objective evidence for impairment includes observable data that the payment status of borrowers in a group has adversely changed. It may also include observable data that local or economic conditions have worsened which correlate with defaults on the assets in the Bank. If management has determined, based on their judgement, that objective evidence for impairment exists, expected future cash flows are estimated based on historical loss experience for assets with credit risk characteristics similar to those of the Bank. Historical loss experience is adjusted on the basis of the current observable data.

Management reviews the methodology and assumptions used in estimating future cash flows regularly to reduce any difference between loss estimates and actual loss experience.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

32 Possible impact of amendments, new standards and interpretations issued but not yet effective for the year ended 31 December 2015

Up to the date of issue of the financial statements, the HKICPA has issued a few amendments and new standards which are not yet effective for the year ended 31 December 2015 and which have not been adopted in these financial statements. These include the following which may be relevant to the Bank.

	Effective for accounting periods beginning on or after
Annual Improvements to HKFRSs 2012-2014 Cycle	1 January 2016
Amendments to HKAS 1, *Disclosure initiative*	1 January 2016
Amendments to HKAS 16 and HKAS 38, *Clarification of acceptable methods of depreciation and amortisation*	1 January 2016
HKFRS 9, *Financial instruments*	1 January 2018
HKFRS 15, *Revenue from contracts with customers*	1 January 2018

The Bank is 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 them is unlikely to have a significant impact on the Bank's results of operations and financial position except for HKFRS 9, Financial Instruments. It is however impracticable to quantify the effect of the implications of this standard as at the date of publication of these financial statements.

Unaudited supplementary financial information

(Expressed in Hong Kong dollars)

(a) Capital and capital adequacy

	2015	2014
Capital ratio:		
Common Equity Tier 1 ("CET1") Capital Ratio	34.60%	34.22%
Tier 1 Capital Ratio	34.60%	34.22%
Total Capital Ratio	36.04%	35.64%

The components of total capital before and after deductions are shown below:

	2015 '000	2014 '000
CET1 Capital:		
CET1 Capital instruments	300,000	300,000
Retained earnings	216,850	224,832
Disclosed reserves	26,293	27,175
CET1 Capital before deductions	**543,143**	**552,007**
Regulatory deductions to CET1 capital:		
Reserves arising from revaluation of land and buildings	(11,244)	(11,244)
Reserve for general banking risk	(16,000)	(16,000)
Net deferred tax assets	(1,234)	(1,132)
Total CET1 Capital	**514,665**	**523,631**
Additional Tier 1 ("AT1") Capital	-	-
Total Tier 1 ("T1") Capital	**514,665**	**523,631**
Tier 2 ("T2") Capital		
Reserves arising from revaluation of land and buildings	5,060	5,060
Reserve for general banking risk and collective impairment allowances	16,219	16,632
Regulatory deductions to T2 capital	-	-
Total T2 Capital	**21,279**	**21,692**
Total Capital	**535,944**	**545,323**

Unaudited supplementary financial information

(Expressed in Hong Kong dollars)

(a) Capital and capital adequacy (continued)

The capital adequacy ratios were calculated in accordance with the Banking (Capital) Rules (the "Capital Rules"). In accordance with the Capital Rules, the Bank has adopted the "Basic Approach" for the calculation of the risk-weighted assets for credit risk, and the "Basic Indicator Approach" for the calculation of operational risk. The Bank has been exempted under section 22(1) of the Banking (Capital) Rules from the calculation of market risk under section 17.

CET1 capital instruments represents HK$300,000,000 (2014: HK$300,000,000) of issued and fully paid ordinary shares. The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Bank. All ordinary shares rank equally with regard to the Bank's residual assets.

The revaluation reserve has been set up in accordance with the accounting policies adopted for land and buildings. The revaluation reserve is not available for distribution to shareholders.

A regulatory reserve of $16,000,000 (2014: $16,000,000) is maintained to satisfy the provisions of the Hong Kong Banking Ordinance. Movements in the reserve are made directly through retained earnings.

A collective impairment allowance is maintained to cover potential impairment losses for a group of financial assets with similar credit risk characteristics where the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset.

No item benefits from the transitional arrangements set out in Section 4H to the Capital Rules.

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

- A detailed breakdown of the CETI capital, Additional Tier 1 capital, Tier 2 capital and regulatory deductions applied to the capital base of the institution by using the standard capital disclosures template as specified by the HKMA.

- A full reconciliation of the CETI capital items, Additional Tier 1 capital items, Tier 2 capital items and regulatory deductions applied to the capital base of the institution and the balance sheet in the published financial statements of the institution.

- A description of the main features and the terms and conditions of capital instruments issued by the institution.

Unaudited supplementary financial information

(Expressed in Hong Kong dollars)

(b) Leverage Ratio

	2015	2014
Leverage Ratio	21.05%	20.20%

	2015	2014
	'000	'000
Tier 1 Capital	**514,665**	**523,631**
Exposure Measure	**2,444,991**	**2,592,847**

The leverage ratio as at 31 December 2015 and 31 December 2014 were compiled in accordance with the Leverage Ratio Framework issued by the HKMA.

Leverage ratio disclosures as required by section 24A of the Banking (Disclosure) Rules are available in the section of Regulatory Disclosures of our website www.hbzhongkong.com.

(c) Liquidity information

	2015	2014
Average liquidity maintenance ratio for the year	143.65%	N/A
Average liquidity ratio for the year	N/A	114.27%

The average liquidity maintenance ratio ("LMR") for the year is calculated as the simple average of each month's average LMR as reported in the Liquidity Position Return.

The average liquidity ratio for the year is calculated as the simple average of each month's average ratio in accordance with the Fourth Schedule of the Hong Kong Banking Ordinance.

Unaudited supplementary financial information

(Expressed in Hong Kong dollars)

(d) Segmental information

The Bank's total operating income (net of interest expense) and operating assets directly attributable to the following classes of business are set out below:

	2015			2014		
	Trade finance and deposits taking	Treasury and others	Total	Trade finance and deposits taking	Treasury and others	Total
Interest income	62,004,441	8,985,804	70,990,245	78,026,815	7,112,160	85,138,975
Interest expense	(22,449,900)	(234,438)	(22,684,338)	(23,314,952)	(446,958)	(23,761,910)
Net interest income	**39,554,541**	**8,751,366**	**48,305,907**	**54,711,863**	**6,665,202**	**61,377,065**
Fee and commission income	28,107,898	-	28,107,898	33,050,980	-	33,050,980
Fee and commission expense	(525,271)	-	(525,271)	(544,470)	-	(544,470)
Net fee and commission income	**27,582,627**	-	**27,582,627**	**32,506,510**	-	**32,506,510**
Other net income	**20,222,344**	**1,031,313**	**21,253,657**	**25,068,334**	**1,393,247**	**26,461,581**
Operating income	**87,359,512**	**9,782,679**	**97,142,191**	**112,286,707**	**8,058,449**	**120,345,156**
Operating expenses	(61,874,159)	(6,928,782)	(68,802,941)	(61,301,814)	(4,399,430)	(65,701,244)
Operating profit before provisions	**25,485,353**	**2,853,897**	**28,339,250**	**50,984,893**	**3,659,019**	**54,643,912**
Impairment losses on trade bills and advances to customers	(7,603,000)	-	(7,603,000)	(8,478,870)	-	(8,478,870)
Operating profit after provisions	**17,882,353**	**2,853,897**	**20,736,250**	**42,506,023**	**3,659,019**	**46,165,042**
Profit before taxation	**17,882,353**	**2,853,897**	**20,736,250**	**42,506,023**	**3,659,019**	**46,165,042**
Capital expenditure	-	335,731	335,731	-	61,936,903	61,936,903
Depreciation	(4,935,383)	(552,673)	(5,488,056)	(4,352,956)	(312,397)	(4,665,353)
Segment assets	1,198,342,542	1,069,008,250	2,267,350,792	1,491,326,949	884,696,459	2,376,023,408
Total assets	**1,198,342,542**	**1,069,008,250**	**2,267,350,792**	**1,491,326,949**	**884,696,459**	**2,376,023,408**
Segment liabilities	1,709,543,714	14,664,042	1,724,207,756	1,807,846,411	16,170,333	1,824,016,744
Total liabilities	**1,709,543,714**	**14,664,042**	**1,724,207,756**	**1,807,846,411**	**16,170,333**	**1,824,016,744**

Unaudited supplementary financial information

(Expressed in Hong Kong dollars)

(d) Segmental information (continued)

The Bank's principal activities are the taking of deposits and financing of import/export and local trade.

Segment information has been presented in two reportable segments as follows:

The major component of business is trade finance extended to customers by way of opening letters of credit and financing import and export bills. Within the trade finance portfolio, the emphasis is on purchasing/discounting of export bills with a wide geographical spread. Such advances are of short term duration, normally not exceeding 120 days. The short term nature of the advances provides a cushion against the pronounced adverse changes in the business and economic cycles, deflation in assets prices and risk transfer. The financing of import/export and local trade is sourced through deposits.

Treasury and others includes interbank and capital market activities.

(e) Advances to customers

(i) By industry sector

Loans and advances to customers analysed by the coverage of collateral, overdue amount and the impairment allowance is as follows:

	2015							
	Gross loans and advances	% of gross loans and advances covered by collateral	Overdue loans and advances	Impaired loans and advances	Individually assessed impairment allowance	Collectively assessed impairment allowance	Impairment charged to statement of comprehensive income during the year	Impaired loans written off during the year
	'000	%	'000	'000	'000	'000	'000	'000
Loans for use in Hong Kong individual - other loans	$14,271	100%	-	-	-	-	-	-
Trade finance	536,468	41.7%	88,199	36,623	9,885	5,561	1,636	2,605

Unaudited supplementary financial information

(Expressed in Hong Kong dollars)

(e) Advances to customers (continued)

(i) By industry sector (continued)

	2014							
	Gross loans and advances	% of gross loans and advances covered by collateral	Overdue loans and advances	Impaired loans and advances	Individually assessed impairment allowance	Collectively assessed impairment allowance	Impairment charged to statement of comprehensive income during the year	Impaired loans written off during the year
	'000	%	'000	'000	'000	'000	'000	'000
Loans for use in Hong Kong individual - other loans	$26,682	100%	-	-	-	-	-	-
Trade finance	686,224	39.4%	107,163	17,979	9,030	7,385	6,312	7,196

(ii) By geographical area

Advances to customers by geographical area are classified according to the location of the counterparties after taking into account the transfer of risk. In general, risk transfer applies when an advance is guaranteed by a party in an area which is different from that of the counterparty.

	2015	2014
Gross advances to customers		
Hong Kong	536,962,696	705,917,329
Asia Pacific excluding Hong Kong	-	3,928,250
Africa, Caribbean, Latin America and North America	13,776,578	3,060,071
Europe	-	-
	550,739,274	**712,905,650**

All impaired advances to customers at 31 December 2015 and 2014 are located in Hong Kong.

Unaudited supplementary financial information

(Expressed in Hong Kong dollars)

(f) Overdue and rescheduled assets

The gross amount of overdue assets are as follows:

	2015							
	Advances to customers				Trade bills			
	Amount	Collateral value	% of gross advances	Impairment allowance	Amount	Collateral value	% of gross trade bills	Impairment allowance
Overdue for:								
– 6 months or less but over 3 months	7,969,757	7,969,757	1.45%	320,000	536,694	433,037	0.09%	-
– 1 year or less but over 6 months	21,462,976	17,784,510	3.90%	1,942,919	25,228,542	22,145,831	4.24%	1,412,977
– Over 1 year	5,253,804	350,622	0.95%	4,666,691	6,415,399	700,966	1.08%	5,114,702
	34,686,537	**26,104,889**	**6.30%**	**6,929,610**	**32,180,635**	**23,279,834**	**5.41%**	**6,527,679**

	2014							
	Advances to customers				Trade bills			
	Amount	Collateral value	% of gross advances	Impairment allowance	Amount	Collateral value	% of gross trade bills	Impairment allowance
Overdue for:								
– 6 months or less but over 3 months	21,791,701	21,132,298	3.06%	-	11,444,818	6,399,596	1.61%	-
– 1 year or less but over 6 months	3,112,374	1,829,221	0.44%	-	3,016,250	2,257,906	0.42%	395,000
– Over 1 year	6,743,643	2,749,618	0.94%	3,766,794	615,002	-	0.09%	400,000
	31,647,718	**25,711,137**	**4.44%**	**3,766,794**	**15,076,070**	**8,657,502**	**2.12%**	**795,000**

Collaterals held with respect to overdue advances to customers and trade bills are cash deposits and mortgage property with the Bank.

(g) Non-bank Mainland exposures

The analysis of non-bank Mainland exposures is based on the categories of non-bank counterparties and the type of direct exposures defined by the Hong Kong Monetary Authority under the Banking (Disclosure) Rules with reference to the Hong Kong Monetary Authority return of non-bank Mainland exposures.

Unaudited supplementary financial information

(Expressed in Hong Kong dollars)

(g) Non-bank Mainland exposures (continued)

	On-balance sheet exposure '000	Off-balance sheet exposure '000	Total '000
2015			
1. Central government, central government-owned entities and their subsidiaries and joint ventures (JVs)	59,558	-	59,558
2. Local governments, local government-owned entities and their subsidiaries and JVs	41,304	-	41,304
3. PRC nationals residing in Mainland China or other entities incorporated in Mainland China and their subsidiaries and JVs	-	-	-
4. Other entities of central government not reported in item 1 above	-	-	-
5. Other entities of local governments not reported in item 2 above	-	-	-
6. PRC nationals residing outside Mainland China or entities incorporated outside Mainland China where the credit is granted for use in Mainland China	167,207	93,680	260,887
7. Other counterparties where the exposures are considered by the reporting institution to be non-bank Mainland China exposures	81,626	747	82,373
	349,695	**94,427**	**444,122**
Total assets after provision	2,186,740	-	-
On-balance sheet exposures as percentage of total assets	15.99%	-	-
	-	-	-
2014			
1. Central government, central government-owned entities and their subsidiaries and joint ventures (JVs)	19,428	-	19,428
2. Local governments, local government-owned entities and their subsidiaries and JVs	11,468	-	11,468
3. PRC nationals residing in Mainland China or other entities incorporated in Mainland China and their subsidiaries and JVs	-	-	-
4. Other entities of central government not reported in item 1 above	-	-	-
5. Other entities of local governments not reported in item 2 above	-	-	-
6. PRC nationals residing outside Mainland China or entities incorporated outside Mainland China where the credit is granted for use in Mainland China	190,055	168,270	358,325
7. Other counterparties where the exposures are considered by the reporting institution to be non-bank Mainland China exposures	9,264	-	9,264
	230,215	**168,270**	**398,485**
Total assets after provision	2,283,841	-	-
On-balance sheet exposures as percentage of total assets	10.08%	-	-

Unaudited supplementary financial information

(Expressed in Hong Kong dollars)

(h) International claims

The country risk exposures are prepared according to the location and types of the counterparties as defined by the HKMA under the Banking (Disclosure) Rules with reference to the HKMA's Return of International Banking Statistics. International claims are on-balance sheet exposures to counterparties based on the location of the counterparties after taking into account the transfer of risk, and represent the sum of cross-border claims in all currencies and local claims in foreign currencies. International claims on individual areas, after risk transfer, amounting to 10% or more of the aggregate international claims are shown as below.

			Non-bank private sector		
As at 31 December 2015	Banks	Official sector	Non-bank financial institutions	Non-financial private sector	Total
HK$ million equivalent					
Developed countries	48	-	-	95	143
Offshore centres	151	-	-	523	674
Developing Europe	1	-	-	52	53
Developing Latin America and Caribbean	9	-	-	30	39
Developing Africa and Middle East	12	-	-	103	115
Developing Asia and Pacific	466	8	-	220	694
Total	**687**	**8**	**-**	**1,023**	**1,718**

			Non-bank private sector		
As at 31 December 2014	Banks	Official sector	Non-bank financial institutions	Non-financial private sector	Total
HK$ million equivalent					
Developed countries	84	-	-	92	176
Offshore centres	180	-	-	625	805
Developing Europe	-	-	-	38	38
Developing Latin America and Caribbean	11	-	-	34	45
Developing Africa and Middle East	57	-	-	127	184
Developing Asia and Pacific	434	8	-	145	587
Total	**766**	**8**	**-**	**1,061**	**1,835**

Unaudited supplementary financial information

(Expressed in Hong Kong dollars)

(i) Corporate governance

The Bank is committed to high standards of corporate governance, and has complied with the guideline in the supervisory policy manual module CG-1 "Corporate Governance of Locally Incorporated Authorised Institutions" issued by the Hong Kong Monetary Authority ("HKMA").

(1) Board level Committees

The Board of Directors has established two board level committees, namely the Board Risk and Compliance Committee and the Board Audit Committee.

(i) Board Risk and Compliance Committee

The Board Risk and Compliance Committee is responsible for, among other things, the Bank's risk profile, risk appetite and tolerance, effectiveness of the risk management framework and systems of internal control and compliance. The Committee comprises two non-executive directors and one executive director.

(ii) Board Audit Committee

The main purpose of the Board Audit Committee is to represent and assist the Board of Directors in providing independent review and monitoring of financial reporting process, internal control system, the internal and external audit process and compliance with regulatory requirements. The Committee comprises of one independent non-executive director and two non-executive directors.

(2) Specialised Management Committees

The Board of Directors has established several specialised management committees, namely the Risk and Compliance Management Committee, Credit Committee, Asset & Liability Committee and IT Steering Committee.

(i) Risk and Compliance Management Committee

The Risk and Compliance Management Committee is entrusted with the task of putting in place systems and procedures that address the prevention of risks emerging or likely to emerge. The Committee identifies all quantifiable and material risk factors and evaluates the adequacy of organisational policies and procedures to manage the risks effectively. The Committee is also responsible for monitoring and reviewing regulatory compliance within the institution. The Committee comprises the Chief Executive, Alternate Chief Executives, Chief Risk Officer, Chief Financial Officer, Chief Compliance Officer and Executive.

Unaudited supplementary financial information

(Expressed in Hong Kong dollars)

(i) Corporate governance (continued)

(ii) Credit Committee

The Credit Committee is responsible for building and maintaining an infrastructure that promotes growth of a quality loan portfolio and minimises losses within the constraints of established policies and relevant regulations. The Committee approves credit limits up to a defined threshold. It also determines and maintains adequate loan loss allowances. The Committee comprises the Chief Executive, Alternate Chief Executives, Chief Risk Officer, Credit Risk Manager and Executive.

(iii) Asset and Liability Committee

The Asset and Liability Committee's principal responsibility is to maintain an effective risk control framework relating to balance sheet structure, liquidity and capital management and market risks while achieving an optimal return. The Committee recommends policy directives to the Board of Directors and provides analytical services relating to funding and investment strategs. The Committee comprises the Chief Executive, Alternate Chief Executives, Chief Risk Officer, Chief Financial Officer and Executive.

(iv) IT Steering Committee

The IT Steering Committee is responsible for authorisation of system changes, review of computer hardware/ software security and performance, overview of data integrity of transactions and information. The committee comprises the Chief Executive, Alternate Chief Executive, Head of IT, Chief Risk Officer, Chief Financial Officer and Chief Compliance Officer.

Unaudited supplementary financial information

(Expressed in Hong Kong dollars)

(j) Remuneration system

The Bank has adopted and is committed to promoting a sound and prudent remuneration system in accordance with the guideline in Part 3 of the Supervisory Policy Manual Module CG-5 "Guideline on a Sound Remuneration System" issued by the HKMA.

The Bank recognises that achievement of its mission, vision and strategic objectives depends on the quality and commitment of its staff. The principles of the HBZ Remuneration Policy reflect its goal to attract, retain, motivate and reward quality staff. The guiding principles used to determine the institution-wide remuneration policy are based on sound governance, internal equality, competitiveness, sustainability and conservative approach to risk-taking. The remuneration policy is reviewed annually by the Board of Directors.

To establish the relative merit and worth of each position and ensure equity in remuneration, a performance appraisal system is in place and is consistently applied across all areas of work and responsibilities. Performance of individual employees is based on a set of pre-defined criteria which are determined according to the individual's designation as well as relevant qualitative and quantitative factors. Promotions and increments are linked to performance appraisals.

The parameters used for allocating cash versus other forms of remuneration depend on the organizational status of the employee. The remuneration package across the organization is structured with a fixed compensation component only. The remuneration package comprises of basic salary, allowances, retirement scheme contributions, bonuses and benefits. A provident fund under the Occupational Retirement Scheme Ordinance is also in place.

The senior management comprises of the Chief Executive and two Alternate Chief Executives while key personnel include two senior executives of the Bank. The aggregate remuneration for senior management and key personnel are shown below in accordance with the disclosure requirement of the afore-mentioned guideline:

	2015		2014	
	Senior Management	Key Personnel	Senior Management	Key Personnel
Fixed Remuneration				
– Cash based	6,224,708	3,386,844	6,050,800	2,132,448
– Retirement scheme contributions	360,977	213,430	347,828	92,630
– Benefit in kind	600,000	-	600,000	-

Benefit in kind represents provision of the Bank's residential apartment. No sign-on awards or severance payments were made to the senior management or key personnel during the year.

Unaudited supplementary financial information

(Expressed in Hong Kong dollars)

The capital requirements on each class of exposures calculated under the basic (credit risk) approach at the balance sheet date can be analysed as follows:

Classes of exposure

	2015	2014
	'000	'000
Sovereign	640	646
Bank	16,121	15,395
Corporate	72,848	74,860
Other exposures which are not past due	9,495	9,693
Past due	8,024	5,607
Total capital requirements for on-balance sheet exposures	**107,128**	**106,201**
Trade-related contingencies	4,697	5,840
Exchange rate contracts	-	11
Total capital requirements for off-balance sheet exposures	4,697	5,851
	111,825	**112,052**

Capital charge

The capital charge for operational risk calculated in accordance with the basic indicator approach at the balance sheet date is:

	2015	2014
	'000	'000
Capital charge for operational risk	**16,583**	**17,596**

List of branches

Head Office and Main Branch

		17/F, Wing On House, 71 Des Voeux Road,
		Central, Hong Kong
	Tel:	(852) 2521 4631
	Fax:	(852) 2810 4477
	Swift:	HFLIHKHHXXX
	Email:	mainoffice@hbzhongkong.com
	Website:	www.hbzhongkong.com

Kowloon Branch

		Unit 1 & 20, 12/F, Lippo Sun Plaza, 28 Canton Road,
		Tsim Sha Tsui, Kowloon, Hong Kong
	Tel:	(852) 2376 0211
	Fax:	(852) 2375 7629
	Swift:	HFLIHKHHXXX
	Email:	kowloon@hbzhongkong.com

Lai Chi Kok Branch

		Unit C, 25/F, Billion Plaza II, 10 Cheung Yue Street,
		Cheung Sha Wan, Kowloon, Hong Kong
	Tel:	(852) 2480 6786
	Fax:	(852) 2480 0804
	Swift:	HFLIHKHHXXX
	Email:	laichikok@hbzhongkong.com

Kwun Tong Branch

		Unit G, 29/F., Legend Tower, 7 Shing Yip Street,
		Kwun Tong, Kowloon, Hong Kong.
	Tel:	(852) 2389 3808
	Fax:	(852) 2389 5895
	Swift:	HFLIHKHHXXX
	Email:	kwuntong@hbzhongkong.com

Hung Hom Branch

		8/F, 805, Hunghom Com. Centre B, 37 Ma Tau Wai Road,
		Hung Hom, Kowloon, Hong Kong.
	Tel:	(852) 2627 1185
	Fax:	(852) 2627 1135
	Swift:	HFLIHKHHXXX
	Email:	hunghom@hbzhongkong.com

Services we offer

We offer a wide range of financial services for Foreign Trade related activities. Our growth and successful operations are singularly fueled by our commitment to provide fast service and a rapid response to our customers' needs. Flexibility and capability to tailor make products to meet and anticipate emerging needs are the trade marks our customers have come to appreciate.

Our products include:

Corporate Financial Services

- Multi-currency Deposits
- Foreign Exchange
- Letters of Credit & Guarantees
- Post Import Finance
- Pre-shipment Finance
- Export Documents Purchase and Discounting
- Accounts Receivable Financing
- Revolving and Term Loans
- Documentary Collection
- International Payments
- Customised Trade Solutions
- Trade Information and Access to International Network of Correspondent Banks

Financial Institutional Services

- Letters of Credit Advising and Confirmation
- Negotiation and discounting of Documents under Letters of Credit
- Rediscounting of Bankers Acceptances / Forfaiting
- Buyers Credit