



Habib Bank Zurich (Hong Kong) Limited

Annual Report 2019

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Habib Bank Zurich (Hong Kong) Limited

Corporate information

Board of Directors

Mohamedali R. Habib	Chairman
Paul Jeremy Brough	Independent Non-Executive Director
Alex Kwong Fai Kam	Independent Non-Executive Director
Rajat Garg	Non-Executive Director
Ikram Quraishi	Non-Executive Director
Sachil Dagur	Executive Director

Management

Sachil Dagur	Chief Executive
Masud Abid	EVP
Hamza Habib	SVP
Meheryar Mavalvala	CFO

Auditors

KPMG, <i>Certified Public Accountants</i>

Parent company

Habib Bank AG Zurich, <i>Incorporated in Switzerland</i>
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International Finance Centre, Central

Report of the directors

The directors submit herewith their annual report together with the audited financial statements for the year ended 31 December 2019.

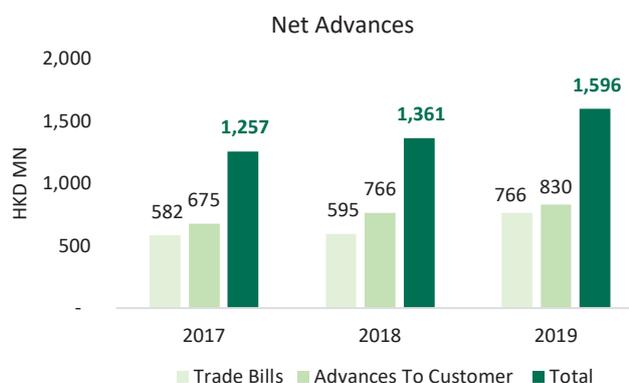
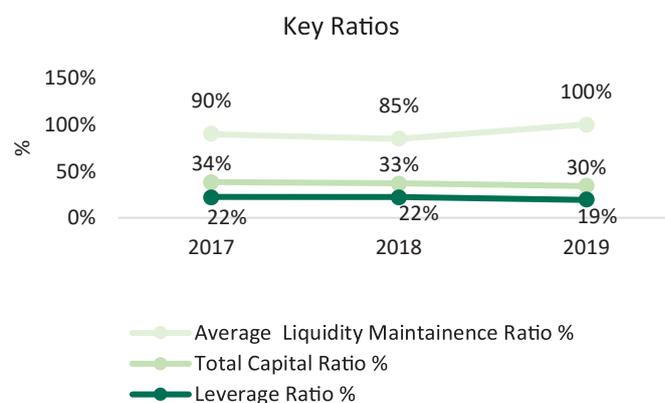
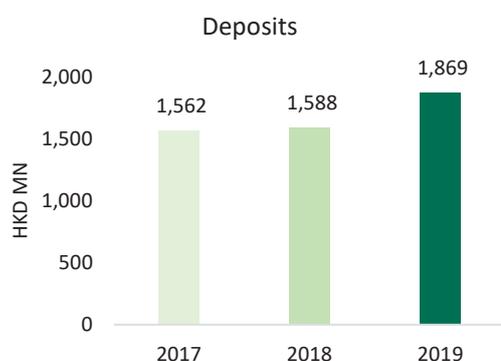
Principal place of business and principal activities

Habib Bank Zurich (Hong Kong) Limited (“the Bank”) is a restricted licence bank 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 Bank is registered as a Restricted Licence Bank under the Hong Kong Banking Ordinance. The principal activities of the Bank are the taking of deposits and financing of import/export and local trade.

Operating results

Hong Kong’s economy contracted by 1.2% for the year 2019, down from a growth of 2.9% in 2018, particularly due to the global economic slowdown, elevated US-Mainland China trade tension and civil unrest in Hong Kong. Exports of goods decreased by 4.7%, down from last year’s growth of 3.5%. Imports of goods decreased by 7.4%, down from last year’s growth of 4.7%. The labour market showed further tightening in 2019 and the unemployment rate stood at 3.0%. Consumer price inflation increased from 2.6% in 2018 to 3.0% in 2019.



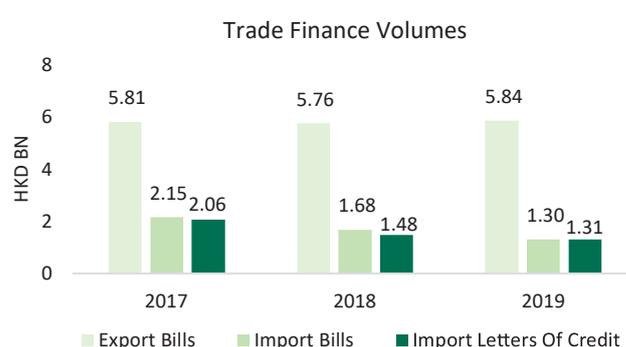
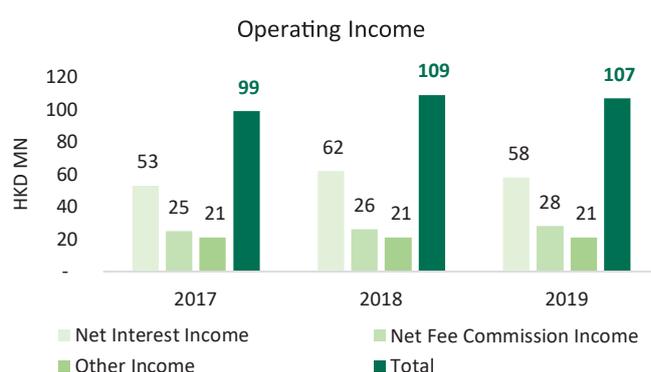
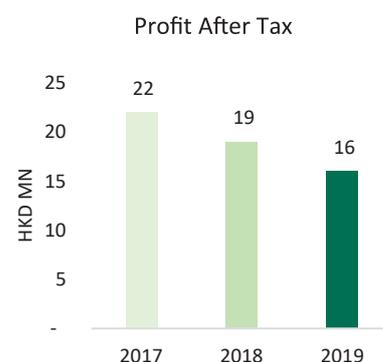
Report of the directors (continued)

Operating results (continued)

As at 31 December 2019, the Bank's capital adequacy ratio stood at 30% 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\$1.87 billion (2018: HK\$1.59 billion). Based on such balance sheet strength, the Bank prudently managed its lending portfolio. As at the year end, total advances to customers including trade bills increased by 18% to HK\$1.6 billion (2018: HK\$1.36 billion).

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 100% (2018: 85%).

During the year, export bills totalling HK\$5.84 billion (2018: HK\$5.76 billion) and import bills of HK\$1.30 billion (2018: HK\$1.68 billion) were processed. Import letters of credit for HK\$1.31 billion (2018: HK\$1.48 billion) were opened. Profit for the year was HK\$16.27 million (2018: HK\$18.93 million).



In 2020, the outlook for the Hong Kong economy is subject to high uncertainty, including the pace of global economic recovery, US-Mainland China trade relations and the possibility of continued civil unrest. Other developments such as the coronavirus infection may also have an impact on the economic environment in the short term. The economic environment in Hong Kong is therefore expected to be very challenging for the remainder of 2020. Taking all these factors into account, the Hong Kong economy which is currently in recession may contract / grow by -1.5% to 0.5% in 2020. Consumer price inflation is forecast at 2.5% for 2020.

Report of the directors (continued)

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 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 Credit Committee and the Board Audit and Compliance Committee.

The Board Risk and Credit 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. The Committee comprises of two independent non-executive directors, two non-executive directors and one executive director.

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

Report of the directors (continued)

Risk management (continued)

(ii) Specialized management committees

The Board of Directors has also established several specialized management committees and working groups, namely the Executive Committee, Risk and Credit Committee, Audit and Compliance Committee, Asset and Liability Committee, Operations and Technology Working Group and Human Resources Working Group.

The Executive Committee addresses issues of management, structure, organization, communication and implementation of current and future strategy. The Committee reviews the development and implementation of the strategy, operating and financial performance, prioritization and allocation of resources, assessment of control risk and operational plans. The Committee comprises the Chief Executive, Alternate Chief Executives, Head of Risk, Chief Financial Officer, Head of Compliance and other executives.

The Risk and Credit 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 responsible for monitoring and reviewing regulatory compliance within the institution. The 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, Head of Risk, Chief Operating Officer, Chief Financial Officer, Head of Credit Risk and other executives.

The purpose of the Audit and Compliance Committee is to review and resolve audit issues and have oversight and ensure compliance with legal and regulatory requirements. The Audit and Compliance Committee consists of the Chief Executive, Alternate Chief Executives, Head of Compliance, Head of Risk and Chief Financial Officer.

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, Head of Risk, Chief Financial Officer and other executives.

The Operations and Technology Working Group is responsible for operational risk and technology related matters such as authorization 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, Head of Risk, Chief Financial Officer, Head of Compliance and other executives.

Report of the directors (continued)

Risk management (continued)

(ii) Specialized management committees (continued)

The Human Resources Working Group is responsible for overseeing various staff management issues like capacity planning practices, succession planning, reviewing compensation and reward policies, performance management schemes, framework for staff promotion and grading, and staff training and development plan. The committee comprises the Chief Executive, Alternate Chief Executives, Head of Human Resources and other executives.

(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.

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.

Report of the directors (continued)

Risk management (continued)

(b) Market risk management (continued)

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 Treasury Department 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.

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, investments, 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 repricedable on a per-transaction basis. Hence the risk element is contained swiftly and the magnitude of the risk posed by interest rates movement is considered 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.

Report of the directors (continued)

Risk management (continued)

(c) Liquidity risk management (continued)

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.

(d) Operational risk management

Operational risk is the risk of potential loss arising from inadequate or 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. An Operations and Technology Working Group is in place to manage operational risks with oversight by the Risk and Credit Committee.

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.

Report of the directors (continued)

Risk management (continued)

(e) Capital management (continued)

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.

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 Audit and Compliance Committee to the Board of Directors.

Financial statements

The results of the Bank for the financial year ended 31 December 2019 and the state of the Bank's affairs as at that date are set out in the financial statements on pages 17 to 104.

The directors recommend the payment of a dividend of HK\$15.0 million (2018: HK\$15.0 million) in respect of the year ended 31 December 2019.

Transfer to reserves

Profit attributable to shareholders, before dividends, of HK\$16.27 million (2018: HK\$18.93 million) has been transferred to reserves. Other movements in reserves are set out on page 19 and note 24.

Habib Bank Zurich (Hong Kong) Limited

Report of the directors (continued)

Compliance with the Banking (Disclosure) Rules

The financial statements for the financial year ended 31 December 2019 comply 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\$191,000 (2018: HK\$161,000).

Directors

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

Mr Mohamedali R. Habib
Mr Rajat Garg
Mr Ikram Quraishi
Mr Paul Jeremy Brough
Mr Alex Kwong Fai Kam
Mr Sachil Dagur

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.

Report of the directors (continued)

Directors' interests in transactions, arrangements or contracts

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

Auditors

KPMG retire and, being eligible, offer themselves for reappointment. A resolution for the reappointment of KPMG as auditors of the Bank is to be proposed at the forthcoming Annual General Meeting.

By order of the Board

Mohamedali R. Habib
Chairman

Hong Kong,
13 March 2020

Habib Bank Zurich (Hong Kong) Limited

Independent auditor's report to the members of Habib Bank Zurich (Hong Kong) Limited (Incorporated in Hong Kong with limited liability)

Opinion

We have audited the financial statements of Habib Bank Zurich (Hong Kong) Limited (“the Bank”) set out on pages 17 to 104, which comprise the statement of financial position as at 31 December 2019, the statement of profit or loss and other comprehensive income, the statement of changes in equity and the cash flow statement for the year then ended and notes to the financial statements, including a summary of significant accounting policies.

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

Basis for opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing (“HKSA”) issued by the HKICPA. Our responsibilities under those standards are further described in the Auditor’s responsibilities for the audit of the financial statements section of our report. We are independent of the Bank in accordance with the HKICPA’s Code of Ethics for Professional Accountants (“the Code”) and we have fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Information other than the financial statements and auditor’s report thereon

The directors are responsible for the other information. The other information comprises all the information included in the annual report, other than the financial statements and our auditor’s report thereon.

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

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

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

***Independent auditor's report to the members of
Habib Bank Zurich (Hong Kong) Limited (continued)
(Incorporated in Hong Kong with limited liability)***

Responsibilities of the directors for the financial statements

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

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

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. 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.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSAAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

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

Habib Bank Zurich (Hong Kong) Limited

Independent auditor's report to the members of Habib Bank Zurich (Hong Kong) Limited (continued) (Incorporated in Hong Kong with limited liability)

Auditor's responsibilities for the audit of the financial statements (continued)

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

KPMG
Certified Public Accountants

8th Floor, Prince's Building
10 Chater Road
Central, Hong Kong
22 April 2020

*Statement of profit or loss and other comprehensive income
for the year ended 31 December 2019*

(Expressed in Hong Kong dollars)

	Note	2019	2018
Interest income calculated using the effective interest method	2(a)	89,234,189	84,254,514
Interest expense	2(b)	(30,961,679)	(22,446,432)
Net interest income		58,272,510	61,808,082
Fee and commission income	3	28,963,629	27,424,138
Fee and commission expense		(881,623)	(892,853)
Net fee and commission income		28,082,006	26,531,285
Other net income	4	21,039,966	20,966,364
Operating income		107,394,482	109,305,731
Operating expenses	5	(85,493,968)	(79,301,453)
		21,900,514	30,004,278
Net charge of impairment allowances	7	(2,526,136)	(7,117,610)
Profit before taxation		19,374,378	22,886,668
Income tax	8(a)	(3,103,361)	(3,961,657)
Profit for the year		16,271,017	18,925,011
Other comprehensive income			
Item that may be reclassified subsequently to profit or loss:			
Financial assets at fair value through other comprehensive income (FVOCI) - net movement in the fair value reserve	9	1,816,605	887,716
Total comprehensive income for the year		18,087,622	19,812,727

The notes on pages 22 to 104 form part of these financial statements.

Habib Bank Zurich (Hong Kong) Limited

Statement of financial position at 31 December 2019

(Expressed in Hong Kong dollars)

	Note	2019	2018
Assets			
Cash and balances with banks	10	168,651,104	207,080,565
Placements with banks	11	39,893,265	9,859,244
Investments	12	576,129,128	460,542,344
Trade bills	13(a)	765,840,917	594,596,815
Advances to customers	14(a)	830,242,082	766,025,122
Tax paid in advance	20(a)	-	2,114,221
Deferred tax assets	20(b)	495,025	3,133,341
Fixed assets	15	104,431,311	102,712,891
Other assets	16	45,068,152	22,400,472
Total assets		2,530,750,984	2,168,465,015
Liabilities			
Deposits and balances from banks	17	71,517,942	6,195,755
Deposits from customers	18	1,611,189,235	1,328,134,836
Current taxation	20(a)	1,985,144	-
Other liabilities	19	289,153,995	280,317,378
Total liabilities		1,973,846,316	1,614,647,969
Equity			
Share capital	23	300,000,000	300,000,000
Reserves		256,904,668	253,817,046
Total equity		556,904,668	553,817,046
Total equity and liabilities		2,530,750,984	2,168,465,015

The notes on pages 22 to 104 form part of these financial statements.

Approved and authorised for issue by the Board of Directors on 13 March 2020.

Sachil Dagur
Chief Executive
& Executive Director

Mohamedali R. Habib
Chairman

*Statement of changes in equity
for the year ended 31 December 2019
(Expressed in Hong Kong dollars)*

	Share capital	Property revaluation reserve	Regulatory reserve	Fair value reserve	Retained earnings	Total
At 1 January 2018, as previously reported	300,000,000	11,243,741	16,000,000	(1,182,181)	228,671,080	554,732,640
Adjustment on initial application of HKFRS 9	-	-	-	-	(5,728,321)	(5,728,321)
At 1 January 2018, as restated	300,000,000	11,243,741	16,000,000	(1,182,181)	222,942,759	549,004,319
Dividend approved and paid in respect of prior year	-	-	-	-	(15,000,000)	(15,000,000)
Profit for the year	-	-	-	-	18,925,011	18,925,011
Other comprehensive income for the year	-	-	-	887,716	-	887,716
At 31 December 2018	300,000,000	11,243,741	16,000,000	(294,465)	226,867,770	553,817,046
At 1 January 2019	300,000,000	11,243,741	16,000,000	(294,465)	226,867,770	553,817,046
Dividend approved and paid in respect of prior year	-	-	-	-	(15,000,000)	(15,000,000)
Profit for the year	-	-	-	-	16,271,017	16,271,017
Other comprehensive income for the year	-	-	-	1,816,605	-	1,816,605
At 31 December 2019	300,000,000	11,243,741	16,000,000	1,522,140	228,138,787	556,904,668

The notes on pages 22 to 104 form part of these financial statements.

Habib Bank Zurich (Hong Kong) Limited

Cash flow statement for the year ended 31 December 2019 (Expressed in Hong Kong dollars)

	2019	2018
Operating activities		
Profit before taxation	19,374,378	22,886,668
Adjustments for non-cash items:		
Depreciation	4,088,530	4,244,518
Charge for impairment losses	2,526,136	7,123,610
Advances written off net of recoveries	(1,269,636)	(17,891,437)
Loss on disposal of fixed assets	536	27,845
Gain on redemption/disposal of investment	(114,744)	(92,867)
Amortisation of bond premium	2,804,032	3,784,597
Exchange revaluation of bonds	714,948	735,808
	28,124,180	20,818,742
Decrease in placements with banks with original maturity beyond 3 months	1,632,176	106,806,406
Increase in trade bills	(172,691,925)	(5,681,853)
Increase in advances to customers	(63,724,650)	(93,929,614)
Increase/(decrease) in deposits and placements from banks	67,592,310	(3,948,976)
Increase in deposits from customers	283,054,399	90,785,226
Increase/(decrease) in other liabilities	7,819,260	(132,558,190)
(Increase)/decrease in other assets	(22,644,705)	62,234,274
Cash generated from operations	129,161,045	44,526,015
Income tax received/(paid)		
- Hong Kong profits tax received/(paid)	3,307,276	(5,721,782)
Net cash generated from operating activities	132,468,321	38,804,233

***Cash flow statement
for the year ended 31 December 2019 (continued)
(Expressed in Hong Kong dollars)***

	2019	2018
Investing activities		
Payments for purchase of fixed assets	(4,582,199)	(835,117)
Payments for purchase of investments	(337,100,388)	(201,517,977)
Proceeds from redemption of investments	212,234,658	112,818,428
Proceeds from sales of investments	7,920,650	10,047,168
Net cash used in investing activities	(121,527,279)	(79,487,498)
Financing activity		
Capital element of lease rentals paid	(207,735)	-
Interest element of lease rentals paid	(9,810)	-
Dividends paid	(15,000,000)	(15,000,000)
Net cash used in financing activity	(15,217,545)	(15,000,000)
Net decrease in cash and cash equivalents	(4,276,503)	(55,683,265)
Cash and cash equivalents at 1 January	213,111,066	268,794,331
Cash and cash equivalents at 31 December	208,834,563	213,111,066
Analysis of the balances of cash and cash equivalents		
Cash and balances with banks	168,834,563	207,151,196
Overdraft	-	(2,270,123)
Placements with banks with original maturity of three months or less	40,000,000	8,229,993
	208,834,563	213,111,066
Cash flows from operating activities include:		
Interest received	93,608,466	80,513,650
Interest paid	(29,465,553)	(20,066,783)

The notes on pages 22 to 104 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 a restricted licensed bank 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.

(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”), accounting principles generally accepted in Hong Kong and the requirements of the Hong Kong Companies Ordinance. Significant accounting policies adopted by the Bank are disclosed below.

The HKICPA has issued certain new and revised HKFRSs that are first effective or available for early adoption for the current accounting period of the Bank. Note 1(c) provides information on any changes in accounting policies resulting from initial application of these developments to the extent that they are relevant to the Bank for the current and prior accounting periods reflected in these financial statements.

(b) Basis of preparation of the financial statements

The measurement basis used in the preparation of the financial statements is the historical cost basis except for 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 major sources of estimation uncertainty are discussed in note 30.



Victoria Harbour, Hong Kong

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(c) Changes in accounting policies

The HKICPA has issued a new HKFRS, HKFRS 16, Leases, and a number of amendments to HKFRSs that are first effective for the current accounting period of the Bank.

Except for HKFRS 16, Leases, none of the developments have had a material effect on how the Bank's results and financial position for the current or prior periods have been prepared or presented. The Bank has not applied any new standard or interpretation that is not yet effective for the current accounting period.

HKFRS 16, Leases

HKFRS 16 replaces HKAS 17, Leases, and the related interpretations, HK(IFRIC) 4, Determining whether an arrangement contains a lease, HK(SIC) 15, Operating leases – incentives, and HK(SIC) 27, Evaluating the substance of transactions involving the legal form of a lease. It introduces a single accounting model for lessees, which requires a lessee to recognise a right-of-use asset and a lease liability for all leases, except for leases that have a lease term of 12 months or less (“short-term leases”) and leases of low-value assets. The lessor accounting requirements are brought forward from HKAS 17 substantially unchanged.

HKFRS 16 also introduces additional qualitative and quantitative disclosure requirements which aim to enable users of the financial statements to assess the effect that leases have on the financial position, financial performance and cash flows of an entity.

The Bank has initially applied HKFRS 16 as from 1 January 2019. The Bank has elected to use the modified retrospective approach and has therefore recognised the cumulative effect of initial application as an adjustment to the opening balance of equity at 1 January 2019. Comparative information has not been restated and continues to be reported under HKAS 17.

Further details of the nature and effect of the changes to previous accounting policies and the transition options applied are set out below:

a. New definition of a lease

The change in the definition of a lease mainly relates to the concept of control. HKFRS 16 defines a lease on the basis of whether a customer controls the use of an identified asset for a period of time, which may be determined by a defined amount of use. Control is conveyed where the customer has both the right to direct the use of the identified asset and to obtain substantially all of the economic benefits from that use.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(c) Changes in accounting policies (continued)

a. New definition of a lease (continued)

The Bank applies the new definition of a lease in HKFRS 16 only to contracts that were entered into or changed on or after 1 January 2019. For contracts entered into before 1 January 2019, the Bank has used the transitional practical expedient to grandfather the previous assessment of which existing arrangements are or contain leases. Accordingly, contracts that were previously assessed as leases under HKAS 17 continue to be accounted for as leases under HKFRS 16 and contracts previously assessed as non-lease service arrangements continue to be accounted for as executory contracts.

b. Lessee accounting and transitional impact

HKFRS 16 eliminates the requirement for a lessee to classify leases as either operating leases or finance leases, as was previously required by HKAS 17. Instead, the Bank is required to capitalise all leases when it is the lessee, including leases previously classified as operating leases under HKAS 17, other than those short-term leases and leases of low-value assets which are exempt. As far as the Bank is concerned, these newly capitalised leases are primarily in relation to office equipment as disclosed in note 15. For an explanation of how the Bank applies lessee accounting, see note 1(l).

At the date of transition to HKFRS 16 (i.e. 1 January 2019), the Bank determined the length of the remaining lease terms and measured the lease liabilities for the leases previously classified as operating leases at the present value of the remaining lease payments, discounted using the relevant incremental borrowing rates at 1 January 2019. The weighted average of the incremental borrowing rates used for determination of the present value of the remaining lease payments was 1.95%.

To ease the transition to HKFRS 16, the Bank applied the following recognition exemption and practical expedients at the date of initial application of HKFRS 16:

- (i) the Bank elected not to apply the requirements of HKFRS 16 in respect of the recognition of lease liabilities and right-of-use assets to leases for which the remaining lease term ends within 12 months from the date of initial application of HKFRS 16, i.e. where the lease term ends on or before 31 December 2019;

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(c) Changes in accounting policies (continued)

b. Lessee accounting and transitional impact (continued)

(ii) when measuring the lease liabilities at the date of initial application of HKFRS 16, the Bank applied a single discount rate to a portfolio of leases with reasonably similar characteristics (such as leases with a similar remaining lease term for a similar class of underlying asset in a similar economic environment); and

(iii) when measuring the right-of-use assets at the date of initial application of HKFRS 16, the Bank relied on the previous assessment for onerous contract provisions as at 31 December 2018 as an alternative to performing an impairment review.

The following table reconciles the operating lease commitments as disclosed in note 26(b) as at 31 December 2018 to the opening balance for lease liabilities recognised as at 1 January 2019

	1 January 2019
Operating lease commitments at 31 December 2018	608,604
Less: commitments relating to leases exempt from capitalisation:	
- short-term leases and other leases with remaining lease term ending on or before 31 December 2019	(250,004)
Less: total future interest expenses	(5,473)
Present value of remaining lease payments, discounted using the incremental borrowing rate at 1 January 2019	353,127
Add: finance lease liabilities recognised as at 31 December 2018	
Total lease liabilities recognised at 1 January 2019	353,127

The right-of-use assets in relation to leases previously classified as operating leases have been recognised at an amount equal to the amount recognised for the remaining lease liabilities, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the statement of financial position at 31 December 2018.

So far as the impact of the adoption of HKFRS 16 on leases previously classified as finance leases is concerned, the Bank is not required to make any adjustments at the date of initial application of HKFRS 16, other than changing the captions for the balances. There is no impact on the opening balance of equity.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(c) Changes in accounting policies (continued)

The following table summarises the impacts of the adoption of HKFRS 16 on the Bank's statement of financial position:

	<i>Carrying amount at 31 December 2018</i>	<i>Capitalisation of operating lease contracts</i>	<i>Carrying amount at 1 January 2019</i>
Line items in the statement of financial position impacted by the adoption of HKFRS 16:			
Fixed assets	102,712,891	353,127	103,066,018
Lease liabilities	-	353,127	353,127
Net assets	102,712,891	-	102,712,891

c. Impact on the financial result and cash flows of the Bank

After the initial recognition of right-of-use assets and lease liabilities as at 1 January 2019, the Bank as a lessee is required to recognise interest expense accrued on the outstanding balance of the lease liability, and the depreciation of the right-of-use asset, instead of the previous policy of recognising rental expenses incurred under operating leases on a straight-line basis over the lease term. This results in a positive impact on the reported profit from operations in the Bank's statement of profit or loss and other comprehensive income, as compared to the results if HKAS 17 had been applied during the year.

In the cash flow statement, the Bank as a lessee is required to split rentals paid under capitalised leases into their capital element and interest element. These elements are classified as financing cash outflows, similar to how leases previously classified as finance leases under HKAS 17 were treated, rather than as operating cash outflows, as was the case for operating leases under HKAS 17. Although total cash flows are unaffected, the adoption of HKFRS 16 therefore results in a significant change in presentation of cash flows within the cash flow statement.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(d) Revenue and other income

(i) Interest income and expense

Effective interest rate

Interest income and expense for all interest-bearing financial instruments are recognised in profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to the gross carrying amount of the financial asset or the amortised cost of the financial liability.

When calculating the effective interest rate for financial instruments, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not the expected credit losses (“ECL”).

The calculation of the effective interest rate includes transaction costs and fees and points paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or financial liability.

Amortised cost and gross carrying amount

The amortised cost of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any expected credit loss.

The gross carrying amount of a financial asset is the amortised cost of a financial asset before adjusting for any expected credit loss allowance.

Calculation of interest income and expense

The effective interest rate of a financial asset or financial liability is calculated on initial recognition of a financial asset or a financial liability. In calculating interest income and expense, the effective interest rate is applied to the gross carrying amount of the asset (when the asset is not credit-impaired) or to the amortised cost of the liability. The effective interest rate is revised as a result of periodic re-estimation of cash flows of floating rate instruments to reflect movements in market rates of interest.

However, for financial assets that have become credit-impaired subsequent to initial recognition, interest income is calculated by applying the effective interest rate to the amortised cost of the financial asset. If the asset is no longer credit-impaired, then the calculation of interest income reverts to the gross basis.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(d) Revenue and other income (continued)

Presentation

Interest income calculated using the effective interest method presented in the statement of profit or loss and other comprehensive income (“OCI”) includes interest on financial assets and financial liabilities measured at amortised cost and interest on debt instruments measured at fair value through other comprehensive income (“FVOCI”).

Interest expense presented in the statement of profit or loss includes financial liabilities measured at amortised cost.

Interest income and expense on other financial assets and financial liabilities at fair value through profit or loss (“FVTPL”) are presented in net income from other financial instruments at FVTPL.

(ii) Fee and commission income

Fee and commission income is recognized in profit or loss on an accrual basis in accordance with the terms of the relevant agreements. Other fee and commission expenses relate mainly to transaction and service fees, which are expensed as the services are received.

(iii) Net income from other financial instruments at FVTPL

Net income from other financial instruments at FVTPL relates to non-trading derivatives held for risk management purposes that do not form part of qualifying hedging relationships, financial assets and financial liabilities designated as at FVTPL and non-trading assets mandatorily measured at FVTPL. The line item includes fair value changes, interest, dividends and foreign exchange differences.

(e) Intangible assets

Intangible assets comprise a club membership acquired by the Bank which is stated in the statement of financial position at cost less impairment losses (see note 1(i)).

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.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Financial assets and financial liabilities

(i) Recognition and initial measurement

The Bank initially recognises loans and advances, deposits and debt securities issued on the date on which they are originated. All other financial instruments (including regular-way purchases and sales of financial assets) are recognised on the trade date, which is the date on which the Bank becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus, for an item not at FVTPL, transaction costs that are directly attributable to its acquisition or issue.

(ii) Classification

Financial assets

On initial recognition, a financial asset is classified as measured at: amortised cost, FVOCI or FVTPL.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- the asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest (“SPPI”).

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

- the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are SPPI.

All other financial assets are classified as measured at FVTPL.

In addition, on initial recognition, the Bank may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Financial assets and financial liabilities (continued)

Business model assessment

The Bank makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of the assets;
- how the performance of the portfolio is evaluated and reported to the Bank's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and its strategy for how those risks are managed; and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading or managed and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

Assessment of whether contractual cash flows are SPPI

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Financial assets and financial liabilities (continued)

In assessing whether the contractual cash flows are SPPI, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Bank considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Bank's claim to cash flows from specified assets (e.g. non-recourse loans); and
- features that modify consideration of the time value of money (e.g. periodical reset of interest rates).

Non-recourse loans

In some cases, loans made by the Bank that are secured by collateral of the borrower limit the Bank's claim to cash flows of the underlying collateral (non-recourse loans). The Bank applies judgment in assessing whether the non-recourse loans meet the SPPI criterion. The Bank typically considers the following information when making this judgement:

- whether the contractual arrangement specifically defines the amounts and dates of the cash payments of the loan;
- the fair value of the collateral relative to the amount of the secured financial asset;
- the ability and willingness of the borrower to make contractual payments, notwithstanding a decline in the value of collateral;
- whether the borrower is an individual or a substantive operating entity or is a special-purpose entity;
- the Bank's risk of loss on the asset relative to a full-recourse loan;
- the extent to which the collateral represents all or a substantial portion of the borrower's assets; and
- whether the Bank will benefit from any upside from the underlying assets

Reclassifications

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Bank changes its business model for managing financial assets.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Financial assets and financial liabilities (continued)

(iii) Derecognition

Financial assets

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire (see also (iv)), or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset (excluding equity investment securities), the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss.

The Bank enters into transactions whereby it transfers assets recognised on its statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. In such cases, the transferred assets are not derecognised. Examples of such transactions are securities lending and sale-and-repurchase transactions.

When assets are sold to a third party with a concurrent total rate of return swap on the transferred assets, the transaction is accounted for as a secured financing transaction similar to sale-and-repurchase transactions, because the Bank retains all or substantially all of the risks and rewards of ownership of such assets.

In transactions in which the Bank neither retains nor transfers substantially all of the risks and rewards of ownership of a financial asset and it retains control over the asset, the Bank continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

Financial liabilities

The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled, or expire.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Financial assets and financial liabilities (continued)

(iv) Modifications of financial assets and financial liabilities

Financial assets

If the terms of a financial asset are modified, then the Bank evaluates whether the cash flows of the modified asset are substantially different.

If the cash flows are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised (see (iii)) and a new financial asset is recognised at fair value plus any eligible transaction costs. Any fees received as part of the modification are accounted for as follows:

- fees that are considered in determining the fair value of the new asset and fees that represent reimbursement of eligible transaction costs are included in the initial measurement of the asset; and
- other fees are included in profit or loss as part of the gain or loss on derecognition.

If cash flows are modified when the borrower is in financial difficulties, then the objective of the modification is usually to maximise recovery of the original contractual terms rather than to originate a new asset with substantially different terms. If the Bank plans to modify a financial asset in a way that would result in forgiveness of cash flows, then it first considers whether a portion of the asset should be written off before the modification takes place. This approach impacts the result of the quantitative evaluation and means that the derecognition criteria are not usually met in such cases.

If the modification of a financial asset measured at amortised cost or FVOCI does not result in derecognition of the financial asset, then the Bank first recalculates the gross carrying amount of the financial asset using the original effective interest rate of the asset and recognises the resulting adjustment as a modification gain or loss in profit or loss. For floating-rate financial assets, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification. Any costs or fees incurred and fees received as part of the modification adjust the gross carrying amount of the modified financial asset and are amortised over the remaining term of the modified financial asset.

If such a modification is carried out because of financial difficulties of the borrower (see (vii)), then the gain or loss is presented together with impairment losses. In other cases, it is presented as interest income calculated using the effective interest rate method.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Financial assets and financial liabilities (continued)

Financial liabilities

The Bank derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different. In this case, a new financial liability based on the modified terms is recognised at fair value. The difference between the carrying amount of the financial liability derecognised and consideration paid is recognised in profit or loss. Consideration paid includes non-financial assets transferred, if any, and the assumption of liabilities, including the new modified financial liability.

If the modification of a financial liability is not accounted for as derecognition, then the amortised cost of the liability is recalculated by discounting the modified cash flows at the original effective interest rate and the resulting gain or loss is recognised in profit or loss. For floating-rate financial liabilities, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification. Any costs and fees incurred are recognised as an adjustment to the carrying amount of the liability and amortised over the remaining term of the modified financial liability by re-computing the effective interest rate on the instrument.

(v) Offsetting

Financial assets and financial liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Bank currently has a legally enforceable right to set off the amounts and it intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

(vi) Fair value measurement

‘Fair value’ is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When one is available, the Bank measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as ‘active’ if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Financial assets and financial liabilities (continued)

(vi) Fair value measurement (continued)

If there is no quoted price in an active market, then the Bank uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

The best evidence of the fair value of a financial instrument on initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the Bank determines that the fair value on initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique for which any unobservable inputs are judged to be insignificant in relation to the measurement, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value on initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

If an asset or a liability measured at fair value has a bid price and an ask price, then the Bank measures assets and long positions at average of bid and ask prices and liabilities and short positions at an ask price.

Portfolios of financial assets and financial liabilities that are exposed to market risk and credit risk that are managed by the Bank on the basis of the net exposure to either market or credit risk are measured on the basis of a price that would be received to sell a net long position (or paid to transfer a net short position) for the particular risk exposure. Portfolio-level adjustments – e.g. bid-ask adjustment or credit risk adjustments that reflect the measurement on the basis of the net exposure – are allocated to the individual assets and liabilities on the basis of the relative risk adjustment of each of the individual instruments in the portfolio.

The fair value of a financial liability with a demand feature (e.g. a demand deposit) is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

The Bank recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Financial assets and financial liabilities (continued)

(vii) Impairment

The ECL model requires an ongoing measurement of credit risk associated with a financial asset.

12-month ECL are the portion of ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date. Financial instruments for which a 12-month ECL is recognised are referred to as “Stage 1 financial instruments”.

Life-time ECL are the ECL that result from all possible default events over the expected life of the financial instrument. Financial instruments for which a lifetime ECL is recognised but which are not credit-impaired are referred to as “Stage 2 financial instruments”.

Measurement of ECL

ECL are a probability-weighted estimate of credit losses. They are measured as follows:

- financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive);
- financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows; and
- financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Bank expects to recover.

Restructured financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised (see (iv)) and ECL are measured as follows.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Financial assets and financial liabilities (continued)

(vii) Impairment (continued)

Restructured financial assets (continued)

- If the expected restructuring will not result in derecognition of the existing asset, then the expected cash flows arising from the modified financial asset are included in calculating the cash shortfalls from the existing asset.
- If the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is included in calculating the cash shortfalls from the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

Credit-impaired financial assets

At each reporting date, the Bank assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI, are credit-impaired (referred to as “Stage 3 financial instruments”). A financial asset is ‘credit-impaired’ when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred.

Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by the Bank on terms that the Bank would not consider otherwise;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for a security because of financial difficulties.

A loan that has been renegotiated due to a deterioration in the borrower’s condition is usually considered to be credit-impaired unless there is evidence that the risk of not receiving contractual cash flows has reduced significantly and there are no other indicators of impairment.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Financial assets and financial liabilities (continued)

(vii) Impairment (continued)

Credit-impaired financial assets (continued)

In making an assessment of whether an investment in sovereign debt is credit-impaired, the Bank considers the following factors.

- The market's assessment of creditworthiness as reflected in the bond yields.
- The rating agencies' assessments of creditworthiness.
- The country's ability to access the capital markets for new debt issuance.
- The probability of debt being restructured, resulting in holders suffering losses through voluntary or mandatory debt forgiveness.
- The international support mechanisms in place to provide the necessary support as 'lender of last resort' to that country, as well as the intention, reflected in public statements, of governments and agencies to use those mechanisms. This includes an assessment of the depth of those mechanisms and, irrespective of the political intent, whether there is the capacity to fulfil the required criteria.

Presentation of allowance for ECL in the statement of financial position

Loss allowances for ECL are presented in the statement of financial position as follows:

- financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
- financial guarantee contracts: generally, as a provision;
- debt instruments measured at FVOCI: no loss allowance is recognised in the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the fair value reserve.

Write-off

Loans and debt securities are written off (either partially or in full) when there is no reasonable expectation of recovering a financial asset in its entirety or a portion thereof. This is generally the case when the Bank determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. This assessment is carried out at the individual asset level.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(f) Financial assets and financial liabilities (continued)

(vii) Impairment (continued)

Write-off (continued)

Recoveries of amounts previously written off are included in ‘impairment losses on financial instruments’ in the statement of profit or loss and OCI.

Financial assets that are written off could still be subject to enforcement activities in order to comply with the Bank’s procedures for recovery of amounts due.

Non-integral financial guarantee contracts

The Bank assesses whether a financial guarantee contract held is an integral element of a financial asset that is accounted for as a component of that instrument or is a contract that is accounted for separately. The factors that the Bank considers when making this assessment include whether:

- the guarantee is implicitly part of the contractual terms of the debt instrument;
- the guarantee is required by laws and regulations that govern the contract of the debt instrument;
- the guarantee is entered into at the same time as and in contemplation of the debt instrument; and
- the guarantee is given by the parent of the borrower or another company within the borrower’s bank.

(g) Loans and receivables

Loans and receivables include loans and advances measured at amortised cost; they are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method.

(h) Investments

Investments include:

- debt investment securities measured at amortised cost; these are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method; and
- debt securities measured at FVOCI.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(h) Investments (continued)

For debt securities measured at FVOCI, gains and losses are recognised in other comprehensive income, except for the following, which are recognised in profit or loss in the same manner as for financial assets measured at amortised cost:

- interest revenue using the effective interest method;
- ECL and reversals; and
- foreign exchange gains and losses.

When debt security measured at FVOCI is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from fair value reserve to profit or loss.

(i) Impairment of non-financial assets

The carrying amounts of the Bank's non-financial assets are reviewed at the end of each reporting period 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.

Internal and external sources of information are reviewed at the end of each reporting period 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 of disposal 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 the 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).

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(i) Impairment of non-financial assets (continued)

- Recognition of impairment losses

An impairment loss is recognised in profit or loss if 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 of disposal, if measurable, or value in use, if determinable.

- 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.

(j) 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. Bank overdrafts that are repayable on demand and form an integral part of the Bank's cash management are also included as a component of cash and cash equivalents for the purpose of the cash flow statement.

Cash and cash equivalents are carried at amortised cost in the statement of financial position.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(k) Fixed assets

Fixed assets are held for own use and are stated at cost or valuation less accumulated depreciation and impairment losses (note 1(i)). 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 estimated useful lives using the straight line method as follows:

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

(l) Leased assets

At inception of a contract, the Bank assesses whether the contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. Control is conveyed where the customer has both the right to direct the use of the identified asset and to obtain substantially all of the economic benefits from that use.

(A) Policy applicable from 1 January 2019

Where the contract contains lease component(s) and non-lease component(s), the Bank has elected not to separate non-lease components and accounts for each lease component and any associated non-lease components as a single lease component for all leases.

At the lease commencement date, the Bank recognises a right-of-use asset and a lease liability, except for short-term leases that have a lease term of 12 months or less and leases of low-value assets. When the Bank enters into a lease in respect of a low-value asset, the Bank decides whether to capitalise the lease on a lease-by-lease basis. The lease payments associated with those leases which are not capitalised are recognised as an expense on a systematic basis over the lease term.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(l) Leased assets (continued)

(A) Policy applicable from 1 January 2019 (continued)

Where the lease is capitalised, the lease liability is initially recognised at the present value of the lease payments payable over the lease term, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, using a relevant incremental borrowing rate. After initial recognition, the lease liability is measured at amortised cost and interest expense is calculated using the effective interest method. Variable lease payments that do not depend on an index or rate are not included in the measurement of the lease liability and hence are charged to profit or loss in the accounting period in which they are incurred.

The right-of-use asset recognised when a lease is capitalised is initially measured at cost, which comprises the initial amount of the lease liability plus any lease payments made at or before the commencement date, and any initial direct costs incurred. Where applicable, the cost of the right-of-use assets also includes an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, discounted to their present value, less any lease incentives received. The right-of-use asset is subsequently stated at cost less accumulated depreciation and impairment losses (see notes 1(i)).

The lease liability is remeasured when there is a change in future lease payments arising from a change in an index or rate, or there is a change in the Bank's estimate of the amount expected to be payable under a residual value guarantee, or there is a change arising from the reassessment of whether the Bank will be reasonably certain to exercise a purchase, extension or termination option. When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

In the statement of financial position, the Bank presents right-of-use assets within the same line item as similar underlying assets and presents lease liabilities separately.

(B) Policy applicable prior to 1 January 2019

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

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

1 Significant accounting policies (continued)

(l) Leased assets (continued)

(B) Policy applicable prior to 1 January 2019 (continued)

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 recognized 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.

(m) 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.

(n) 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 end of reporting period, 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)

(n) 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 back or 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 end of the reporting period. Deferred tax assets and liabilities are not discounted.

The carrying amount of a deferred tax asset is reviewed at each reporting 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 profits 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)

(o) 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.

(p) Foreign currency transactions

Transactions in foreign currencies 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 end of reporting period. Exchange gains and losses are recognised in profit or loss.

Non-monetary assets and liabilities that are measured based on 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.

(q) 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)

(q) 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 the Bank 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.

(r) 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.

The Bank also operates a Mandatory Provident Fund Scheme ("the MPF scheme") under the Hong Kong Mandatory Provident Fund Schemes Ordinance for employees employed under the jurisdiction of the Hong Kong Employment Ordinance. The MPF scheme is a defined contribution retirement plan administered by independent trustees. Under the MPF scheme, the employer and its employees are each required to make contributions to the plan at 5% of the employees' relevant income, subject to a cap of monthly relevant income of HK\$30,000. Contributions to the plan vest immediately.

(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 calculated using the effective interest method and interest expense

	2019	2018
(a) Interest income calculated using the effective interest method arising from		
Trade bills and advances to customers	70,189,483	69,302,065
Placements with banks	4,933,457	2,111,495
Investments	14,111,249	12,840,954
	89,234,189	84,254,514
(b) Interest expense arising from		
Deposits from customers	28,772,093	21,111,904
Deposits and balances from banks	2,179,776	1,334,528
Financing leased assets	9,810	-
	30,961,679	22,446,432

3 Fee and commission income

	2019	2018
Fee and commission income	28,963,629	27,424,138

Fee and commission income in 2019 and 2018 mainly comprised fee and commission income from L/C bills and export bills.

4 Other net income

	2019	2018
Net gains from dealing in foreign currencies	9,808,492	9,765,603
Others	11,231,474	11,200,761
	21,039,966	20,966,364

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

5 Operating expenses

	2019	2018
(a) Staff costs		
Salaries and other benefits	52,839,838	50,235,636
Contribution to defined contribution scheme	2,634,799	2,484,595
	55,474,637	52,720,231
(b) Depreciation	4,088,530	4,244,518
(c) Other operating expenses		
Premises and equipment expenses, excluding depreciation		
- rent and rates	1,337,478	1,374,365
- repairs and maintenance	488,366	555,074
Auditor's remuneration		
- audit services	1,133,105	1,088,620
- tax services	72,000	66,000
- other services	790,095	289,210
Others	22,109,757	18,963,435
	25,930,801	22,336,704
	85,493,968	79,301,453

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

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:

	2019	2018
Directors' fees	1,200,000	800,000
Salaries, allowances and benefits in kind	3,204,000	4,542,576
Deferred compensation	615,000	490,000
Discretionary bonuses	-	528,810
Retirement scheme contributions	180,000	263,286
Total	5,199,000	6,624,672

Note 2018: The benefits in kind are in the form of provision of the Bank's residential apartment to a director.

7 Net charge of impairment allowances

	2019	2018
Trade bills and advances to customers	2,225,149	7,856,258
Cash and balances with banks	112,828	(228,143)
Placements with banks	103,810	(261,071)
Investments	107,519	43,502
Other financial assets	(22,975)	(55,239)
Loan commitments and financial guarantees issued	(195)	(237,697)
Net charge of impairment allowances	2,526,136	7,117,610

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

8 Income tax in the statement of profit or loss and other comprehensive income

(a) Taxation charged to profit or loss:

	2019	2018
Current tax - Hong Kong profits tax		
Provision for the year	1,056,898	2,422,993
Over-provision in respect of prior years	(264,809)	(67,765)
	792,089	2,355,228
Deferred tax		
Origination and reversal of temporary differences	2,311,272	1,606,429
	3,103,361	3,961,657

The provision for Hong Kong Profits Tax for 2019 is calculated at 16.5% (2018: 16.5%) of the estimated assessable profits for the year, taking into account a reduction granted by the Hong Kong SAR Government of 75% of the tax payable for the year of assessment 2018-19 subject to a maximum reduction of \$20,000 for each business (2018: a maximum reduction of \$20,000 was granted for the year of assessment 2017-18 and was taken into account in calculating the provision for 2018).

(b) Reconciliation between tax expense charged to profit or loss and accounting profit at applicable tax rates:

	2019	2018
Profit before tax	19,374,378	22,886,668
Notional tax on profit before taxation, calculated at 16.5%	3,196,772	3,776,300
Tax effect of non-deductible expenses	171,398	253,122
Over-provision in respect of prior years	(264,809)	(67,765)
Actual tax expense charged to profit or loss	3,103,361	3,961,657

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

	2019			2018		
	Before-tax amount	Tax charge (note 20(b))	Net-of-tax amount	Before-tax amount	Tax charge	Net-of-tax amount
Financial assets measured at FVOCI: net movement in FVOCI financial assets revaluation reserve	2,143,649	(327,044)	1,816,605	1,063,133	(175,417)	887,716

10 Cash and balances with banks

	2019	2018
Cash in hand	126,264	99,731
Balances with banks	168,708,299	207,051,465
Less: Impairment allowances		
-Stage 1	(183,459)	(70,631)
	168,651,104	207,080,565

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

11 Placements with banks

	2019	2018
Placements with banks	39,893,265	9,859,244
Remaining maturity		
- within one month	40,000,000	3,242,322
- between one month and three months	-	6,619,847
- between three months and one year	-	-
Less: Impairment allowances		
- Stage 1	(106,735)	(2,925)
	39,893,265	9,859,244

12 Investments

	2019		
	Debt securities at fair value through other comprehensive income	Debt securities at amortised cost	Total
Debt securities:			
- Listed in Hong Kong	122,327,312	82,957,667	205,284,979
- Listed outside Hong Kong	190,164,619	115,223,031	305,387,650
	312,491,931	198,180,698	510,672,629
- Unlisted	28,830,170	36,683,635	65,513,805
	341,322,101	234,864,333	576,186,434
Less: Impairment allowances			
- Stage 1	-	(57,306)	(57,306)
- Stage 2	-	-	-
- Stage 3	-	-	-
	-	(57,306)	(57,306)
Total debt securities	341,322,101	234,807,027	576,129,128

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

12 Investments (continued)

	2018		
	Debt securities at fair value through other comprehensive income	Debt securities at amortised cost	Total
Debt securities:			
- Listed in Hong Kong	114,837,673	81,631,052	196,468,725
- Listed outside Hong Kong	42,542,929	197,917,853	240,460,782
	157,380,602	279,548,905	436,929,507
- Unlisted	9,976,600	13,693,466	23,670,066
	167,357,202	293,242,371	460,599,573
Less: Impairment allowances			
- Stage 1	-	(57,229)	(57,229)
	-	(57,229)	(57,229)
Total debt securities	167,357,202	293,185,142	460,542,344

13 Trade bills

(a) Trade bills less impairment:

	2019	2018
Gross trade bills	771,885,670	599,193,745
Less: Impairment allowances		
- Stage 1	(1,669,325)	(570,622)
- Stage 2	(363,232)	(326,718)
- Stage 3	(4,012,196)	(3,699,590)
	765,840,917	594,596,815

(b) Impaired trade bills:

	2019	2018
Gross impaired trade bills	17,329,136	12,692,485
Less: Impairment allowances		
- Stage 3	(4,012,196)	(3,699,590)
	13,316,940	8,992,895

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

14 Advances to customers

(a) Advances to customers less impairment:

	2019	2018
Gross advances to customers	851,147,969	787,423,319
Less: Impairment allowances		
- Stage 1	(4,812,690)	(2,599,143)
- Stage 2	(4,284,595)	(13,085,222)
- Stage 3	(11,808,602)	(5,713,832)
	830,242,082	766,025,122

(b) Impaired advances to customers:

	2019	2018
Gross impaired advances to customers	18,518,537	20,703,197
Less: Impairment allowances		
- Stage 3	(11,808,602)	(5,713,832)
	6,709,935	14,989,365

Notes to the financial statements (continued)
 (Expressed in Hong Kong dollars)

15 Fixed assets

	Leasehold improvements	Buildings	Furniture, fixtures, office equipment and motor vehicles	Right-of-use leased assets	Total
Cost or valuation:					
At 31 December 2018	9,022,788	129,209,411	15,340,350	-	153,572,549
Impact on initial application of HKFRS 16 (Note)	-	-	-	353,127	353,127
At 1 January 2019	9,022,788	129,209,411	15,340,350	353,127	153,925,676
Additions	4,317,012	-	265,187	872,160	5,454,359
Disposals/written off	-	-	(347,007)	-	(347,007)
At 31 December 2019	13,339,800	129,209,411	15,258,530	1,225,287	159,033,028
Representing:					
Cost	13,339,800	114,709,411	15,258,530	1,225,287	144,533,028
Valuation	-	14,500,000	-	-	14,500,000
	13,339,800	129,209,411	15,258,530	1,225,287	159,033,028
Aggregate depreciation:					
At 1 January 2019	8,571,629	28,547,909	13,740,120	-	50,859,658
Charge for the year	411,143	2,782,142	681,522	213,723	4,088,530
Written back on disposals	-	-	(346,471)	-	(346,471)
At 31 December 2019	8,982,772	31,330,051	14,075,171	213,723	54,601,717
Net book value:					
At 31 December 2019	4,357,028	97,879,360	1,183,359	1,011,564	104,431,311

Note: The Bank has initially applied HKFRS 16 using the modified retrospective method and adjusted the opening balances at 1 January 2019 to recognise right-of-use assets relating to leases which were previously classified as operating leases under HKAS 17. See note 1(c).

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

15 Fixed assets (continued)

	Leasehold improvements	Buildings	Furniture, fixtures, office equipment and motor vehicles	Total
Cost or valuation:				
At 1 January 2018	9,022,788	129,209,411	14,796,866	153,029,065
Additions	-	-	835,117	835,117
Disposals/written off	-	-	(291,633)	(291,633)
At 31 December 2018	9,022,788	129,209,411	15,340,350	153,572,549
Representing:				
Cost	9,022,788	114,709,411	15,340,350	139,072,549
Valuation	-	14,500,000	-	14,500,000
	9,022,788	129,209,411	15,340,350	153,572,549
Aggregate depreciation:				
At 1 January 2018	7,865,317	25,765,766	13,247,845	46,878,928
Charge for the year	706,312	2,782,143	756,063	4,244,518
Written back on disposals	-	-	(263,788)	(263,788)
At 31 December 2018	8,571,629	28,547,909	13,740,120	50,859,658
Net book value:				
At 31 December 2018	451,159	100,661,502	1,600,230	102,712,891

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

	2019	2018
Customer liabilities under acceptances	16,605,087	9,811,645
Interest receivable	8,852,302	10,305,961
Others	19,620,742	2,315,820
Less: Impairment allowances		
- Stage 1	(9,979)	(13,063)
- Stage 2	-	(19,891)
	45,068,152	22,400,472

Included in other assets are intangible assets of \$225,000 (2018: \$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

	2019	2018
Banks	2,746,691	6,195,755
Parent bank - time deposit	68,771,251	-
	71,517,942	6,195,755

18 Deposits from customers

	2019	2018
Staff provident fund	55,007,406	55,298,716
Time and call deposits	1,556,181,829	1,272,836,120
	1,611,189,235	1,328,134,836

Staff provident fund represents liability to a defined contribution scheme (under the Occupational Retirement Scheme Ordinance) operated by the Bank. Subsequent to the balance sheet date, on 25 February 2020, amounts relating to the staff provident fund were transferred to an independent external scheme registered with the Mandatory Provident Fund Schemes Authority.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

19 Other liabilities

	2019	2018
Acceptances outstanding	16,605,087	9,811,645
Interest payable	8,043,342	6,608,582
Imprest accounts	240,741,510	227,224,235
Margin on L/Cs and trade bills	16,841,504	32,265,742
Interest received in advance	570,395	509,029
Lease liability	1,017,552	-
Others	5,261,981	3,825,326
Add: Impairment allowances of loan commitments and financial guarantees issued		
- Stage 1	65,852	33,442
- Stage 2	6,772	501
- Stage 3	-	38,876
	289,153,995	280,317,378

Lease Liability

	<i>31 December 2019</i>		<i>1 January 2019 (Note)</i>	
	Present value of the minimum lease payments	Total minimum lease payments	Present value of the minimum lease payments	Total minimum lease payments
Within 1 year	222,503	224,700	213,251	215,160
After 1 year but within 5 years	795,049	842,625	139,876	143,440
	1,017,552	1,067,325	353,127	358,600
Less: total future interest expenses		(49,773)		(5,473)
Present value of lease liabilities		1,017,552		353,127

Note: The Bank has initially applied HKFRS 16 using the modified retrospective approach and adjusted the opening balances at 1 January 2019 to recognise lease liabilities relating to leases which were previously classified as operating leases under HKAS 17. Comparative information as at 31 December 2018 has not been restated. Further details on the impact of the transition to HKFRS 16 are set out in note 1(c).

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

20 Income tax in the statement of financial position

(a) Current taxation in the statement of financial position represents:

	2019	2018
Provision for Hong Kong profits tax for the year	1,056,898	2,422,993
Provisional profits tax paid	(624,969)	(4,537,214)
	431,929	(2,114,221)
Balance of profits tax provision relating to prior years	1,553,215	-
	1,985,144	(2,114,221)

(b) Deferred tax assets and liabilities recognised

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

	2019					
	Differences between depreciation allowances and related depreciation	Revaluation of properties	Stage 3 ECL	Stages 1 and 2 ECL	Fair value reserve	Total
At 1 January 2019,	(768,142)	1,855,217	(1,553,215)	(2,609,013)	(58,188)	(3,133,341)
Charged to income statement	83,093	-	1,553,215	674,964	-	2,311,272
Credited to other comprehensive income	-	-	-	-	327,044	327,044
At 31 December 2019	(685,049)	1,855,217	-	(1,934,049)	268,856	(495,025)
At 1 January 2018, as previously reported	(681,976)	1,855,217	(2,996,730)	(2,036,361)	(233,605)	(4,093,455)
Adjustment on initial application of HKFRS 9 - Credited to retained earnings	-	-	-	(821,732)	-	(821,732)
At 1 January 2018, as restated	(681,976)	1,855,217	(2,996,730)	(2,858,093)	(233,605)	(4,915,187)
Charged/(credited) to income statement	(86,166)	-	1,443,515	249,080	-	1,606,429
Credited to other comprehensive income	-	-	-	-	175,417	175,417
At 31 December 2018	(768,142)	1,855,217	(1,553,215)	(2,609,013)	(58,188)	(3,133,341)

Habib Bank Zurich (Hong Kong) Limited

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

21 Material related party transactions

(a) Transactions with other related parties

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	
	2019	2018	2019	2018	2019	2018	2019	2018
Commission rebate	-	-	-	-	515,161	1,040,545	-	-
Interest income	-	-	-	-	143,525	164,486	-	-
Interest expenses	2,002,751	-	-	-	14,092	29,568	-	-
IT maintenance	4,943,808	4,429,291	-	-	-	-	-	-
Other services	3,343,945	2,289,580	-	-	-	-	-	-
Staff Provident Fund expense	-	-	-	-	2,634,799	2,484,595	-	-
Cash and balances with banks	10,445,313	1,514,020	405,123	2,398,396	5,780,856	8	-	-
Deposits and balances from banks	71,431,359	3,839,580	79,281	78,750	7,301	2,160,351	-	-
Time and call deposits	-	-	-	-	-	-	11,305,035	11,338,220
Imprest accounts	-	-	-	-	-	-	465,593	222,922
Staff Provident Fund deposit	-	-	-	-	55,007,406	55,298,715	-	-

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.

(b) Key management personnel remuneration

	2019	2018
Short-term employee benefits	12,100,849	12,187,316
Post-employment benefits	572,228	570,495
	12,673,077	12,757,811

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

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

22 Loans to directors and entities connected with directors

Loans to directors of the Bank and entities connected with directors 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:

	2019	2018
Loans made by a third party under a guarantee given by the Bank	-	-
Loans made by the Bank	-	-

23 Share capital

	2019		2018	
	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

In accordance with section 135 of the Hong Kong Companies Ordinance, the ordinary shares of the company do not have a par value.

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.

24 Reserves and dividends

(a) Nature and purpose of reserves

(i) Fair value reserve

The fair value reserve comprises the cumulative net change in the fair value of debt securities measured at fair value through other comprehensive income until the assets are derecognised or reclassified. This amount is increased by the amount of loss allowance.

(ii) Property revaluation reserve

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

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

24 Reserves and dividends (continued)

(a) Nature and purpose of reserves (continued)

(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 HKFRS 9, “Financial instruments”. 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 2019, the aggregate amount of reserves available for distribution to equity shareholders of the Bank was \$228,138,787 (2018: \$226,867,770).

(c) Dividends

	2019	2018
Final dividend in respect of the current financial year proposed after the end of reporting period of \$5 per ordinary share (2018: \$5.00 per ordinary share)	15,000,000	15,000,000

The dividend proposed after the end of reporting period has not been recognised as a liability at the end of reporting period.

	2019	2018
Final dividend in respect of the previous financial year, approved and paid during the year, of \$5 per ordinary share (2018: \$5.00 per ordinary share)	15,000,000	15,000,000

25 Assets pledged as security

The following assets have been pledged as collateral.

	2019	2018
Balances with banks	680,515	1,191,819
Investments	86,175,906	86,924,203
	86,856,421	88,116,022

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)

26 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:

	2019	2018
Trade-related contingencies	190,837,752	273,234,748
Credit risk weighted amounts	29,956,620	42,274,957

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 2018, the total future minimum lease payments in respect of IT services and properties under non-cancellable operating leases were payable as follows:

	2018(Restated)
Within 1 year	465,164
After 1 year but within 5 years	143,440
	608,604

The Bank is the lessee in respect of a number of items of plant and machinery and office equipment held under leases which were previously classified as operating leases under HKAS 17. The Bank has initially applied HKFRS 16 using the modified retrospective approach. Under this approach, the Bank adjusted the opening balances at 1 January 2019 to recognise lease liabilities relating to these leases (see note 1(c)). From 1 January 2019 onwards, future lease payments are recognised as lease liabilities in the statement of financial position in accordance with the policies set out in note 1(l), and the details regarding the Bank's future lease payments are disclosed in note 19.

27 Ultimate and immediate holding company

As at 31 December 2019, 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.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 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 is 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)

28 Financial risk management (continued)

(a) Credit risk (continued)

(A) Credit quality analysis

The following table sets out information about the credit quality of financial assets measured at amortised cost and FVOCI debt investments.

Unless specifically indicated, for financial assets, the amounts in the table represent net carrying amounts. For loan commitments and financial guarantee contracts, the amounts in the table represent the amounts committed or guaranteed, respectively.

Explanation of the terms “Stage 1”, “Stage 2” and “Stage 3” is included in Note 1(f)(vii).

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

The following table sets out information about the credit quality of trade bills and advances to customers. The amounts in the table represent net carrying amount.

	2019			
	Stage 1	Stage 2	Stage 3	Total
Trade bills at amortised cost				
Pass	733,961,694	19,699,631	-	753,661,325
Special Mention	-	895,209	-	895,209
Substandard	-	-	6,070,770	6,070,770
Doubtful	-	-	11,258,366	11,258,366
Loss	-	-	-	-
Impairment allowances	(1,669,325)	(363,232)	(4,012,196)	(6,044,753)
Carrying amount	732,292,369	20,231,608	13,316,940	765,840,917
	2018			
	Stage 1	Stage 2	Stage 3	Total
Trade bills at amortised cost				
Pass	563,933,588	5,189,590	-	569,123,178
Special Mention	-	17,378,082	-	17,378,082
Substandard	-	-	12,692,485	12,692,485
Doubtful	-	-	-	-
Loss	-	-	-	-
Impairment allowances	(570,622)	(326,718)	(3,699,590)	(4,596,930)
Carrying amount	563,362,966	22,240,954	8,992,895	594,596,815

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(A) Credit quality analysis (continued)

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

	2019			
Advances to customers at amortised cost	Stage 1	Stage 2	Stage 3	Total
Pass	788,791,896	27,014,152	-	815,806,048
Special Mention	-	16,823,384	-	16,823,384
Substandard	-	-	14,892,232	14,892,232
Doubtful	-	-	3,626,305	3,626,305
Loss	-	-	-	-
Impairment allowances	(4,812,690)	(4,284,595)	(11,808,602)	(20,905,887)
Carrying amount	783,979,206	39,552,941	6,709,935	830,242,082

	2018			
Advances to customers at amortised cost	Stage 1	Stage 2	Stage 3	Total
Pass	642,480,014	35,426,775	-	677,906,789
Special Mention	-	88,813,333	-	88,813,333
Substandard	-	-	19,837,923	19,837,923
Doubtful	-	-	865,274	865,274
Loss	-	-	-	-
Impairment allowances	(2,599,143)	(13,085,222)	(5,713,832)	(21,398,197)
Carrying amount	639,880,871	111,154,886	14,989,365	766,025,122

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk

(A) Credit quality analysis (continued)

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

2019				
Trade bills at amortised cost – gross carrying amount	Stage 1	Stage 2	Stage 3	Total
Current	715,565,728	20,494,954	4,397,904	740,458,586
Overdue < 30 days	18,395,966	99,886	309,843	18,805,695
Overdue > 30 days	-	-	12,621,389	12,621,389
Total	733,961,694	20,594,840	17,329,136	771,885,670

2018				
Trade bills at amortised cost – gross carrying amount	Stage 1	Stage 2	Stage 3	Total
Current	530,777,520	21,668,384	4,846,863	557,292,767
Overdue < 30 days	33,156,068	650,264	3,557,729	37,364,061
Overdue > 30 days	-	249,024	4,287,893	4,536,917
Total	563,933,588	22,567,672	12,692,485	599,193,745

2019				
Advances to customers at amortised cost – gross carrying amount	Stage 1	Stage 2	Stage 3	Total
Current	767,054,741	34,722,109	11,404,191	813,181,041
Overdue < 30 days	21,737,155	4,961,978	636,180	27,335,313
Overdue > 30 days	-	4,153,449	6,478,166	10,631,615
Total	788,791,896	43,837,536	18,518,537	851,147,969

2018				
Advances to customers at amortised cost – gross carrying amount	Stage 1	Stage 2	Stage 3	Total
Current	610,875,198	99,643,556	13,012,568	723,531,322
Overdue < 30 days	31,604,815	13,162,103	3,147,368	47,914,286
Overdue > 30 days	-	11,434,450	4,543,261	15,977,711
Total	642,480,013	124,240,109	20,703,197	787,423,319

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(A) Credit quality analysis (continued)

(ii) Credit quality of other financial assets

The following table sets out information about the credit quality of other financial assets. The amounts in the table represent gross carrying amount.

	2019			
Cash and balances with banks at amortised cost	Stage 1	Stage 2	Stage 3	Total
Pass	168,834,563	-	-	168,834,563
Special Mention	-	-	-	-
Substandard	-	-	-	-
Doubtful	-	-	-	-
Loss	-	-	-	-
Impairment allowances	(183,459)	-	-	(183,459)
Carrying amount	168,651,104	-	-	168,651,104
	2018			
Cash and balances with banks at amortised cost	Stage 1	Stage 2	Stage 3	Total
Pass	207,151,196	-	-	207,151,196
Special Mention	-	-	-	-
Substandard	-	-	-	-
Doubtful	-	-	-	-
Loss	-	-	-	-
Impairment allowances	(70,631)	-	-	(70,631)
Carrying amount	207,080,565	-	-	207,080,565

As at 31 December 2019, there were no overdue or impaired cash and balances with banks (2018: Nil)

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(A) Credit quality analysis (continued)

(ii) Credit quality of other financial assets (continued)

	2019			
	Stage 1	Stage 2	Stage 3	Total
Placements with banks at amortised cost				
Pass	40,000,000	-	-	40,000,000
Special Mention	-	-	-	-
Substandard	-	-	-	-
Doubtful	-	-	-	-
Loss	-	-	-	-
Impairment allowances	(106,735)	-	-	(106,735)
Carrying amount	39,893,265	-	-	39,893,265
	2018			
	Stage 1	Stage 2	Stage 3	Total
Placements with banks at amortised cost				
Pass	9,862,169	-	-	9,862,169
Special Mention	-	-	-	-
Substandard	-	-	-	-
Doubtful	-	-	-	-
Loss	-	-	-	-
Impairment allowances	(2,925)	-	-	(2,925)
Carrying amount	9,859,244	-	-	9,859,244

As at 31 December 2019, there were no overdue or impaired placements with banks (2018: Nil).

	2019			
	Stage 1	Stage 2	Stage 3	Total
Debt investments at amortised cost				
AAA	-	-	-	-
AA+ to AA-	-	-	-	-
A+ to A-	119,906,045	-	-	119,906,045
BBB+ to BBB-	114,958,288	-	-	114,958,288
Unrated	-	-	-	-
Impairment allowances	(57,306)	-	-	(57,306)
Carrying amount	234,807,027	-	-	234,807,027

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(A) Credit quality analysis (continued)

(ii) Credit quality of other financial assets (continued)

	2018			
	Stage 1	Stage 2	Stage 3	Total
Debt investments at amortised cost				
AAA	-	-	-	-
AA+ to AA-	-	-	-	-
A+ to A-	136,615,620	-	-	136,615,620
BBB+ to BBB-	156,626,751	-	-	156,626,751
Unrated	-	-	-	-
Impairment allowances	(57,229)	-	-	(57,229)
Carrying amount	293,185,142	-	-	293,185,142

	2019			
	Stage 1	Stage 2	Stage 3	Total
Debt investments at FVOCI				
AAA	-	-	-	-
AA+ to AA-	17,862,368	-	-	17,862,368
A+ to A-	120,249,828	-	-	120,249,828
BBB+ to BBB-	203,209,905	-	-	203,209,905
Unrated	-	-	-	-
Carrying amount	341,322,101	-	-	341,322,101
Impairment allowances	161,564	-	-	161,564

	2018			
	Stage 1	Stage 2	Stage 3	Total
Debt investments at FVOCI				
AAA	-	-	-	-
AA+ to AA-	17,763,051	-	-	17,763,051
A+ to A-	101,036,346	-	-	101,036,346
BBB+ to BBB-	48,557,805	-	-	48,557,805
Unrated	-	-	-	-
Carrying amount	167,357,202	-	-	167,357,202
Impairment allowances	54,122	-	-	54,122

As at 31 December 2019, there were no overdue or impaired debt investments (2018: Nil).

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(A) Credit quality analysis (continued)

(ii) Credit quality of other financial assets (continued)

Other financial assets at amortised cost	2019			Total
	Stage 1	Stage 2	Stage 3	
Pass	25,457,389	-	-	25,457,389
Special Mention	-	-	-	-
Substandard	-	-	-	-
Doubtful	-	-	-	-
Loss	-	-	-	-
Impairment allowances	(9,979)	-	-	(9,979)
Carrying amount	25,447,410	-	-	25,447,410
Other financial assets at amortised cost	2018			Total
	Stage 1	Stage 2	Stage 3	
Pass	19,447,885	669,721	-	20,117,606
Special Mention	-	-	-	-
Substandard	-	-	-	-
Doubtful	-	-	-	-
Loss	-	-	-	-
Impairment allowances	(13,063)	(19,891)	-	(32,954)
Carrying amount	19,434,822	649,830	-	20,084,652

The following table shows an analysis of counterparty credit exposures arising from derivative transactions.

In HK\$	Over-the-counter	
	Notional amount	Fair value
2019		
Derivative assets	-	-
Derivative liabilities	-	-
2018		
Derivative assets	109,613,269	-
Derivative liabilities	109,613,269	148,215

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(B) Concentration risk

Maximum exposure to credit risk before collateral held or other credit enhancement

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

	2019	2018 (Restated)
Cash and balances with banks	168,524,840	206,980,834
Placements with banks	39,893,265	9,859,244
Investments	576,129,128	460,542,344
Trade bills	765,840,917	594,596,815
Advances to customers	830,242,082	766,025,122
Other assets	45,068,152	22,400,472
	2,425,698,384	2,060,404,831

Maximum exposure to credit risk relating to items unrecorded in the statement of financial position are as follows:

	2019	2018
Direct credit substitutes	-	-
Trade-related contingencies	190,837,752	273,234,748
Commitments excluding those that are unconditionally cancellable without prior notice	-	-
	190,837,752	273,234,748

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(C) Collateral held and other credit enhancements

The Bank holds collateral and other credit enhancements against certain of its credit exposures.

Trade bills and advances to customers

The general creditworthiness of a commercial / small and medium enterprises (“SME”) customer tends to be the most relevant indicator of credit quality of a loan extended to it. However, collateral provides additional security and the Bank generally requests that the borrowers provide it. The Bank may take collateral in the form of mortgages over property and cash deposits.

The valuation of collateral is updated during the review or enhancement process. For credit-impaired loans, the Bank obtains appraisals of collateral because it provides input into determining the management credit risk actions.

At 31 December 2019, the net carrying amount of credit-impaired trade bills and advances to customers amounted to HKD 35.8 million (2018: HKD 33.4 million) and the value of identifiable collateral (mainly residential and commercial properties) held against those trade bills and advances to customers amounted to HKD 17.7 million (2018: HKD 18.4 million).

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL

Inputs, assumptions and techniques used for estimating impairment

Trade bills and advances to customers

- Default on a single facility amounts to default on all facilities belonging to the same customer, with the first default event considered as the “default date”.
- Customers with facilities that have closed during the performance period are considered to be performing unless they are tagged as “for adjustment purpose” (“FAP”) 11 – 13 or have days past due exceeding 89 days during the performance period.
- Since the “write-off date” is provided as at year end, it is assumed to be the last day of the reporting period.
- Customers with a “write-off date” are assumed to have obtained write-off status due to non-performance and are transferred to default status on “settlement date”.
- In instances where the “maturity date” exceeds the “write-off date”, the date of closure is considered to be the ‘write off date’.

Significant increase in credit risk

When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Bank considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Bank’s historical experience and expert credit assessment and including forward-looking information.

The Bank’s business model is relationship-based lending in which the customer is evaluated and monitored as a single entity. Hence, weaknesses evident in an account is considered relevant for the entire customer portfolio.

Credit risk grades

The Bank allocates each exposure to a credit risk grade based on a variety of data that is determined to be predictive of the risk of default and applying experienced credit judgement.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

It is defined using qualitative and quantitative factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower.

According to the Bank's policy, FAP tag is used for classification of facilities to monitor customer performance. The FAP tag is used to identify such accounts. FAP tag 11 to 13 are used to indicate non-performing accounts. Performance of non-performing accounts may differ significantly due to different judgmental criteria used to tag each individual account.

Each exposure is allocated to a credit risk grade on initial recognition based on available information about the borrower. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade. The monitoring typically involves use of the following data.

Commercial / SME exposures	All exposures
<ul style="list-style-type: none"> - Information obtained during periodic review of customer files – e.g. audited financial statements, management accounts, budgets and projections. - Data from credit reference agencies, press articles, changes in external credit ratings. - Actual and expected significant changes in the political, regulatory and technological environment of the borrower or in its business activities. 	<ul style="list-style-type: none"> - Payment record – this includes overdue status as well as a range of variables about payment ratios - Utilisation of the granted limit - Existing and forecast changes in business, financial and economic conditions

Generating the term structure of probability of default (“PD”)

The Bank employs statistical models to analyse the data collected and generate estimates of the remaining lifetime PD of exposures and how these are expected to change as a result of the passage of time.

Determining whether credit risk has increased significantly

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

The Bank assesses whether credit risk has increased significantly since initial recognition at each reporting date. Determining whether an increase in credit risk is significant depends on the characteristics of the financial instrument and the borrower.

As a general indicator, credit risk of a particular exposure is deemed to have increased significantly since initial recognition if, based on the Bank's quantitative modelling, the remaining lifetime PD is determined to have increased by more than a predetermined range.

The credit risk may also be deemed to have increased significantly since initial recognition based on qualitative factors linked to the Bank's credit risk management processes that may not otherwise be fully reflected in its quantitative analysis on a timely basis. Such qualitative factors are based on its expert judgment and relevant historical experiences.

As a backstop, the Bank considers that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due or, for certain types of exposure, more than 15 days past due. Days past due are determined by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received. Due dates are determined without considering any grace period that might be available to the borrower.

Definition of Default

The Bank considers a financial asset to be in default when

- The borrower is more than 90 days past due on contractual payments; or
- The borrower has been tagged as FAP 11, 12 or 13 based on observed payment delays or early warning indicators detected by the Country Credit function's portfolio monitoring activities.

While developing the model, an "ever default" definition has been employed in order to capture all accounts obtaining default status over a twelve-month period, regardless of whether the account ceases to be in default at the end of the period.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

Incorporation of forward-looking information

The economic scenarios used as at 31 December 2019 included the following key indicators for the years ending 31 December 2019 to 2023.

Year	Real GDP (National currency)	Total Investment (% of GDP)
2020	2,820.1	23.0%
2021	2,902.6	22.7%
2022	2,993.7	22.3%
2023	3,087.2	22.4%

Modified financial assets

The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be derecognised and the renegotiated loan recognised as a new loan at fair value.

When the terms of a financial asset are modified and the modification does not result in derecognition, the determination of whether the asset's credit risk has increased significantly reflects comparison of:

- its remaining lifetime probability of default ("PD") at the reporting date based on the modified terms; with
- the remaining lifetime PD estimated based on data on initial recognition and the original contractual terms.

When modification results in derecognition, a new loan is recognised and allocated to Stage 1 (assuming it is not credit-impaired at that time).

The Bank renegotiates loans to customers in financial difficulties to maximise collection opportunities and minimise the risk of default. This is granted on a selective basis if the debtor is currently in default on its debt or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms and the debtor is expected to be able to meet the revised terms.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

Modified financial assets (continued)

The revised terms usually include extending the maturity, changing the timing of interest payments and amending the terms of loan covenants. The Bank's Credit Committee regularly reviews the performance of the borrower.

For modified financial assets, the estimate of PD reflects whether the modification has improved or restored the Bank's ability to collect interest and principal and the Bank's previous experience of similar action. As part of this process, the Bank evaluates the borrower's payment performance against the modified contractual terms and considers various behavioural indicators.

Generally, this is a qualitative indicator of a significant increase in credit risk and an expectation that may constitute evidence that an exposure is credit-impaired. A customer needs to demonstrate consistently good payment behaviour over a period of time before the exposure is no longer considered to be credit-impaired or the PD is considered to have decreased such that the loss allowance reverts to being measured at an amount equal to Stage 1.

Measurement of ECL

The key inputs into the measurement of ECL are the term structure of the following variables:

- probability of default ("PD");
- loss given default ("LGD"); and
- exposure at default ("EAD").

ECL for exposures in Stage 1 is calculated by multiplying the 12-month PD by LGD and EAD. Lifetime ECL is calculated by multiplying the lifetime PD by LGD and EAD.

The methodology of estimating PDs is discussed above under the heading 'Generating the term structure of PD'.

LGD is the magnitude of the likely loss if there is a default. The Bank estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

Measurement of ECL (continued)

The LGD models consider the structure, collateral, seniority of the claim, counterparty industry and recovery costs of any collateral that is integral to the financial asset. LGD estimates are recalibrated for different economic scenarios. They are calculated on a discounted cash flow basis using the effective interest rate as the discounting factor.

EAD represents the expected exposure in the event of a default. The Bank derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract and arising from amortisation. The EAD of a financial asset is its gross carrying amount at the time of default. For lending commitments and financial guarantees, the EADs are potential future amounts that may be drawn under the contract, which are estimated based on historical observations and forward-looking forecasts.

As described above, and subject to using a maximum of a 12-month PD for Stage 1 financial assets, the Bank measures ECL considering the risk of default over the maximum contractual period (including any borrower's extension options) over which it is exposed to credit risk, even if, for credit risk management purposes, the Bank considers a longer period. The maximum contractual period extends to the date at which the Bank has the right to require repayment of an advance or terminate a loan commitment or guarantee.

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

Loss allowance reconciliation

The following tables show reconciliations from the opening to the closing balance of the loss allowance by class of financial instrument. Explanation of the terms: Stage 1 ECL, Stage 2 ECL and Stage 3 ECL are included in note 1(f)(vii).

Advances to customers	2019			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	2,599,143	13,085,222	5,713,832	21,398,197
Transfer to Stage 1 ECL	8,446,074	(8,446,074)	-	-
Transfer to Stage 2 ECL	(128,810)	128,810	-	-
Transfer to Stage 3 ECL	(187,948)	(1,474,688)	1,662,636	-
New financial assets originated	2,879,596	1,233,187	1,607,387	5,720,170
Financial assets that have been derecognised	(222,008)	(1,335,325)	(3,018,380)	(4,575,713)
Write-offs	-	-	(2,253,597)	(2,253,597)
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	(8,573,357)	1,093,463	8,096,724	616,830
Balance at 31 December	4,812,690	4,284,595	11,808,602	20,905,887

Advances to customers	2018			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	2,175,978	14,066,029	12,242,000	28,484,007
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	-	-	-	-
Transfer to Stage 3 ECL	-	-	-	-
New financial assets originated	3,915,567	12,748,896	4,546,441	21,210,904
Financial assets that have been derecognised	(3,492,402)	(13,729,703)	(11,001)	(17,233,106)
Write-offs	-	-	(11,063,608)	(11,063,608)
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	-	-	-	-
Balance at 31 December	2,599,143	13,085,222	5,713,832	21,398,197

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

Loss allowance reconciliation (continued)

Trade bills	2019			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	570,622	326,718	3,699,590	4,596,930
Transfer to Stage 1 ECL	216,732	(216,732)	-	-
Transfer to Stage 2 ECL	(12,799)	12,799	-	-
Transfer to Stage 3 ECL	(1,229)	(5,769)	6,998	-
New financial assets originated	1,669,325	363,232	157,705	2,190,262
Financial assets that have been derecognised	(773,326)	(117,016)	(371,685)	(1,262,027)
Write-offs	-	-	-	-
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	-	-	519,588	519,588
Balance at 31 December	1,669,325	363,232	4,012,196	6,044,753

Trade bills	2018			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	476,233	1,144,066	5,920,000	7,540,299
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	-	-	-	-
Transfer to Stage 3 ECL	-	-	-	-
New financial assets originated	502,040	100,939	4,607,419	5,210,398
Financial assets that have been derecognised	(407,651)	(918,287)	-	(1,325,938)
Write-offs	-	-	(6,827,829)	(6,827,829)
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	-	-	-	-
Balance at 31 December	570,622	326,718	3,699,590	4,596,930

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

Loss allowance reconciliation (continued)

	2019			
Investments measured at amortized cost	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	57,229	-	-	57,229
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	-	-	-	-
Transfer to Stage 3 ECL	-	-	-	-
New financial assets originated	25,297	-	-	25,297
Financial assets that have been derecognised	(25,503)	-	-	(25,503)
Write-offs	-	-	-	-
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	283	-	-	283
Balance at 31 December	57,306	-	-	57,306

	2018			
Investments measured at amortized cost	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	58,085	-	-	58,085
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	-	-	-	-
Transfer to Stage 3 ECL	-	-	-	-
New financial assets originated	-	-	-	-
Financial assets that have been derecognised	(856)	-	-	(856)
Write-offs	-	-	-	-
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	-	-	-	-
Balance at 31 December	57,229	-	-	57,229

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

Loss allowance reconciliation (continued)

Investments measured at FVOCI	2019			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	54,122	-	-	54,122
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	-	-	-	-
Transfer to Stage 3 ECL	-	-	-	-
New financial assets originated	94,181	-	-	94,181
Financial assets that have been derecognised	(9,578)	-	-	(9,578)
Write-offs	-	-	-	-
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	22,839	-	-	22,839
Balance at 31 December	161,564	-	-	161,564

Investments measured at FVOCI	2018			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	9,764	-	-	9,764
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	-	-	-	-
Transfer to Stage 3 ECL	-	-	-	-
New financial assets originated	44,358	-	-	44,358
Financial assets that have been derecognised	-	-	-	-
Write-offs	-	-	-	-
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	-	-	-	-
Balance at 31 December	54,122	-	-	54,122

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

Loss allowance reconciliation (continued)

Cash and balances with banks	2019			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	70,631	-	-	70,631
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	-	-	-	-
Transfer to Stage 3 ECL	-	-	-	-
New financial assets originated	2,050	-	-	2,050
Financial assets that have been derecognised	-	-	-	-
Write-offs	-	-	-	-
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	110,778	-	-	110,778
Balance at 31 December	183,459	-	-	183,459

Cash and balances with banks	2018			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	298,774	-	-	298,774
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	-	-	-	-
Transfer to Stage 3 ECL	-	-	-	-
New financial assets originated	34,808	-	-	34,808
Financial assets that have been derecognised	(262,951)	-	-	(262,951)
Write-offs	-	-	-	-
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	-	-	-	-
Balance at 31 December	70,631	-	-	70,631

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

Loss allowance reconciliation (continued)

Placements with banks	2019			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	2,925	-	-	2,925
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	-	-	-	-
Transfer to Stage 3 ECL	-	-	-	-
New financial assets originated	106,735	-	-	106,735
Financial assets that have been derecognised	(2,925)	-	-	(2,925)
Write-offs	-	-	-	-
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	-	-	-	-
Balance at 31 December	106,735	-	-	106,735

Placements with banks	2018			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	263,996	-	-	263,996
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	-	-	-	-
Transfer to Stage 3 ECL	-	-	-	-
New financial assets originated	1,753	-	-	1,753
Financial assets that have been derecognised	(262,824)	-	-	(262,824)
Write-offs	-	-	-	-
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	-	-	-	-
Balance at 31 December	2,925	-	-	2,925

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

Loss allowance reconciliation (continued)

Other financial assets	2019			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	13,063	19,891	-	32,954
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	-	-	-	-
Transfer to Stage 3 ECL	-	-	-	-
New financial assets originated	9,979	-	-	9,979
Financial assets that have been derecognised	(13,063)	(19,891)	-	(32,954)
Write-offs	-	-	-	-
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	-	-	-	-
Balance at 31 December	9,979	-	-	9,979

Other financial assets	2018			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	56,014	32,179	-	88,193
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	-	-	-	-
Transfer to Stage 3 ECL	-	-	-	-
New financial assets originated	48,319	-	-	48,319
Financial assets that have been derecognised	(91,270)	(12,288)	-	(103,558)
Write-offs	-	-	-	-
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	-	-	-	-
Balance at 31 December	13,063	19,891	-	32,954

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

Loss allowance reconciliation (continued)

Loan commitments and financial guarantees issued	2019			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	33,442	501	38,876	72,819
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	(528)	528	-	-
Transfer to Stage 3 ECL	(110)	-	110	-
New financial assets originated	65,752	6,772	-	72,524
Financial assets that have been derecognised	(31,679)	(1,029)	(38,986)	(71,694)
Write-offs	-	-	-	-
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	(1,025)	-	-	(1,025)
Balance at 31 December	65,852	6,772	-	72,624

Loan commitments and financial guarantees issued	2018			
	Stage 1 ECL	Stage 2 ECL	Stage 3 ECL	Total
Balance at 1 January	49,969	260,547	-	310,516
Transfer to Stage 1 ECL	-	-	-	-
Transfer to Stage 2 ECL	-	-	-	-
Transfer to Stage 3 ECL	-	-	-	-
New financial assets originated	69,887	501	38,876	109,264
Financial assets that have been derecognised	(86,414)	(260,547)	-	(346,961)
Write-offs	-	-	-	-
Changes in models	-	-	-	-
Foreign exchange	-	-	-	-
Net remeasurement of loss allowance	-	-	-	-
Balance at 31 December	33,442	501	38,876	72,819

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(a) Credit risk (continued)

(D) Amounts arising from ECL (continued)

Loss allowance reconciliation (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 statement of financial position.

	Note	2019			2018		
		Gross amounts of financial instruments in the statement of financial position '000	Related financial instruments that have not been offset in the statement of financial position '000	Net amount '000	Gross amounts of financial instruments in the statement of financial position '000	Related financial instruments that have not been offset in the statement of financial position '000	Net amount '000
Financial assets							
Trade bills	13(a)	771,886	125,054	646,832	599,194	96,655	502,539
Advances to customers	14(a)	851,148	213,357	637,791	787,423	159,556	627,867
		1,623,034	338,411	1,284,623	1,386,617	256,211	1,130,406
Financial liabilities							
Deposit from customers	18	1,611,189	272,902	1,338,287	1,328,135	206,347	1,121,788
Imprest and margin accounts	19	257,583	65,509	192,074	259,490	49,864	209,626
		1,868,772	338,411	1,530,361	1,587,625	256,211	1,331,414

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 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 Treasury Department 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)

28 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:

	2019			2018		
	Total	United States Dollars	Other foreign currencies	Total	United States Dollars	Other foreign currencies
In thousands of HKD equivalents						
Assets						
Cash and balances with banks	107,683	60,406	47,277	102,986	85,235	17,751
Placements with banks	-	-	-	9,862	-	9,862
Investments	448,190	448,190	-	384,670	384,670	-
Trade bills	771,885	766,635	5,250	599,194	595,019	4,175
Advances to customers	464,795	457,313	7,482	463,126	440,368	22,758
Other assets	17,401	17,401	-	9,812	9,812	-
Spot assets	1,809,954	1,749,945	60,009	1,569,650	1,515,104	54,546
Liabilities						
Deposits and balances of banks	(70,963)	(70,963)	-	(5,690)	(5,573)	(117)
Deposits from customers	(1,465,322)	(1,430,706)	(34,616)	(1,196,084)	(1,164,177)	(31,907)
Other liabilities	(260,840)	(235,915)	(24,925)	(253,735)	(233,518)	(20,217)
Spot liabilities	(1,797,125)	(1,737,584)	(59,541)	(1,455,509)	(1,403,268)	(52,241)
Forward purchases	-	-	-	1,795	1,653	142
Forward sales	-	-	-	(109,472)	(107,819)	(1,653)
	-	-	-	(107,677)	(106,166)	(1,511)
Net non-structural position	12,829	12,361	468	6,464	5,670	794

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 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 (98%) of the Bank's financial instruments at 31 December 2019 and 2018 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 statement of financial position. 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 repriced 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)

28 Financial risk management (continued)

(b) Market risk management (continued)

(ii) Interest rate risk (continued)

Interest sensitivity of assets and liabilities	Effective interest rate	Total	2019				Non-interest bearing
			3 months or less	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	
In thousands of HKD equivalents							
Assets							
Cash and balances with banks	-	168,651	-	-	-	-	168,651
Placements with banks	2.91%	39,893	40,000	-	-	-	(107)
Investments	3.01%	576,129	40,646	176,549	358,991	-	(57)
Trade bills	5.03%	765,841	602,299	169,587	-	-	(6,045)
Advances to customers	5.11%	830,242	607,382	90,212	144,904	8,650	(20,906)
Tax paid in advance	-	-	-	-	-	-	-
Deferred tax assets	-	495	-	-	-	-	495
Fixed assets	-	104,431	-	-	-	-	104,431
Other assets	-	45,069	-	-	-	-	45,069
Total assets		2,530,751	1,290,327	436,348	503,895	8,650	291,531
Liabilities							
Deposits and balances of banks	2.38%	71,518	62,931	5,840	-	-	2,747
Deposits from customers	2.10%	1,611,189	1,284,033	321,695	5,461	-	-
Current taxation	-	1,985	-	-	-	-	1,985
Other liabilities	-	289,154	-	-	-	-	289,154
Total liabilities		1,973,846	1,346,964	327,535	5,461	-	293,886
Net Re-Pricing gap		556,905	(56,637)	108,813	498,434	8,650	(2,355)

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(b) Market risk management (continued)

(ii) Interest rate risk (continued)

Interest sensitivity of assets and liabilities	Effective interest rate	2018					
		Total	3 months or less	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	Non-interest bearing
In thousands of HKD equivalents							
Assets							
Cash and balances with banks	-	207,081	-	-	-	-	207,081
Placements with banks	2.03%	9,859	9,862	-	-	-	(3)
Investments	2.84%	460,543	34,482	152,691	273,427	-	(57)
Trade bills	5.36%	594,597	518,063	81,131	-	-	(4,597)
Advances to customers	5.12%	766,025	553,875	91,752	141,796	-	(21,398)
Tax paid in advance	-	2,114	-	-	-	-	2,114
Deferred tax assets	-	3,133	-	-	-	-	3,133
Fixed assets	-	102,713	-	-	-	-	102,713
Other assets	-	22,400	-	-	-	-	22,400
Total assets		2,168,465	1,116,282	325,574	415,223	-	311,386
Liabilities							
Deposits and balances of banks	-	6,196	-	-	-	-	6,196
Deposits from customers	1.67%	1,328,135	875,960	437,725	14,450	-	-
Current taxation	-	-	-	-	-	-	-
Other liabilities	-	280,317	-	-	-	-	280,317
Total liabilities		1,614,648	875,960	437,725	14,450	-	286,513
Net Re-Pricing gap		553,817	240,322	(112,151)	400,773	-	24,873

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(b) Market risk management (continued)

(ii) Interest rate risk (continued)

At 31 December 2019, it is estimated that a general increase/decrease of 50 basis points in interest rates (2018: 50 basis points in interest rates), with all other variables held constant, would not significantly impact the Bank's profit after taxation (2018: not significant impact).

The sensitivity analysis above has been determined assuming that the change in interest rate had occurred at end of the reporting period 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 reporting date.

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(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 2019 of 100.29% (2018: liquidity maintenance ratio of 85.29%) 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)

28 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 end of reporting period to the contractual maturity date.

In thousands of HKD equivalents	2019							
	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
Assets								
Cash and balances with banks	168,651	168,651	-	-	-	-	-	-
Placements with banks	39,893	-	39,893	-	-	-	-	-
Investments	576,129	-	4,004	36,638	176,532	358,942	-	13
Trade bills	765,841	47,422	248,342	300,958	169,119	-	-	-
Advances to customers	830,242	27,383	178,124	383,696	89,203	143,283	8,553	-
Tax paid in advance	-	-	-	-	-	-	-	-
Deferred tax assets	495	-	-	-	-	-	-	495
Fixed assets	104,431	-	-	-	-	-	-	104,431
Other assets	45,069	19,622	14,577	10,698	172	-	-	-
Total assets	2,530,751	263,078	484,940	731,990	435,026	502,225	8,553	104,939
Liabilities								
Deposits and balances of banks	71,518	2,747	32,704	30,227	5,840	-	-	-
Deposits from customers	1,611,189	298,329	352,969	632,735	321,695	5,461	-	-
Current taxation	1,985	-	-	-	1,985	-	-	-
Other liabilities	289,154	263,489	13,771	10,704	173	1,017	-	-
Total liabilities	1,973,846	564,565	399,444	673,666	329,693	6,478	-	-
Net liability gap	556,905	(301,487)	85,496	58,324	105,333	495,747	8,553	104,939

Notes to the financial statements (continued)
 (Expressed in Hong Kong dollars)

28 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 end of reporting period to the contractual maturity date.

In thousands of HKD equivalents	2018							
	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
Assets								
Cash and balances with banks	207,081	207,081	-	-	-	-	-	-
Placements with banks	9,859	-	3,241	6,618	-	-	-	-
Investments	460,543	-	15,668	18,810	152,672	273,393	-	-
Trade bills	594,597	50,726	167,349	295,512	81,010	-	-	-
Advances to customers	766,025	62,353	144,494	330,282	89,924	138,972	-	-
Tax paid in advance	2,114	-	-	-	-	-	-	2,114
Deferred tax assets	3,133	-	-	-	-	-	-	3,133
Fixed assets	102,713	-	-	-	-	-	-	102,713
Other assets	22,400	2,315	15,130	4,955	-	-	-	-
Total assets	2,168,465	322,475	345,882	656,177	323,606	412,365	-	107,960
Liabilities								
Deposits and balances of banks	6,196	6,196	-	-	-	-	-	-
Deposits from customers	1,328,135	5,555	425,369	445,036	437,725	14,450	-	-
Current taxation	-	-	-	-	-	-	-	-
Other liabilities	280,317	263,387	11,972	4,958	-	-	-	-
Total liabilities	1,614,648	275,138	437,341	449,994	437,725	14,450	-	-
Net liability gap	553,817	47,337	(91,459)	206,183	(114,119)	397,915	-	107,960

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

28 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:

2019								
	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
In thousands of HKD equivalents								
Deposits and balances of banks	71,518	71,927	2,747	32,884	30,394	5,902	-	-
Deposits from customers	1,611,189	1,624,032	298,337	356,197	637,553	326,454	5,491	-
	1,682,707	1,695,959	301,084	389,081	667,947	332,356	5,491	-
2018								
	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
In thousands of HKD equivalents								
Deposits and balances of banks	6,196	6,196	6,196	-	-	-	-	-
Deposits from customers	1,328,135	1,340,579	5,570	426,737	449,907	458,365	-	-
	1,334,331	1,346,775	11,766	426,737	449,907	458,365	-	-

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

28 Financial risk management (continued)

(d) Operational risk

Operational risk is the risk of potential loss arising from inadequate or 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 Credit 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.

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 2019 and 2018 and is well above the minimum required ratio set by the HKMA

Notes to the financial statements (continued)

(Expressed in Hong Kong dollars)

29 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 - Unadjusted quoted prices in active markets for identical instruments at the measurement date.
- 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.

(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:

	2019			
	Level 1	Level 2	Level 3	Total
Assets				
Financial assets at fair value through other comprehensive income				
- Debt securities	-	341,322,101	-	341,322,101
Derivative financial instruments:				
- Forward exchange contracts	-	-	-	-
	-	341,322,101	-	341,322,101
Liabilities				
Derivative financial instruments:				
- Forward exchange contracts	-	-	-	-

Notes to the financial statements (continued)
(Expressed in Hong Kong dollars)

29 Fair values of financial instruments (continued)

(b) Fair value (continued)

	2018			Total
	Level 1	Level 2	Level 3	
Assets				
Financial assets at fair value through other comprehensive income				
- Debt securities	-	167,357,202	-	167,357,202
Derivative financial instruments:				
- Forward exchange contracts	-	48,605	-	48,605
	-	167,405,807	-	167,405,807
Liabilities				
Derivative financial instruments:				
- Forward exchange contracts	-	196,820	-	196,820

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

30 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)

31 Possible impact of amendments, new standards and interpretations issued but not yet effective for the year ended 31 December 2019

Up to the date of issue of these financial statements, the HKICPA has issued a number of amendments, which are not yet effective for the year ended 31 December 2019 and which have not been adopted in these financial statements. These include the following which may be relevant to the company.

	Effective for accounting periods beginning on or after
Amendments to HKFRS 3, Definition of a business	1 January 2020
Amendments to HKAS 1 and HKAS 8, Definition of material	1 January 2020

The company is in the process of making an assessment of what the impact of these developments 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 financial statements.



Tsing Ma Bridge, Tsing Yi

Unaudited supplementary financial information
(Expressed in Hong Kong dollars)

(a) Capital and capital adequacy

	2019	2018
Capital ratio:		
Common Equity Tier 1 (“CET1”) Capital Ratio	28.56%	31.07%
Tier 1 Capital Ratio	28.56%	31.07%
Total Capital Ratio	29.96%	32.50%

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

	2019	2018
	’000	’000
CET1 Capital:		
CET1 Capital instruments	300,000	300,000
Retained earnings	228,139	226,867
Disclosed reserves	28,605	26,950
CET1 Capital before deductions	556,744	553,817
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	(495)	(3,133)
Total CET1 Capital	529,005	523,440
Additional Tier 1 (“AT1”) Capital	-	-
Total Tier 1 (“T1”) Capital	529,005	523,440
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	20,832	18,953
Regulatory deductions to T2 capital	-	-
Total T2 Capital	25,892	24,013
Total Capital	554,897	547,453

Unaudited supplementary financial information (continued)
(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 (2018: 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 (2018: \$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.

Unaudited supplementary financial information (continued)
(Expressed in Hong Kong dollars)

(a) Capital and capital adequacy (continued)

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 CET1 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 CET1 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.

(b) Leverage Ratio

	2019	2018
Leverage Ratio	19.45%	22.07%
	2019	2018
	’000	’000
Tier 1 Capital	529,005	523,440
Exposure Measure	2,720,053	2,372,016

The leverage ratio as at 31 December 2019 and 31 December 2018 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.

Unaudited supplementary financial information (continued)
(Expressed in Hong Kong dollars)

(c) Countercyclical Capital Buffer Ratio

	2019	2018
Countercyclical Capital Buffer Ratio	1.647%	1.639%

The relevant disclosures pursuant to section 24B of the Banking (Disclosure) Rules for 2019 are available in the section of Regulatory Disclosures of our website www.hbzhongkong.com

(d) Capital Conservation Buffer Ratio

Under section 3M of the Capital Rules, the capital conservation buffer ratios for calculating the Bank's buffer level are 2.5% for 2019 and 1.875% for 2018.

(e) Liquidity information

	2019	2018
Average liquidity maintenance ratio for the year	100.29%	85.29%

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.

Unaudited supplementary financial information (continued)
(Expressed in Hong Kong dollars)

(f) 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:

	2019			2018		
	Trade finance and deposits taking	Treasury and others	Total	Trade finance and deposits taking	Treasury and others	Total
Interest income calculated using the effective interest method	70,189,483	19,044,706	89,234,189	69,302,065	14,952,449	84,254,514
Interest expense	(28,772,093)	(2,179,776)	(30,951,869)	(21,111,903)	(1,334,529)	(22,446,432)
Net interest income	41,417,390	16,864,930	58,282,320	48,190,162	13,617,920	61,808,082
Fee and commission income	28,963,629	-	28,963,629	27,424,138	-	27,424,138
Fee and commission expense	(881,623)	-	(881,623)	(892,853)	-	(892,853)
Net fee and commission income	28,082,006	-	28,082,006	26,531,285	-	26,531,285
Other net income	20,554,695	485,271	21,039,966	20,719,445	246,919	20,966,364
Operating income	90,054,091	17,350,201	107,404,292	95,440,892	13,864,839	109,305,731
Operating expenses	(71,691,409)	(13,812,369)	(85,503,778)	(69,242,493)	(10,058,960)	(79,301,453)
Operating profit before provisions	18,362,682	3,537,832	21,900,514	26,198,399	3,805,879	30,004,278
Net charge of impairment allowances	(2,526,136)	-	(2,526,136)	(7,117,610)	-	(7,117,610)
Operating profit after provisions	15,836,546	3,537,832	19,374,378	19,080,789	3,805,879	22,886,668
Profit before taxation	15,836,546	3,537,832	19,374,378	19,080,789	3,805,879	22,886,668
Capital expenditure	-	5,650,813	5,650,813	-	835,117	835,117
Depreciation	3,428,065	660,465	4,088,530	(3,706,124)	(538,394)	(4,244,518)
Segment assets	1,612,688,086	917,744,661	2,530,432,747	1,370,433,582	798,031,433	2,168,465,015
Total assets	1,612,688,086	917,744,661	2,530,432,747	1,370,433,582	798,031,433	2,168,465,015
Segment liabilities	1,885,377,336	88,312,312	1,973,689,648	1,597,436,457	17,211,512	1,614,647,969
Total liabilities	1,885,377,336	88,312,312	1,973,689,648	1,597,436,457	17,211,512	1,614,647,969

Unaudited supplementary financial information (continued)
(Expressed in Hong Kong dollars)

(f) 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.

Unaudited supplementary financial information (continued)

(Expressed in Hong Kong dollars)

(g) 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:

2019								
	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	5,240	100%	-	-	-	-	-	-
Trade finance	845,908	38.2%	37,967	19,374	4,360	9,097	(5,754)	2,254

2018								
	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	3,390	100%	-	-	-	-	-	-
Trade finance	784,033	33.3%	63,892	20,703	5,714	15,684	3,978	11,064

Unaudited supplementary financial information (continued)
(Expressed in Hong Kong dollars)

(g) Advances to customers (continued)

(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, or if the claims are on an overseas branch of a bank whose head office is located in another country.

	2019	2018
Gross advances to customers		
Hong Kong	827,724,822	760,261,758
Asia Pacific excluding Hong Kong	-	302,857
Africa, Caribbean, Latin America and North America	23,423,147	26,817,635
Europe	-	-
	851,147,969	787,382,250

All impaired advances to customers at 31 December 2019 and 2018 are located in Hong Kong.

Unaudited supplementary financial information (continued)

(Expressed in Hong Kong dollars)

(h) Overdue and rescheduled assets

The gross amount of overdue assets are as follows:

	2019							
	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	1,711,544	-	0.20%	780,000	486,933	-	0.06%	201,000
-1 year or less but over 6 months	80,669	1,626	0.01%	-	4,645,377	-	0.60%	4,645,377
-Over 1 year	3,276,843	-	0.38%	2,805,583	6,607,497	-	0.86%	6,607,497
	5,069,056	1,626	0.59%	3,585,583	11,739,807	-	1.52%	11,453,874

	2018							
	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	837,440	-	-	837,440	-	-	-	-
-1 year or less but over 6 months	-	-	-	-	-	-	-	-
-Over 1 year	-	-	-	-	-	-	-	-
	837,440	-	-	837,440	-	-	-	-

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

Unaudited supplementary financial information (continued)
 (Expressed in Hong Kong dollars)

(i) 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 Mainland Activities.

2019	On-balance sheet exposure	Off-balance sheet exposure	Total
	'000	'000	'000
1. Central government, central government-owned entities and their subsidiaries and joint ventures (JVs)	59,241	-	59,241
2. Local governments, local government-owned entities and their subsidiaries and JVs	65,896	-	65,896
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	170,132	46,386	216,518
7. Other counterparties where the exposures are considered by the reporting institution to be non-bank Mainland China exposures	73,218	-	73,218
	368,487	46,386	414,873
Total assets after provision	2,513,755		
On-balance sheet exposures as percentage of total assets	14.66%		
2018	On-balance sheet exposure	Off-balance sheet exposure	Total
	'000	'000	'000
1. Central government, central government-owned entities and their subsidiaries and joint ventures (JVs)	49,118	-	49,118
2. Local governments, local government-owned entities and their subsidiaries and JVs	61,048	-	61,048
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	187,964	87,433	275,397
7. Other counterparties where the exposures are considered by the reporting institution to be non-bank Mainland China exposures	68,723	6,092	74,815
	366,853	\$93,525	460,378
Total assets after provision	2,156,188		
On-balance sheet exposures as percentage of total assets	17.01%		

Unaudited supplementary financial information (continued)
(Expressed in Hong Kong dollars)

(j) International claims

The country risk exposures are prepared according to the location and types of the counterparties as defined by the Hong Kong Monetary Authority under the Banking (Disclosure) Rules with reference to the Hong Kong Monetary Authority'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.

	<i>Non-bank private sector</i>				Total
	Banks	Official sector	Non-bank financial institutions	Non-financial private sector	
HK\$ million equivalent					
As at 31 December 2019					
Developed countries	55	-	-	89	144
Offshore centres	71	-	-	558	629
of which Hong Kong	64	-	-	473	537
Developing Europe	6	-	-	53	59
Developing Latin America and Caribbean	17	-	-	28	45
Developing Africa and Middle East	39	-	-	91	130
Developing Asia and Pacific	534	-	-	294	828
Total	722	-	-	1,113	1,835

Unaudited supplementary financial information (continued)
(Expressed in Hong Kong dollars)

(j) International claims (continued)

	<i>Non-bank private sector</i>				Total
	Banks	Official sector	Non-bank financial institutions	Non-financial private sector	
HK\$ million equivalent					
As at 31 December 2018					
Developed countries	26	-	-	75	101
Offshore centres	77	-	-	541	618
of which Hong Kong	75	-	-	503	578
Developing Europe	3	-	-	51	54
Developing Latin America and Caribbean	21	-	-	49	70
Developing Africa and Middle East	41	-	-	93	134
Developing Asia and Pacific	333	-	-	285	618
Total	501	-	-	1,094	1,595

Unaudited supplementary financial information (continued)
(Expressed in Hong Kong dollars)

(k) 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 and a Mandatory Provident Fund Scheme under the Mandatory Provident Fund Scheme Ordinance are also in place.

The senior management comprises of the Chief Executive and two Alternate Chief Executives (2018: including Chief Executive Designate) 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:

	2019		2018	
	Senior Management	Key Personnel	Senior Management	Key Personnel
Fixed Remuneration				
- Cash based	7,545,652	2,740,197	9,146,733	1,617,250
- Retirement scheme contributions	414,499	157,729	486,388	84,107
- Benefit in kind	-	-	300,000	-
- Deferred compensation	615,000	-	490,000	-

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

Unaudited supplementary financial information (continued)
(Expressed in Hong Kong dollars)

(l) Specific disclosures and additional quarterly disclosures

The specific disclosures and additional quarterly disclosures to be made by authorized institutions incorporated in Hong Kong respectively required by Part 2A and 2B of the Banking (Disclosure) Rules are available in the section of Regulatory Disclosures of our website www.hbzhongkong.com.

(m) Classes of exposure

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

	2019	2018
	'000	'000
Sovereign	161	157
Bank	17,229	11,013
Corporate	103,318	98,308
Other exposures which are not past due	9,951	8,860
Past due	2,017	100
Total capital requirements for on-balance sheet exposures	132,676	118,438
Trade-related contingencies	2,662	3,539
Exchange rate contracts	-	18
Total capital requirements for off-balance sheet exposures	2,662	3,557
	135,338	121,995

(n) Capital charge

The capital charge for operational risk calculated in accordance with the basic indicator approach at the end of the reporting period is:

	2019	2018
	'000	'000
Capital charge for operational risk	15,900	15,084

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Services we offer

We offer a wide range of financial services for Trade related activities. Our growth and successful operations are singularly fueled by our commitment to provide efficient services and rapid response to our customers' need. 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 - both Call and Term
- Foreign Exchange Transactions
- 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
- Financial Institution Loans