



Standard Chartered Bank
(Hong Kong) Limited

Directors' Report and
Consolidated Financial
Statements

For the year ended 31 December 2007

Standard Chartered Bank (Hong Kong) Limited
Contents

	<i>Page</i>
<i>Report of the directors</i>	1
<i>Auditors' report</i>	4
<i>Consolidated income statement</i>	5
<i>Consolidated balance sheet</i>	6
<i>Balance sheet</i>	7
<i>Consolidated statement of recognised income and expense</i>	8
<i>Consolidated cash flow statement</i>	9
<i>Notes to the financial statements</i>	11
<i>Unaudited supplementary financial information</i>	84

Report of the directors

The directors have pleasure in submitting their annual report together with the audited financial statements for the year ended 31 December 2007.

Principal place of business

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

Principal activities

The Bank is a licensed bank registered under the Hong Kong Banking Ordinance. The Bank's principal activities are the provision of banking and related financial services. The principal activities and other particulars of the Bank's subsidiaries are set out in note 17 to the financial statements.

Financial statements

The profit of the Bank and its subsidiaries for the year ended 31 December 2007 and the state of the Bank's and its subsidiaries' affairs as at that date are set out in the financial statements on pages 5 to 83.

During the year ended 31 December 2007, the directors had declared and paid a special dividend of HK\$0.61 (2006: HK\$ Nil) per 'A' ordinary share and 'B' ordinary share totalling HK\$1,181 million. Subsequent to 31 December 2007, the directors have further declared and paid a special dividend of HK\$0.60 per each 'A' and 'B' ordinary share, totalling HK\$1,162 million.

Other movements in reserves are set out in note 32 to the financial statements.

Charitable donations

Charitable donations made by the Bank and its subsidiaries during the year amounted to HK\$13 million (2006: HK\$15 million).

Fixed assets

Details of the movements in the fixed assets are set out in note 19 to the financial statements.

Share capital

Details of the movements in the share capital of the Bank during the year are set out in note 31 to the financial statements.

Directors

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

Executive directors

Benjamin Hung Pi Cheng (appointed on 1 January 2008)

Julian Fong Loong Choon

Peter David Sullivan (retired on 31 December 2007)

Non-executive directors

Chow Chung Kong*, Chairman

Jaspal Singh Bindra (appointed on 13 February 2008)

Nicholas Robert Sallnow-Smith (appointed on 8 October 2007)

Kaikhushru Shiavax Nargolwala (resigned on 6 September 2007)

Michael Bernard DeNoma

Raymond Kwok Ping Luen*

Edgar Cheng Wai Kin* (retired on 28 June 2007)

Ma Xuezheng*

Norman Lyle*

Chan Wing Kin* (appointed on 24 July 2007)

** Independent non-executive directors*

Mr Jaspal Singh Bindra, Mr Nicholas Robert Sallnow-Smith, Mr Benjamin Hung Pi Cheng and Mr Chan Wing Kin will retire in accordance with Article 109 of the Bank's Articles of Association at the forthcoming annual general meeting and being eligible, offer themselves for re-election.

Directors' service contracts

The independent non-executive directors were appointed by the board of directors for a term of 3 years. Their remuneration is determined by the shareholders at the general meeting.

Directors' interests in Share Option Schemes

Certain directors of the Bank have been granted options under various share option schemes of Standard Chartered PLC, the ultimate holding company of the Bank. During the year, Benjamin Hung Pi Cheng, Peter David Sullivan, Julian Fong Loong Choon, Nicholas Robert Sallnow-Smith, Kaikhushru Shiavax Nargolwala and Michael Bernard DeNoma were granted options under these schemes.

Directors' rights to acquire shares

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

Directors' interests in contracts

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

Auditors

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

On behalf of the Board

A handwritten signature in black ink, appearing to read "C K Chow". The signature is written in a cursive, slightly stylized font.

Sir C K Chow
Chairman

Hong Kong, 11 April 2008

Auditors' report to the shareholders of Standard Chartered Bank (Hong Kong) Limited

(Incorporated in Hong Kong SAR with limited liability)

We have audited the consolidated financial statements of Standard Chartered Bank (Hong Kong) Limited (the "Bank") set out on pages 5 to 83, which comprise the consolidated and the Bank balance sheets as at 31 December 2007, and the consolidated income statement, the consolidated statement of recognised income and expenses and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility for the financial statements

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

Auditors' responsibility

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

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

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

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

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Bank and of the consolidated state of affairs of the Bank and its subsidiaries as at 31 December 2007 and of the consolidated profit and cash flows of the Bank and its subsidiaries for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

KPMG

Certified Public Accountants

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

11 April 2008

Consolidated income statement

For the year ended 31 December 2007

(Expressed in millions of Hong Kong dollars)

	Note	2007 HK\$'M	2006 HK\$'M
Interest income	3(a)	21,618	19,095
Interest expense	3(b)	(11,513)	(10,296)
Net interest income		<u>10,105</u>	<u>8,799</u>
Fee and commission income		6,080	4,530
Fee and commission expense		(974)	(801)
Net fee and commission income	3(c)	5,106	3,729
Net trading income	3(d)	543	187
Net losses from financial instruments designated at fair value	3(e)	(326)	(219)
Net gains from disposal of available-for-sale securities	5	238	22
Other operating income	3(f)	482	89
		<u>6,043</u>	<u>3,808</u>
Total operating income		16,148	12,607
Staff costs		(3,493)	(2,656)
Premises and equipment expense		(890)	(758)
Others		(2,665)	(1,969)
Operating expenses	3(g)	<u>(7,048)</u>	<u>(5,383)</u>
Operating profit before impairment		9,100	7,224
Impairment charge on advances to customers	4(a)	(227)	49
Other impairment charges	4(b)	(51)	–
Operating profit after impairment		8,822	7,273
Share of profit/(loss) of associates		12	(34)
Profit before taxation		8,834	7,239
Taxation	6(a)	<u>(1,464)</u>	<u>(1,213)</u>
Profit after taxation		7,370	6,026
Profit attributable to minority interests		(2)	–
Profit attributable to shareholders	32	<u>7,368</u>	<u>6,026</u>

The notes on pages 11 to 83 form part of these financial statements.

Consolidated balance sheet as at 31 December 2007*(Expressed in millions of Hong Kong dollars)*

	Note	2007 HK\$'M	2006 HK\$'M
Assets			
Cash and balances with banks and other financial institutions	9	8,113	7,809
Placements with banks and other financial institutions	10	114,827	49,122
Hong Kong SAR Government certificates of indebtedness	11	22,321	20,261
Trading assets	12	26,106	24,239
Advances to customers	13(a)	179,380	169,569
Amounts due from immediate holding company	16	48,890	38,099
Amounts due from fellow subsidiaries	16	17,540	11,941
Investment securities	15	49,929	57,140
Interest in associates	18	1,132	959
Fixed assets	19	3,173	3,250
Goodwill and intangible assets	20	783	763
Deferred tax assets	26	43	56
Other assets	21	9,489	7,834
		<u>481,726</u>	<u>391,042</u>
Liabilities			
Hong Kong SAR currency notes in circulation	11	22,321	20,261
Deposits and balances of banks and other financial institutions	22	16,037	7,514
Deposits from customers	23	358,584	288,513
Trading liabilities	27	17,949	15,854
Financial liabilities designated at fair value	25	4,439	9,514
Debt securities in issue	24	2,300	2,707
Amounts due to immediate holding company	16	6,075	2,608
Amounts due to fellow subsidiaries	16	1,301	580
Current tax liabilities		579	553
Deferred tax liabilities	26	398	23
Other liabilities	28	15,483	9,258
Subordinated liabilities	30	6,234	3,756
		<u>451,700</u>	<u>361,141</u>
Equity			
Share capital	31	97	3,901
Reserves	32	29,929	25,949
Shareholders' equity		30,026	29,850
Minority interests	32(d)	–	51
		<u>30,026</u>	<u>29,901</u>
		<u>481,726</u>	<u>391,042</u>

Approved and authorised for issue by the Board of Directors on 11 April 2008.

Sir C K Chow
Chairman

Hung Pi Cheng Benjamin
Director

Julian Fong Loong Choon
Director

Lai Wing Nga
Company Secretary

The notes on pages 11 to 83 form part of these financial statements.

Balance sheet as at 31 December 2007*(Expressed in millions of Hong Kong dollars)*

	Note	2007 HK\$'M	2006 HK\$'M
Assets			
Cash and balances with banks and other financial institutions	9	8,090	7,809
Placements with banks and other financial institutions	10	114,825	49,118
Hong Kong SAR Government certificates of indebtedness	11	22,321	20,261
Trading assets	12	26,106	24,238
Advances to customers	13(a)	179,380	169,001
Amounts due from immediate holding company	16	48,889	38,098
Amounts due from fellow subsidiaries	16	17,532	11,937
Amounts due from subsidiaries of the Bank	16	759	782
Investment securities	15	48,016	56,971
Investments in subsidiaries of the Bank	17	208	249
Interest in associates	18	1,117	959
Fixed assets	19	3,167	3,250
Goodwill and intangible assets	20	783	763
Deferred tax assets	26	43	56
Other assets	21	9,451	7,753
		<u>480,687</u>	<u>391,245</u>
Liabilities			
Hong Kong SAR currency notes in circulation	11	22,321	20,261
Deposits and balances of banks and other financial institutions	22	16,037	7,514
Deposits from customers	23	358,584	288,513
Trading liabilities	27	17,949	15,853
Financial liabilities designated at fair value	25	4,439	9,514
Debt securities in issue	24	2,300	2,707
Amounts due to immediate holding company	16	6,070	2,608
Amounts due to fellow subsidiaries	16	1,146	563
Amounts due to subsidiaries of the Bank	16	466	301
Current tax liabilities		580	551
Other liabilities	28	15,444	9,238
Subordinated liabilities	30	6,234	3,756
		<u>451,570</u>	<u>361,379</u>
Equity			
Share capital	31	97	3,901
Reserves	32	29,020	25,965
Shareholders' equity		<u>29,117</u>	<u>29,866</u>
		<u>480,687</u>	<u>391,245</u>

Approved and authorised for issue by the Board of Directors on 11 April 2008.

Sir C K Chow
Chairman

Hung Pi Cheng Benjamin
Director

Julian Fong Loong Choon
Director

Lai Wing Nga
Company Secretary

The notes on pages 11 to 83 form part of these financial statements.

Consolidated statement of recognised income and expense
For the year ended 31 December 2007

(Expressed in millions of Hong Kong dollars)

	<i>2007</i> <i>HK\$'M</i>	<i>2006</i> <i>HK\$'M</i>
Effective portion of changes in fair value of cash flow hedges	48	48
Exchange difference on translation of investment in associates	70	34
Changes in fair value of available-for-sale securities	1,518	236
Changes in fair value transferred to the income statement on disposal of available-for-sale securities	(238)	(22)
Actuarial gains on defined benefit plan	7	195
Deferred tax on income and expense recognised directly in equity	(396)	(73)
	<hr/>	<hr/>
Income and expense recognised directly in equity	1,009	418
Profit for the year	<hr/> 7,368	<hr/> 6,026
Total recognised income and expense for the year	<hr/> <hr/> 8,377	<hr/> <hr/> 6,444
Attributable to:		
Shareholders of the Bank	<hr/> <hr/> 8,377	<hr/> <hr/> 6,444

The notes on pages 11 to 83 form part of these financial statements.

Consolidated cash flow statement

For the year ended 31 December 2007

(Expressed in millions of Hong Kong dollars)

	Note	2007 HK\$'M	2006 HK\$'M (restated)
Operating activities			
Profit before taxation		8,834	7,239
Adjustments for:			
Impairment charge on advances to customers		227	(49)
Advances written off net of recoveries		(862)	(1,047)
Unwinding of discount on loan impairment charges		(34)	(18)
Other impairment charges		51	–
Losses/(gains) on disposal of fixed assets		5	(9)
Depreciation		168	179
Amortisation of intangible assets		59	104
Gain on disposal of merchant acquiring business		(86)	–
Recognition of profit on Visa shares		(316)	–
Share of (profit)/loss of associates		(12)	34
Interest expense on subordinated liabilities		268	168
Amortisation and exchange movement of subordinated liabilities		11	10
		<u>8,313</u>	<u>6,611</u>
(Increase)/decrease in operating assets:			
Placements with banks and other financial institutions			
with original maturity beyond three months		(14,350)	(8,477)
Trading assets		(5,651)	(6,296)
Investment securities		8,036	(12,447)
Gross advances to customers		(9,672)	421
Amounts due from immediate holding company			
and fellow subsidiaries		(15,649)	(8,750)
Other assets		(1,630)	(5,869)
Increase/(decrease) in operating liabilities:			
Deposits and balances of banks and other financial institutions		8,963	(1,435)
Deposits from customers		70,071	40,850
Debt securities in issue		(407)	(2,471)
Financial liabilities designated at fair value		(5,075)	4,361
Amounts due to immediate holding company and fellow subsidiaries		4,409	627
Trading liabilities		2,096	1,267
Other liabilities		6,304	5,786
		<u>55,758</u>	<u>14,178</u>
Cash generated from operations		55,758	14,178
Tax paid			
Hong Kong profits tax paid		(1,424)	(1,100)
		<u>54,334</u>	<u>13,078</u>
Net cash generated from operating activities		54,334	13,078

	Note	2007 HK\$'M	2006 HK\$'M (restated)
Investing activities			
Payment for purchase of an associate		(158)	–
Payment for purchase of fixed assets		(133)	(634)
Payment for purchase of intangible assets		(129)	(22)
Proceeds from disposal of merchant acquiring business		153	–
Proceeds from disposal of intangible assets		50	–
Proceeds from disposal of a subsidiary		55	–
Proceeds from disposal of fixed assets		37	21
		<u> </u>	<u> </u>
Net cash used in investing activities		(125)	(635)
		<u>-----</u>	<u>-----</u>
Financing activities			
Repurchase of share capital		(7,020)	–
Issuance of subordinated liabilities		2,377	–
Redemption/repurchase of subordinated liabilities		–	(45)
Interest paid on subordinated liabilities		(239)	(169)
Dividends paid		(1,181)	–
		<u> </u>	<u> </u>
Net cash used in financing activities		(6,063)	(214)
		<u>-----</u>	<u>-----</u>
Net increase in cash and cash equivalents		48,146	12,229
Cash and cash equivalents at 1 January		71,960	59,731
		<u> </u>	<u> </u>
Cash and cash equivalents at 31 December	33	120,106	71,960
		<u> </u>	<u> </u>
Cash flows from operating activities include:			
Interest received		21,310	18,513
Interest paid		11,466	9,618
Dividends received		10	22
		<u> </u>	<u> </u>

The notes on pages 11 to 83 form part of these financial statements.

Notes to the financial statements

(Expressed in millions of Hong Kong dollars)

1 Principal activities

The principal activities of Standard Chartered Bank (Hong Kong) Limited (the “Bank”) and its subsidiaries are the provision of banking and related financial services.

2 Significant accounting policies

(a) Statement of compliance

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

Although HKFRSs have been fully converged with IFRSs in all material respects since 1 January 2005, these financial statements are the first published financial statements in which the Bank and its subsidiaries make an explicit and unreserved statement of compliance with IFRSs. Therefore, in preparing these financial statements, management has given due consideration to the requirements of IFRS 1, First-time Adoption of International Financial Reporting Standards. For this purpose, the date of the Bank and its subsidiaries’ transition to IFRSs was determined to be 1 January 2006, being the beginning of the earliest period for which the Bank and its subsidiaries present full comparative information in these financial statements.

With due regard to the Bank and its subsidiaries’ accounting policies in previous periods and the requirements of IFRS 1, management has concluded that no adjustments to the amounts reported under HKFRSs as at the date of transition to IFRSs, or in respect of the year ended 31 December 2006, were required in order to enable the Bank and its subsidiaries to make an explicit and unreserved statement of compliance with IFRSs in the first IFRS financial statements which included these amounts as comparatives. Accordingly, these financial statements continue to include a statement of compliance with HKFRSs as well including for the first time a statement of compliance with IFRSs, without adjustment to the Consolidated and Bank’s financial position, financial performance or cash flows either at the date of transition to IFRSs or at the end of the latest period presented in accordance with HKFRSs.

(b) Basis of preparation of the financial statements

(i) Basis of Preparation

The consolidated financial statements comprise the accounts of the Bank and its subsidiaries made up to 31 December 2007.

(ii) Consolidated Financial Statements

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

(iii) New and revised IFRSs/HKFRSs

The IASB and HKICPA have issued certain new and revised IFRSs and HKFRSs that are first effective for the current accounting period of the Bank and its subsidiaries. Details of the impact of the new and revised IFRSs and HKFRSs are outlined in note 42.

(c) Subsidiaries

Subsidiaries are entities over which the Bank has the power to directly or indirectly govern the financial and operating policies, generally accompanying a shareholding of more than one half of the voting rights. Subsidiaries are fully consolidated from the date on which the Bank effectively obtains control. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Bank. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, together with costs directly attributable to the acquisition. Identifiable net assets and contingent liabilities acquired are fair valued at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Bank's share of the identifiable net assets and contingent liabilities acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets and contingent liabilities of the subsidiary acquired, the difference is recognised directly in the income statement.

Inter-company transactions, balances and unrealised gains on transactions between the Bank and its subsidiaries are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred.

In the Bank's balance sheet, investments in subsidiaries are stated at cost less any impairment and dividends from pre-acquisition profits received, if any.

(d) Associates

Associates are entities in respect of which the Bank has significant influence, but not control, over the financial and operating policies and procedures. Investments in associates are accounted for using the equity method of accounting in the consolidated financial statements and are initially recognised at cost.

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

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

In the Bank's balance sheet, the investment in an associate is stated at cost less any impairment and dividends from pre-acquisition profits received, if any.

(e) Intangible assets

(i) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Bank's share of the net identifiable assets of the acquired subsidiary/associate at the date of acquisition.

Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses, if any. Goodwill is allocated to cash-generating units for the purpose of impairment testing.

(ii) Computer software

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. Costs associated with the development of software are capitalised where it is probable that it will generate future economic benefits in excess of its cost. Computer software costs are amortised on the basis of the expected useful lives (two to five years). Costs associated with maintaining computer software programmes are recognised as an expense as incurred.

(f) Investment properties

Investment properties are land and buildings which are owned either to earn rental income or for long term investments or for both. Investment properties are stated in the balance sheet at depreciated cost less impairment. Investment properties are depreciated over their estimated useful lives on a straight-line basis.

(g) Other property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and impairment, if any. Cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

The Government of the Hong Kong SAR owns all the land in Hong Kong and permits its use under leasehold arrangements. Where the cost of land is known or can be reliably determined at the inception of the lease, the Bank records its interest in leasehold land and land use rights separately as operating leases. These leases are recorded at original cost and amortised over the term of the lease. Where the cost of the land is unknown, or cannot be reliably determined, the land and buildings are accounted for together as "Building and leasehold land held for own use".

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

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

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

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

(h) Leases

Where the Bank is the lessee

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

Where the Bank is the lessor

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

(i) Financial assets and liabilities (excluding derivatives)

Financial assets are classified in the following categories: financial assets at fair value through profit or loss, loans and receivables, and available-for-sale securities. Financial liabilities are classified either at fair value through profit or loss, or at amortised cost. Management determines the classification of its financial assets and liabilities on initial recognition.

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

This category has two sub-categories: financial assets and liabilities held for trading, and those designated at fair value through profit or loss at inception. A financial asset or liability is classified as trading if acquired principally for the purpose of selling or repurchasing in the short term or is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking.

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

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

(ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

(iii) Available-for-sale securities

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

Initial recognition

Purchases and sales of financial assets and liabilities at fair value through profit or loss, and available-for-sale are initially recognised using trade date accounting (the date on which the Bank commits to purchase or sell the asset). Loans and receivables are recognised when cash is advanced to the borrowers. Financial assets and financial liabilities are initially recognised at fair value plus directly attributable transaction costs for those financial assets and liabilities which are not carried at fair value through profit and loss.

Subsequent measurement

Available-for-sale financial assets and financial assets and liabilities at fair value through profit or loss are subsequently carried at fair value. Loans and receivables are carried at amortised cost using the effective interest rate method.

The fair values of quoted investments in active markets are based on current bid prices. If the market for a financial asset is not active, and for unlisted securities, the Bank establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models, and other valuation techniques commonly used by market participants.

Renegotiated loans

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

Derecognition

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

(j) *Derivative financial instruments and hedge accounting*

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

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

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

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

(i) Fair value hedge

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

(ii) *Cash flow hedge*

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

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

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

Derivatives that do not qualify for hedge accounting

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

(k) Impairment of financial assets

Assets carried at amortised cost

The Bank assesses at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

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

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

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

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

To the extent a loan is irrecoverable, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are credited to the income statement. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

Available-for-sale assets

A significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss (measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss) is removed from equity and recognised in the income statement. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement.

(l) Offsetting financial instruments

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

(m) Fiduciary activities

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

(n) Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including: cash and balances with banks and other financial institutions, placements with banks and other financial institutions, and treasury bills.

(o) Revenue recognition

(i) Interest income and expense

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

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

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised at the original effective interest rate of the financial asset applied to the impaired carrying amount.

(ii) Fees and commissions

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

(iii) Other income from financial assets and liabilities

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

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

Dividends on available-for-sale equity instruments are recognized in the income statement when the Bank's right to receive payment is established.

(p) Income tax

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

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

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

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

Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset. Current tax assets are offset against current tax liabilities, and deferred tax assets against deferred tax liabilities if the Bank and its subsidiaries have 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 Group or 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 either the same taxable entity or different taxable entities for which a legal right of set off exists.

(q) Provisions

Provisions for liabilities and charges are recognised when it is probable that an outflow of economic benefits will be required to settle a present legal or constructive obligation arising from past events and a reliable estimate can be made of the amount of the obligation.

(r) Employee benefits

(i) Short term employee benefits

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

(ii) Pension obligations

The Bank has defined contribution plans and a defined benefit plan.

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

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

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

(iii) Share-based compensation

The Standard Chartered PLC Group operates equity-settled share-based compensation plans in which the Bank's employees participate. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. For equity-settled awards, the total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example, profitability and growth targets). The fair value of equity instruments granted is based on market prices, if available, at the date of grant. In the absence of market prices, the fair value of the instruments is estimated using an appropriate valuation technique, such as a binomial option pricing model.

(s) Translation of foreign currencies

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

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

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

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

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

(t) Related parties

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

3 Operating profit

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

	<i>2007</i> <i>HK\$'M</i>	<i>2006</i> <i>HK\$'M</i>
(a) Interest income		
Interest income on listed securities	132	143
Interest income on unlisted securities	2,355	2,566
Other interest income	<u>19,131</u>	<u>16,386</u>
Amount shown in the income statement	21,618	19,095
Less: Interest income arising from trading assets	(1,057)	(733)
Less: Interest income arising from financial assets designated at fair value	<u>(53)</u>	<u>(151)</u>
Total interest income on financial assets that are not measured at fair value through profit or loss	<u><u>20,508</u></u>	<u><u>18,211</u></u>
Other interest income includes interest income on unwinding of discounts on loan impairment charges of HK\$34 million (note 14) (2006: HK\$18 million) for the year ended 31 December 2007.		
(b) Interest expense		
Interest expense on customer deposits, deposits of banks, certificates of deposit issued and debt securities issued	11,245	10,128
Interest expense on subordinated liabilities	<u>268</u>	<u>168</u>
Amount shown in the income statement	11,513	10,296
Less: Interest expense arising from trading liabilities	<u>(613)</u>	<u>(299)</u>
Total interest expense on financial liabilities that are not measured at fair value through profit or loss	<u><u>10,900</u></u>	<u><u>9,997</u></u>
(c) Net fee and commission income		
Net fee and commission income, other than amounts included in determining the effective interest rate, arising from financial assets or financial liabilities that are not held for trading or designated at fair value		
– fee and commission income	1,130	1,062
– fee and commission expense	<u>288</u>	<u>266</u>
Net fee income from trust and other fiduciary activities where the Bank holds or invests assets on behalf of its customers		
– fee and commission income	499	328
– fee and commission expense	<u>104</u>	<u>71</u>

	2007 HK\$'M	2006 HK\$'M
(d) Net trading income		
Gains less losses from dealing in foreign currencies	358	304
Gains less losses from trading securities	202	(30)
Losses from other dealing activities	(17)	(87)
	<u>543</u>	<u>187</u>
Amount shown in the income statement	543	187
Add: interest income arising from trading assets	1,057	733
Less: interest expense arising from trading liabilities	(613)	(299)
	<u>987</u>	<u>621</u>
Net income from trading instruments	<u><u>987</u></u>	<u><u>621</u></u>
(e) Net losses from financial instruments designated at fair value		
Net losses as shown in the income statement	(326)	(219)
Add: interest income arising from financial assets designated at fair value	53	151
	<u>(273)</u>	<u>(68)</u>
Net losses from financial instruments designated at fair value	<u><u>(273)</u></u>	<u><u>(68)</u></u>
(f) Other operating income		
Dividend income from listed available-for-sale securities	3	3
Dividend income from unlisted available-for-sale securities	7	19
Net gains on disposal of financial instruments measured at amortised cost	17	19
(Losses)/gains on disposal of fixed assets	(5)	9
Gain on disposal of merchant acquiring business	86	–
Recognition of profit on Visa shares	316	–
Others	58	39
	<u>482</u>	<u>89</u>
Other operating income	<u><u>482</u></u>	<u><u>89</u></u>
(g) Operating expenses		
Staff costs		
– contributions to defined contribution plans	82	62
– current service costs in respect of the defined benefits plan (note 29(d))	35	55
– equity-settled share-based payment expenses	84	80
– salaries and other staff costs	3,292	2,459
Depreciation (note 19(a))	168	179
Premises and equipment expense, excluding depreciation		
– rental of premises	428	352
– others	294	227
Amortisation		
– other intangible assets (note 20)	59	104
Auditors' remuneration	9	8
Others	2,597	1,857
	<u>7,048</u>	<u>5,383</u>
Operating expenses	<u><u>7,048</u></u>	<u><u>5,383</u></u>

4 Impairment charges

	2007 HK\$'M	2006 HK\$'M
(a) Impairment charge on advances to customers		
Individual impairment provisions (note 14)		
– additions	756	866
– releases	(259)	(488)
– recoveries	(247)	(364)
	<u>250</u>	<u>14</u>
	-----	-----
Portfolio impairment provisions (note 14)	(23)	(63)
	<u>227</u>	<u>(49)</u>
	=====	=====
(b) Other impairment charges		
Impairment charge on other financial assets measured at amortised cost	37	–
Provision for contingent liabilities	14	–
	<u>51</u>	<u>–</u>
	=====	=====

5 Net gains from disposal of available-for-sale securities

	2007 HK\$'M	2006 HK\$'M
Net gains transferred from reserves (note 32(a))	<u>238</u>	<u>22</u>
	=====	=====

6 Taxation in the consolidated income statement**(a) Taxation in the consolidated income statement represents:**

	2007 HK\$'M	2006 HK\$'M
<i>Current tax</i>		
Provision for the year	1,458	1,258
Over-provision in respect of prior years	(10)	(35)
	<u>1,448</u>	<u>1,223</u>
	-----	-----
<i>Deferred tax (note 26)</i>		
Reversal of temporary differences	1	(10)
Under-provision in respect of prior years	15	–
	<u>16</u>	<u>(10)</u>
	-----	-----
	<u>1,464</u>	<u>1,213</u>
	=====	=====

The provision for Hong Kong Profits Tax for 2007 is calculated at 17.5% (2006: 17.5%) of the estimated assessable profits for the year. Taxation for overseas subsidiaries is charged at the appropriate current rates of taxation ruling in the relevant jurisdictions.

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

	2007 HK\$'M	2006 HK\$'M
Profit before taxation	8,834	7,239
Notional tax on profit before taxation, calculated at Hong Kong profits tax rate of 17.5%	1,546	1,267
Tax effect of non-deductible expenses	44	37
Tax effect of non-taxable revenue	(134)	(64)
Under/(over)-provision in prior years	5	(35)
Tax effect of different tax rates of subsidiaries operating in other jurisdictions	5	–
Others	(2)	8
Actual tax expense	1,464	1,213

7 Directors' remuneration

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

	<i>Bank</i>	
	2007 HK\$'M	2006 HK\$'M
Fees	2	2
Salaries and other emoluments	19	19
	21	21

8 Segmental reporting

	<i>Consumer banking</i>		<i>Wholesale banking</i>		<i>Corporate items not allocated</i>		<i>Consolidated Total</i>	
	2007 HK\$'M	2006 HK\$'M	2007 HK\$'M	2006 HK\$'M	2007 HK\$'M	2006 HK\$'M	2007 HK\$'M	2006 HK\$'M
Total operating income	9,000	7,738	7,062	4,869	86	–	16,148	12,607
Total operating expenses	(3,851)	(3,184)	(3,197)	(2,199)	–	–	(7,048)	(5,383)
Operating profit	5,149	4,554	3,865	2,670	86	–	9,100	7,224
Impairment (charges)/allowances	(314)	(316)	36	365	–	–	(278)	49
Share of profit/(loss) in associates	–	–	–	–	12	(34)	12	(34)
	4,835	4,238	3,901	3,035	98	(34)	8,834	7,239
Segment assets	123,202	132,436	357,349	257,591	43	56	480,594	390,083
Interest in associates	–	–	–	–	1,132	959	1,132	959
Total asset	123,202	132,436	357,349	257,591	1,175	1,015	481,726	391,042
Segment liabilities	190,824	182,081	259,899	178,484	977	576	451,700	361,141
Depreciation and amortisation for the year	(132)	(191)	(95)	(92)	–	–	(227)	(283)
Capital expenditure incurred during the year	(214)	(467)	(48)	(189)	–	–	(262)	(656)

The Bank and its subsidiaries comprise two main business segments: Consumer Banking which provides financial services to customers including lending and deposit taking activities, credit card facilities and investment services; and Wholesale Banking which provides financial services to corporations and institutions, including lending and deposit taking activities, structured finance products, syndicated loans, cash management, investment advice, distributing fixed income and equity investments, interbank and capital market activities and foreign exchange transactions.

The Bank and its subsidiaries comprise only one geographical segment as over 90% of the business is based in Hong Kong.

9 Cash and balances with banks and other financial institutions

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2007</i>	<i>2006</i>	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Cash in hand	1,242	1,376	1,219	1,376
Balances with central bank	3,854	5,222	3,854	5,222
Balances with banks and other financial institutions	3,017	1,211	3,017	1,211
	<u>8,113</u>	<u>7,809</u>	<u>8,090</u>	<u>7,809</u>

10 Placements with banks and other financial institutions

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2007</i>	<i>2006</i>	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Gross placements with banks and other financial institutions				
– maturing within one month	89,840	35,823	89,838	35,819
– maturing between one month to one year	24,869	13,299	24,869	13,299
– maturing between one year to five years	107	–	107	–
– maturing after five years	11	–	11	–
	<u>114,827</u>	<u>49,122</u>	<u>114,825</u>	<u>49,118</u>

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

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

12 Trading assets

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2007</i>	<i>2006</i>	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Trading securities	23,855	20,238	23,855	20,238
Positive fair values of derivatives	2,251	4,001	2,251	4,000
	<u>26,106</u>	<u>24,239</u>	<u>26,106</u>	<u>24,238</u>
Trading securities:				
Treasury bills (including Exchange Fund Bills)	9,789	8,898	9,789	8,898
Certificates of deposit held	3,252	2,919	3,252	2,919
Debt securities	10,814	8,421	10,814	8,421
	<u>23,855</u>	<u>20,238</u>	<u>23,855</u>	<u>20,238</u>
Issued by:				
Central governments and central banks	16,120	11,654	16,120	11,654
Public sector entities	–	290	–	290
Banks and other financial institutions	5,694	7,751	5,694	7,751
Corporate entities	2,041	543	2,041	543
	<u>23,855</u>	<u>20,238</u>	<u>23,855</u>	<u>20,238</u>
By place of listing:				
Listed in Hong Kong	6,330	2,756	6,330	2,756
Listed outside Hong Kong	275	9	275	9
	<u>6,605</u>	<u>2,765</u>	<u>6,605</u>	<u>2,765</u>
Unlisted	17,250	17,473	17,250	17,473
	<u>23,855</u>	<u>20,238</u>	<u>23,855</u>	<u>20,238</u>

Included within the positive fair values of derivatives is HK\$1,490 million (2006: HK\$3,498 million) relating to derivatives that are issued by the immediate holding company.

13 Advances to customers**(a) Advances to customers**

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2007</i>	<i>2006</i>	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Gross advances to customers	177,434	168,470	177,434	167,902
Trade bills	2,852	2,674	2,852	2,674
	<u>180,286</u>	<u>171,144</u>	<u>180,286</u>	<u>170,576</u>
Less : Impairment charges				
– individually assessed (note 14)	(578)	(1,224)	(578)	(1,224)
– collectively assessed (note 14)	(328)	(351)	(328)	(351)
	<u>179,380</u>	<u>169,569</u>	<u>179,380</u>	<u>169,001</u>
Net advances to customers, measured at				
– amortised cost	176,479	167,734	176,479	167,166
– designated at fair value through profit or loss	2,901	1,835	2,901	1,835
	<u>179,380</u>	<u>169,569</u>	<u>179,380</u>	<u>169,001</u>

(b) Impaired advances to customers

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2007</i>	<i>2006</i>	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Gross impaired advances to customers	1,166	1,892	1,166	1,892
Impairment charges – individually assessed	(578)	(1,224)	(578)	(1,224)
	<u>588</u>	<u>668</u>	<u>588</u>	<u>668</u>
Gross impaired advances to customers as a % of gross advances to customers	<u>0.65%</u>	<u>1.11%</u>	<u>0.65%</u>	<u>1.11%</u>
Fair value of collateral held against the covered portion of impaired advances to customers	<u>317</u>	<u>367</u>	<u>317</u>	<u>367</u>
Covered portion of impaired advances to customers	240	286	240	286
Uncovered portion of impaired advances to customers	<u>926</u>	<u>1,606</u>	<u>926</u>	<u>1,606</u>

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

There were no impaired advances to banks and other financial institutions as at 31 December 2007 and 31 December 2006.

(c) Net investment in finance leases

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

	<i>Consolidated</i>					
	2007			2006		
	<i>Present value of the minimum lease payments receivable</i> HK\$'M	<i>Interest income relating to future periods</i> HK\$'M	<i>Total minimum lease payments</i> HK\$'M	<i>Present value of the minimum lease payments receivable</i> HK\$'M	<i>Interest income relating to future periods</i> HK\$'M	<i>Total minimum lease payments</i> HK\$'M
Within 1 year	65	8	73	375	52	427
After 1 year but within 5 years	71	6	77	481	59	540
After 5 years	5	1	6	85	26	111
	<u>141</u>	<u>15</u>	<u>156</u>	<u>941</u>	<u>137</u>	<u>1,078</u>
Impairment charges:						
– individually assessed	–			–		
Net investment in finance leases	<u>141</u>			<u>941</u>		

	<i>Bank</i>					
	2007			2006		
	<i>Present value of the minimum lease payments receivable</i> HK\$'M	<i>Interest income relating to future periods</i> HK\$'M	<i>Total minimum lease payments</i> HK\$'M	<i>Present value of the minimum lease payments receivable</i> HK\$'M	<i>Interest income relating to future periods</i> HK\$'M	<i>Total minimum lease payments</i> HK\$'M
Within 1 year	65	8	73	120	20	140
After 1 year but within 5 years	71	6	77	167	33	200
After 5 years	5	1	6	85	26	111
	<u>141</u>	<u>15</u>	<u>156</u>	<u>372</u>	<u>79</u>	<u>451</u>
Impairment charges:						
– individually assessed	–			–		
Net investment in finance leases	<u>141</u>			<u>372</u>		

14 Movement in impairment charges on advances to customers**Consolidated and Bank**

	<i>Individually assessed HK\$'M</i>	<i>2007 Collectively assessed HK\$'M</i>	<i>Total HK\$'M</i>
At 1 January 2007	1,224	351	1,575
Amounts written off	(1,109)	–	(1,109)
Recoveries of advances written off in previous years	247	–	247
Net charge/(release) to the income statement (note 4(a))	250	(23)	227
Unwind of discount on loan impairment charges (note 3(a))	(34)	–	(34)
	<u>578</u>	<u>328</u>	<u>906</u>
At 31 December 2007 (note 13(a))	<u>578</u>	<u>328</u>	<u>906</u>

Consolidated

	<i>Individually assessed HK\$'M</i>	<i>2006 Collectively assessed HK\$'M</i>	<i>Total HK\$'M</i>
At 1 January 2006	2,275	414	2,689
Amounts written off	(1,411)	–	(1,411)
Recoveries of advances written off in previous years	364	–	364
Net charge/(release) to the income statement (note 4(a))	14	(63)	(49)
Unwind of discount on loan impairment charges (note 3(a))	(18)	–	(18)
	<u>1,224</u>	<u>351</u>	<u>1,575</u>
At 31 December 2006 (note 13(a))	<u>1,224</u>	<u>351</u>	<u>1,575</u>

Bank

	<i>Individually assessed HK\$'M</i>	<i>2006 Collectively assessed HK\$'M</i>	<i>Total HK\$'M</i>
At 1 January 2006	2,274	413	2,687
Amounts written off	(1,408)	–	(1,408)
Recoveries of advances written off in previous years	364	–	364
Net charge/(release) to the income statement	12	(62)	(50)
Unwind of discount on loan impairment charges	(18)	–	(18)
	<u>1,224</u>	<u>351</u>	<u>1,575</u>
At 31 December 2006 (note 13(a))	<u>1,224</u>	<u>351</u>	<u>1,575</u>

15 Investment securities

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2007</i>	<i>2006</i>	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Available-for-sale securities				
Treasury bills (including Exchange Fund Bills)	14,457	15,218	14,457	15,218
Certificates of deposit held	960	307	960	307
Debt securities	31,948	41,160	31,734	41,160
Equity shares	2,160	460	461	291
Less: Impairment charges	(5)	(5)	(5)	(5)
	<u>49,520</u>	<u>57,140</u>	<u>47,607</u>	<u>56,971</u>
Loans and receivables – Debt securities	452	–	452	–
Less: Impairment charges	(43)	–	(43)	–
	<u>49,929</u>	<u>57,140</u>	<u>48,016</u>	<u>56,971</u>
Issued by:				
Central governments and central banks	15,898	16,487	15,898	16,487
Public sector entities	4,175	5,524	4,175	5,524
Banks and other financial institutions	26,406	34,059	24,707	33,890
Corporate entities	3,450	1,070	3,236	1,070
	<u>49,929</u>	<u>57,140</u>	<u>48,016</u>	<u>56,971</u>
By place of listing:				
Listed in Hong Kong	939	265	939	265
Listed outside Hong Kong	4,271	1,711	2,572	1,542
	<u>5,210</u>	<u>1,976</u>	<u>3,511</u>	<u>1,807</u>
Unlisted	44,719	55,164	44,505	55,164
	<u>49,929</u>	<u>57,140</u>	<u>48,016</u>	<u>56,971</u>

Available-for-sale securities included HK\$2,343 million (2006: HK\$2,334 million) of securities that are issued by the immediate holding company and HK\$2,586 million (2006: HK\$2,084 million) of securities that are issued by a fellow subsidiary.

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

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

(i) Consolidated

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

	<i>Immediate holding company</i>		<i>Fellow subsidiaries</i>	
	<i>2007</i>	<i>2006</i>	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Income	1,517	1,258	950	471
Expenses	567	916	681	422

(ii) The Bank

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

	<i>Immediate holding company</i>		<i>Fellow subsidiaries</i>		<i>Subsidiaries of the Bank</i>	
	<i>2007</i>	<i>2006</i>	<i>2007</i>	<i>2006</i>	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Income	1,517	1,258	950	471	34	37
Expenses	567	916	681	422	1	1

17 Investments in subsidiaries of the Bank

	<i>Bank</i>	
	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Unlisted shares, at cost less impairment charges, if any	<u>208</u>	<u>249</u>

The following list contains only the particulars of subsidiaries which principally affected the results, assets or liabilities of the Bank and its subsidiaries. The class of shares held is ordinary unless otherwise stated.

<i>Name of company</i>	<i>Place of incorporation</i>	<i>Particulars of issued and paid up capital and securities</i>	<i>Proportion of ownership interest held by the Bank</i>	<i>Principal activity</i>
Standard Chartered Investment Services Limited	Hong Kong	1,500,000 shares of HK\$10 each	100%	Investment advisory services
Standard Chartered APR Limited	United Kingdom	21,971,715 shares of US\$1 each	100%	Investment holdings
Horsford Nominees Limited	Hong Kong	10 shares of HK\$10 each	100%	Provision of nominee services
Popular Ambience Sdn Bhd	Malaysia	100 shares of RM1 each	100%*	Investment holdings

* The Bank directly holds 49% of the share capital issued by the company and has an effective interest of 100% in the company.

18 Interest in associates**Consolidated**

	2007 HK\$'M	2006 HK\$'M
Share of net assets	1,132	959

Bank

	2007 HK\$'M	2006 HK\$'M
Unlisted shares, at cost less impairment losses, if any	1,117	959

The associated companies of the Bank and its subsidiaries are:

<i>Name of associate</i>	<i>Place of establishment and operation</i>	<i>Particulars of issued and paid up capital</i>	<i>Proportion of ownership interest</i>	<i>Principal activity</i>
China Bohai Bank Company Limited ("Bohai")	The People's Republic of China	5,000,000,000 ordinary shares of RMB1 each	19.99%	Provision of banking and related financial services
Merchant Solutions Private Limited	Singapore	560,000 "A" shares and 440,000 "B" shares	44.00%	Credit card merchant acquiring business

Summary of financial information of associates

	<i>Assets HK\$'M</i>	<i>Liabilities HK\$'M</i>	<i>Equity HK\$'M</i>	<i>Revenue HK\$'M</i>	<i>Profit HK\$'M</i>
2007					
100 per cent	35,236	29,666	5,570	666	63
Bank's effective interest	7,100	5,968	1,132	137	12
	<i>Assets HK\$'M</i>	<i>Liabilities HK\$'M</i>	<i>Equity HK\$'M</i>	<i>Revenue HK\$'M</i>	<i>Loss HK\$'M</i>
2006					
100 per cent	15,293	10,494	4,799	277	172
Bank's effective interest	3,057	2,098	959	55	34

19 Fixed assets**(a) Consolidated**

	2007				
	<i>Buildings and leasehold land held for own use HK\$'M</i>	<i>Equipment, furniture & fixtures HK\$'M</i>	<i>Sub-total HK\$'M</i>	<i>Investment properties HK\$'M</i>	<i>Total fixed assets HK\$'M</i>
Cost:					
At 1 January 2007	2,431	469	2,900	886	3,786
Additions	79	54	133	–	133
Disposals	(53)	(33)	(86)	–	(86)
Reclassifications	208	34	242	(242)	–
At 31 December 2007	<u>2,665</u>	<u>524</u>	<u>3,189</u>	<u>644</u>	<u>3,833</u>
Accumulated depreciation:					
At 1 January 2007	247	268	515	21	536
Charge for the year (note 3(g))	86	70	156	12	168
Written back on disposals	(18)	(26)	(44)	–	(44)
Reclassifications	12	–	12	(12)	–
At 31 December 2007	<u>327</u>	<u>312</u>	<u>639</u>	<u>21</u>	<u>660</u>
Net book value:					
At 31 December 2007	<u>2,338</u>	<u>212</u>	<u>2,550</u>	<u>623</u>	<u>3,173</u>
	2006				
	<i>Buildings and leasehold land held for own use HK\$'M</i>	<i>Equipment, furniture & fixtures HK\$'M</i>	<i>Sub-total HK\$'M</i>	<i>Investment properties HK\$'M</i>	<i>Total fixed assets HK\$'M</i>
Cost:					
At 1 January 2006	2,406	519	2,925	385	3,310
Additions	53	80	133	501	634
Disposals	(28)	(130)	(158)	–	(158)
At 31 December 2006	<u>2,431</u>	<u>469</u>	<u>2,900</u>	<u>886</u>	<u>3,786</u>
Accumulated depreciation:					
At 1 January 2006	184	311	495	8	503
Charge for the year (note 3(g))	79	87	166	13	179
Written back on disposals	(16)	(130)	(146)	–	(146)
At 31 December 2006	<u>247</u>	<u>268</u>	<u>515</u>	<u>21</u>	<u>536</u>
Net book value:					
At 31 December 2006	<u>2,184</u>	<u>201</u>	<u>2,385</u>	<u>865</u>	<u>3,250</u>

(b) Bank

	2007				
	<i>Buildings and leasehold land held for own use HK\$'M</i>	<i>Equipment, furniture & fixtures HK\$'M</i>	<i>Sub-total HK\$'M</i>	<i>Investment properties HK\$'M</i>	<i>Total fixed assets HK\$'M</i>
Cost:					
At 1 January 2007	2,431	469	2,900	886	3,786
Additions	79	47	126	–	126
Disposals	(53)	(33)	(86)	–	(86)
Reclassifications	208	34	242	(242)	–
At 31 December 2007	<u>2,665</u>	<u>517</u>	<u>3,182</u>	<u>644</u>	<u>3,826</u>
Accumulated depreciation:					
At 1 January 2007	247	268	515	21	536
Charge for the year	86	69	155	12	167
Written back on disposals	(18)	(26)	(44)	–	(44)
Reclassifications	12	–	12	(12)	–
At 31 December 2007	<u>327</u>	<u>311</u>	<u>638</u>	<u>21</u>	<u>659</u>
Net book value:					
At 31 December 2007	<u>2,338</u>	<u>206</u>	<u>2,544</u>	<u>623</u>	<u>3,167</u>
	2006				
	<i>Buildings and leasehold land held for own use HK\$'M</i>	<i>Equipment, furniture & fixtures HK\$'M</i>	<i>Sub-total HK\$'M</i>	<i>Investment properties HK\$'M</i>	<i>Total fixed assets HK\$'M</i>
Cost:					
At 1 January 2006	2,406	512	2,918	385	3,303
Additions	53	80	133	501	634
Disposals	(28)	(123)	(151)	–	(151)
At 31 December 2006	<u>2,431</u>	<u>469</u>	<u>2,900</u>	<u>886</u>	<u>3,786</u>
Accumulated depreciation:					
At 1 January 2006	184	305	489	8	497
Charge for the year	79	86	165	13	178
Written back on disposals	(16)	(123)	(139)	–	(139)
At 31 December 2006	<u>247</u>	<u>268</u>	<u>515</u>	<u>21</u>	<u>536</u>
Net book value:					
At 31 December 2006	<u>2,184</u>	<u>201</u>	<u>2,385</u>	<u>865</u>	<u>3,250</u>

Buildings and leasehold land held for own use:

	<i>Consolidated and Bank</i>	
	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Leasehold in Hong Kong, at cost		
– medium-term leases	2,224	2,089
– short leases	114	95
	<u>2,338</u>	<u>2,184</u>

Investment properties:

	<i>Consolidated and Bank</i>	
	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Leasehold in Hong Kong, at cost		
– medium-term leases	135	367
Freehold outside Hong Kong	488	498
	<u>623</u>	<u>865</u>

The investment properties are stated at depreciated cost less impairment. The fair value of the investment properties located in Hong Kong and outside Hong Kong as at 31 December 2007 was HK\$133 million (2006: HK\$377 million) and HK\$786 million (2006: HK\$708 million) respectively. The fair value was based on an open market value basis calculated by reference to net rental income allowing for reversionary income potential. The valuations of investment properties located in Hong Kong were carried out by an independent firm which has among its staff, members of the Hong Kong Institute of Surveyors with recent experience in the location and category of property being valued. The valuation of investment properties located outside Hong Kong was carried out by an independent firm which has among its staff, members of the Royal Institute of Chartered Surveyors with recent experience in the location and category of property being valued.

Impairment tests for cash-generating units containing goodwill

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

	2007 HK\$'M	2006 HK\$'M
Credit cards and personal loans	611	611

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

In assessing impairment of goodwill, the Bank assumed growth at a steady rate in line with long-term forecast GDP growth. A discount rate of 11.5 per cent (2006: 14.5 per cent) was used.

21 Other assets

	<i>Consolidated</i>		<i>Bank</i>	
	2007 HK\$'M	2006 HK\$'M	2007 HK\$'M	2006 HK\$'M
Prepayments and accrued income	5,212	4,519	5,200	4,507
Acceptances and endorsements	3,002	2,897	3,002	2,897
Positive fair values of hedging derivatives	63	35	63	35
Others	1,212	383	1,186	314
	<u>9,489</u>	<u>7,834</u>	<u>9,451</u>	<u>7,753</u>

Positive fair values of hedging derivatives represent derivatives that are issued by the immediate holding company.

22 Deposits and balances of banks and other financial institutions

	<i>Consolidated and Bank</i>	
	2007 HK\$'M	2006 HK\$'M
Deposits and balances of central banks	7,291	1,804
Deposits and balances of other banks	8,746	5,710
	<u>16,037</u>	<u>7,514</u>

23 Deposits from customers

	<i>Consolidated and Bank</i>	
	2007 HK\$'M	2006 HK\$'M
Current accounts	40,332	23,763
Savings accounts	158,843	126,820
Time, call and notice deposits	159,409	137,930
	<u>358,584</u>	<u>288,513</u>

24 Debt securities in issue

	<i>Consolidated and Bank</i>	
	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Certificates of deposit, measured at amortised cost	1,408	2,707
Other debt securities, measured at amortised cost	892	–
	<u>2,300</u>	<u>2,707</u>

Other debt securities represent securities that are issued to a fellow subsidiary of the Bank.

25 Financial liabilities designated at fair value

	<i>Consolidated and Bank</i>	
	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Structured customer deposits	3,301	8,137
Debt securities issued	1,138	1,377
	<u>4,439</u>	<u>9,514</u>

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

- have fixed rates of interest and interest rate swaps or other interest related derivatives have been transacted with the intention of significantly reducing interest rate risk; or
- are exposed to foreign currency risk and derivatives have been transacted with the intention of significantly reducing exposure to market changes; or
- have been acquired to fund trading asset portfolios or assets, or where the assets and liabilities are managed, and performance evaluated, on a fair value basis for a documented risk management or investment strategy.

At 31 December 2007, the carrying amount of these financial liabilities exceeded the contractual amount payable at maturity by HK\$43 million (2006: HK\$60 million). This change is attributable to changes in market rates.

26 Taxation in the balance sheet**Deferred tax assets and liabilities:**

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

Consolidated

	<i>Depreciation allowances in excess of related depreciation HK\$'M</i>	<i>Impairment losses on financial assets HK\$'M</i>	<i>Others HK\$'M</i>	<i>Total HK\$'M</i>
	2007			
Deferred tax arising from:				
At 1 January 2007	2	(61)	26	(33)
Charge to income statement (note 6(a))	6	4	6	16
Charge to reserves (note 32(a))	–	–	396	396
Disposal of a subsidiary	(24)	–	–	(24)
At 31 December 2007	<u>(16)</u>	<u>(57)</u>	<u>428</u>	<u>355</u>
	2006			
At 1 January 2006	13	(71)	(38)	(96)
(Credit)/charge to income statement (note 6(a))	(11)	10	(9)	(10)
Charge to reserves (note 32(a))	–	–	73	73
At 31 December 2006	<u>2</u>	<u>(61)</u>	<u>26</u>	<u>(33)</u>

Bank

	<i>Depreciation allowances in excess of related depreciation HK\$'M</i>	<i>Impairment losses on financial assets HK\$'M</i>	<i>Others HK\$'M</i>	<i>Total HK\$'M</i>
2007				
Deferred tax arising from:				
At 1 January 2007	(21)	(61)	26	(56)
Charge to income statement	5	4	6	15
Credit to reserves (note 32(b))	—	—	(2)	(2)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
At 31 December 2007	<u>(16)</u>	<u>(57)</u>	<u>30</u>	<u>(43)</u>
2006				
At 1 January 2006	(12)	(71)	(38)	(121)
(Credit)/charge to income statement	(9)	10	(9)	(8)
Charge to reserves (note 32(b))	—	—	73	73
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
At 31 December 2006	<u>(21)</u>	<u>(61)</u>	<u>26</u>	<u>(56)</u>
Consolidated				
	<i>2007</i>	<i>2006</i>	<i>Bank</i>	
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>2007</i>	<i>2006</i>
			<i>HK\$'M</i>	<i>HK\$'M</i>
Analysed by:				
Net deferred tax asset recognised on the balance sheet	(43)	(56)	(43)	(56)
Net deferred tax liability recognised on the balance sheet	398	23	—	—
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
	<u>355</u>	<u>(33)</u>	<u>(43)</u>	<u>(56)</u>

On 27 February 2008, the Financial Secretary of the Hong Kong SAR Government announced his annual Budget which proposed a cut in profits tax rate from 17.5% to 16.5% with effect from the fiscal year 2008-2009 and a one-off reduction of 75% of the tax payable for the 2007-2008 assessment subject to a ceiling of HK\$25,000. No adjustments have been made to these financial statements as a result of this announcement. The directors have estimated that the impact of these proposed changes to the Bank's and its subsidiaries' deferred tax balances is not material.

27 Trading liabilities

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2007</i>	<i>2006</i>	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Short positions in securities	16,047	11,886	16,047	11,886
Negative fair values of derivatives	1,902	3,968	1,902	3,967
	<u>17,949</u>	<u>15,854</u>	<u>17,949</u>	<u>15,853</u>

Included within the negative fair values of derivatives are HK\$1,413 million (2006: HK\$3,850 million) relating to derivatives that are issued by the immediate holding company.

28 Other liabilities

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2007</i>	<i>2006</i>	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Accruals and deferred income	2,423	1,947	2,405	1,933
Provision for liabilities and charges	30	16	30	16
Negative fair values of hedging derivatives	15	126	15	126
Acceptance and endorsements	3,002	2,897	3,002	2,897
Others	10,013	4,272	9,992	4,266
	<u>15,483</u>	<u>9,258</u>	<u>15,444</u>	<u>9,238</u>

Negative fair values of hedging derivatives represent derivatives that are issued by the immediate holding company.

29 Employee retirement benefits

The Bank makes contributions to a defined benefit retirement scheme (the "Scheme") which covers 30% (2006: 38%) of the Bank's employees. The Scheme is administered by a trustee, with the assets held separately from those of the Bank.

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

	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Fair value of plan assets	1,980	1,719
Present value of wholly or partly funded obligations	<u>(1,666)</u>	<u>(1,458)</u>
Net asset recognised in the balance sheet (included in "Other assets")	<u>314</u>	<u>261</u>

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

	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
At the beginning of the year	1,458	1,377
Current service cost	90	90
Interest cost	55	56
Benefits paid	(107)	(74)
Actuarial losses	170	9
	<u>1,666</u>	<u>1,458</u>

(c) Movements in the fair value of assets:

	2007 HK\$'M	2006 HK\$'M
At the beginning of the year	1,719	1,415
Contributions	81	83
Expected return on assets	110	91
Benefits paid	(107)	(74)
Actuarial gains on plan assets	177	204
	<u>1,980</u>	<u>1,719</u>

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

	2007 HK\$'M	2006 HK\$'M
At the beginning of the year	261	38
Contributions	81	83
Expense recognised in the income statement (note 3(g))	(35)	(55)
Actuarial gains to pension reserve (note 32(a))	7	195
	<u>314</u>	<u>261</u>

As at 31 December 2007, the Scheme did not invest in the Bank's own financial instruments and properties (2006: HK\$Nil). The Bank expects to contribute approximately HK\$64 million to the Scheme in 2008 (2007: HK\$83 million).

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

	2007 HK\$'M	2006 HK\$'M
Current service cost	90	90
Interest cost	55	56
Actuarial expected return on plan assets	(110)	(91)
	<u>35</u>	<u>55</u>

The actual return on plan assets (taking into account all changes in the fair value of the plan assets excluding contributions paid and received) was a net income of HK\$287 million (2006: HK\$295 million).

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

	2007	2006
Discount rate	3.45%	4.00%
Expected rate of return on plan assets	6.50%	6.50%
Future salary increases	4.50%	4.50%

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

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

	2007	2006
Equities	53%	53%
Bonds	43%	43%
Cash	4%	4%
	100%	100%
	100%	100%

30 Subordinated liabilities

	<i>Consolidated and Bank</i>	
	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
HK\$670 million (2006: HK\$625 million) Floating Rate Step-Up Notes 2014 ⁽¹⁾	670	624
HK\$500 million 3.5% Fixed/Floating Rate Step-Up Notes 2014 ⁽²⁾	496	489
US\$350 million 4.375% Fixed/Floating Rate Step-Up Notes 2014 ⁽³⁾	2,735	2,643
US\$300 million Floating Rate Step-Up Notes 2017 ⁽⁴⁾	2,333	—
	6,234	3,756
	6,234	3,756

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

- (1) Interest rate at three month HIBOR plus 0.37 per cent, payable quarterly, to the call option date on 4 December 2009. Thereafter, it will be reset to three-month HIBOR plus 0.87 per cent, payable quarterly.
- (2) Interest rate at 3.5 per cent per annum, payable semi-annually, to the call option date on 4 December 2009. Thereafter, it will be reset to three-month HIBOR plus 0.87 per cent, payable quarterly.
- (3) Interest rate at 4.375 per cent per annum, payable semi-annually, to the call option date on 4 December 2009. Thereafter, it will be reset to three-month US dollar LIBOR plus 0.86 per cent, payable quarterly.
- (4) Interest rate at three-month US dollar LIBOR plus 0.25 per cent, payable quarterly, to the call option date on 13 April 2012. Thereafter, it will be reset to three-month US dollar LIBOR plus 0.75 per cent, payable quarterly.

31 Share capital

	2007		2006	
	No. of shares in million	HK\$'M	No. of shares in million	HK\$'M
Authorised, issued and fully paid:				
'A' ordinary shares of HK\$0.05 each	706	35	780	39
'B' ordinary shares of HK\$0.05 each	1,231	62	1,231	62
	<u>1,937</u>	<u>97</u>	<u>2,011</u>	<u>101</u>
Preference shares of HK\$1.00 each	–	–	3,800	3,800
	<u>1,937</u>	<u>97</u>	<u>5,811</u>	<u>3,901</u>

- (i) The preference shares bear a non-cumulative preferential dividend at a rate of 8.25% per annum on their nominal amount and rank in priority to the 'A' ordinary shares and the 'B' ordinary shares with respect to the payment of dividends and any return of capital. The 'B' ordinary shares rank in priority to the 'A' ordinary shares with respect to any return of capital.
- (ii) During the year ended 31 December 2007, the Bank repurchased 3,800 million of its own non-cumulative preference shares and 74 million of its 'A' ordinary shares.

32 Reserves**(a) Consolidated**

	Share premium	Capital redemption reserve	Property revaluation reserve	Cash flow hedge reserve	Available-for-sale investment reserve	Pension reserve	Exchange reserve	Retained profits	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
At 1 January 2007	12,477	–	3	(4)	97	130	34	13,212	25,949
Available-for-sale securities:									
– changes in fair value	–	–	–	–	1,518	–	–	–	1,518
– transfer to income statement on disposal (note 5)	–	–	–	–	(238)	–	–	–	(238)
– deferred tax charged (note 26)	–	–	–	–	(392)	–	–	–	(392)
Cash flow hedge:									
– effective portion of changes in fair value	–	–	–	48	–	–	–	–	48
– deferred tax charged (note 26)	–	–	–	(8)	–	–	–	–	(8)
Capitalisation of reserve	–	3,804	–	–	–	–	–	(7,020)	(3,216)
Exchange differences	–	–	–	–	–	–	70	–	70
Transfer of reserve	–	–	(3)	–	–	–	–	3	–
Actuarial gains on defined benefits plan (note 29(d))	–	–	–	–	–	7	–	–	7
Tax on actuarial gains on defined benefits plan (note 26)	–	–	–	–	–	4	–	–	4
Dividend paid	–	–	–	–	–	–	–	(1,181)	(1,181)
Profit for the year attributable to shareholders	–	–	–	–	–	–	–	7,368	7,368
At 31 December 2007	<u>12,477</u>	<u>3,804</u>	<u>–</u>	<u>36</u>	<u>985</u>	<u>141</u>	<u>104</u>	<u>12,382</u>	<u>29,929</u>

	Share premium HK\$'M	Property revaluation reserve HK\$'M	Cash flow hedge reserve HK\$'M	Available- for-sale investment reserve HK\$'M	Pension reserve HK\$'M	Exchange reserve HK\$'M	Retained profits HK\$'M	Total HK\$'M
At 1 January 2006	12,477	3	(44)	(86)	(31)	–	7,186	19,505
Available-for-sale securities:								
– changes in fair value	–	–	–	236	–	–	–	236
– transfer to income statement on disposal (note 5)	–	–	–	(22)	–	–	–	(22)
– deferred tax charged (note 26)	–	–	–	(31)	–	–	–	(31)
Cash flow hedge:								
– effective portion of changes in fair value	–	–	48	–	–	–	–	48
– deferred tax charged (note 26)	–	–	(8)	–	–	–	–	(8)
Exchange differences	–	–	–	–	–	34	–	34
Actuarial gains on defined benefits plan (note 29(d))	–	–	–	–	195	–	–	195
Tax on actuarial gains on defined benefits plan (note 26)	–	–	–	–	(34)	–	–	(34)
Profit for the year attributable to shareholders	–	–	–	–	–	–	6,026	6,026
At 31 December 2006	12,477	3	(4)	97	130	34	13,212	25,949

(b) Bank

	Share premium HK\$'M	Capital redemption reserve HK\$'M	Property revaluation reserve HK\$'M	Cash flow hedge reserve HK\$'M	Available- for-sale investment reserve HK\$'M	Pension reserve HK\$'M	Retained profits HK\$'M	Total HK\$'M
At 1 January 2007	12,477	–	3	(4)	98	130	13,261	25,965
Available-for-sale securities:								
– changes in fair value	–	–	–	–	189	–	–	189
– transfer to income statement on disposal	–	–	–	–	(238)	–	–	(238)
– deferred tax credited (note 26)	–	–	–	–	6	–	–	6
Cash flow hedge:								
– effective portion of changes in fair value	–	–	–	48	–	–	–	48
– deferred tax charged (note 26)	–	–	–	(8)	–	–	–	(8)
Capitalisation of reserve	–	3,804	–	–	–	–	(7,020)	(3,216)
Transfer of reserve	–	–	(3)	–	–	–	3	–
Actuarial gains on defined benefits plan	–	–	–	–	–	7	–	7
Tax on actuarial gains on defined benefits plan (note 26)	–	–	–	–	–	4	–	4
Dividend paid	–	–	–	–	–	–	(1,181)	(1,181)
Profit for the year attributable to shareholders	–	–	–	–	–	–	7,444	7,444
At 31 December 2007	12,477	3,804	–	36	55	141	12,507	29,020

	Share premium HK\$'M	Property revaluation reserve HK\$'M	Cash flow hedge reserve HK\$'M	Available- for-sale investment reserve HK\$'M	Pension reserve HK\$'M	Retained profits HK\$'M	Total HK\$'M
At 1 January 2006	12,477	3	(44)	(86)	(31)	7,193	19,512
Available-for-sale securities:							
– changes in fair value	–	–	–	237	–	–	237
– transfer to income statement on disposal	–	–	–	(22)	–	–	(22)
– deferred tax charged (note 26)	–	–	–	(31)	–	–	(31)
Cash flow hedge:							
– effective portion of changes in fair value	–	–	48	–	–	–	48
– deferred tax charged (note 26)	–	–	(8)	–	–	–	(8)
Actuarial gains on defined benefits plan	–	–	–	–	195	–	195
Tax on actuarial gains on defined benefits plan (note 26)	–	–	–	–	(34)	–	(34)
Profit for the year attributable to shareholders	–	–	–	–	–	6,068	6,068
At 31 December 2006	<u>12,477</u>	<u>3</u>	<u>(4)</u>	<u>98</u>	<u>130</u>	<u>13,261</u>	<u>25,965</u>

The consolidated profit attributable to equity shareholders of the Bank includes a profit of HK\$7,444 million (2006: HK\$6,068 million) which has been dealt with in the financial statements of the Bank.

During the year ended 31 December 2007, the Bank repurchased 3,800 million of its own non-cumulative preference shares and 74 million of its ordinary 'A' shares at a total consideration of HK\$7,020 million. A capital redemption reserve of HK\$3,804 million was recorded and the premium paid on the repurchase of the shares of HK\$7,020 million was charged to retained profits.

During the year ended 31 December 2007, the directors had declared and paid a special dividend of HK\$0.61 per each 'A' and 'B' ordinary share (2006: HK\$ Nil) totalling HK\$1,181 million.

Subsequent to 31 December 2007, the directors have further declared and paid a special dividend of HK\$0.60 per each 'A' and 'B' ordinary share totalling HK\$1,162 million.

(c) Nature and purpose of reserves**(i) Share premium**

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

(ii) Capital redemption reserve

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

(iii) Available-for-sale investment reserve

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

(iv) Cash flow hedge reserve

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

(v) Pension reserve

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

(vi) Exchange reserve

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

The HKMA requires the Bank to maintain a minimum level of impairment allowances which is in excess of the impairment allowances required under Hong Kong Financial Reporting Standards. Of the retained earnings as at 31 December 2007, an amount of HK\$914 million (2006: HK\$552 million) has been reserved for this purpose.

(d) Minority interests

	<i>Consolidated</i>	
	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
At 1 January	51	51
Profit for the year	2	–
Disposal of a subsidiary	(53)	–
	<hr/>	<hr/>
At 31 December	<hr/> <hr/> –	<hr/> <hr/> 51

33 Cash and cash equivalents

	2007 HK\$'M	2006 HK\$'M (restated)
(a) Components of cash and cash equivalents in the cash flow statement		
Cash and balances with banks and other financial institutions	8,077	7,333
Trading assets with original maturity within three months	1,305	5,088
Placements with banks and other financial institutions with original maturity within three months	83,108	31,753
Investment securities with original maturity within three months	4,178	4,912
Amounts due from immediate holding company and fellow subsidiaries with original maturity within three months	23,438	22,874
	<u>120,106</u>	<u>71,960</u>
	2007 HK\$'M	2006 HK\$'M
(b) Reconciliation with the consolidated balance sheet		
Cash and balances with banks and other financial institutions	8,113	7,809
Placements with banks and other financial institutions	114,827	49,122
Trading securities	23,855	20,238
Investment securities	49,929	57,140
Amounts due from immediate holding company and fellow subsidiaries	66,430	50,040
Overdrafts included in "deposits and balances of banks and other financial institutions"	(36)	(476)
Overdrafts included in "amounts due to immediate holding company"	(461)	(282)
	<u>262,657</u>	<u>183,591</u>
Less: amounts with an original maturity of beyond three months	(142,551)	(111,631)
	<u>120,106</u>	<u>71,960</u>
Cash and cash equivalents in the consolidated cash flow statement	<u>120,106</u>	<u>71,960</u>

(c) Disposal of a subsidiary

During the year, the Bank disposed 100% of its holding in a subsidiary. The details of assets and liabilities disposed and the disposal consideration are as follows:

	2007 HK\$'M	2006 HK\$'M
Net proceeds from disposal (discharged by cash)	55	—
– Trading assets	1	—
– Advances to customers	530	—
– Amount due from immediate holding company	2	—
– Other assets	3	—
– Amounts due to immediate holding company	(400)	—
– Deferred tax liabilities	(24)	—
– Current tax liabilities	2	—
– Trading liabilities	(1)	—
– Other liabilities	(5)	—
– Minority interests	(53)	—
Net assets disposed	55	—
Gain on disposal	—	—

34 Derivatives

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

(a) Notional amounts of derivatives

Derivatives are contracts whose value depends on the value of one or more underlying financial instruments, interest or exchange rates or indices. The notional amounts of these instruments indicate the volume of transactions outstanding and do not represent amounts at risk.

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

Consolidated

	2007			
	<i>Qualifying for hedge accounting HK\$'M</i>	<i>Managed in conjunction with financial instruments designated at fair value through profit or loss HK\$'M</i>	<i>Others, including held for trading HK\$'M</i>	<i>Total HK\$'M</i>
Exchange rate contracts				
Forwards	–	114	423,012	423,126
Cross currency swaps	–	–	–	–
Options purchased	–	185,321	–	185,321
Options written	–	184,368	–	184,368
Interest rate contracts				
Forwards	–	6,578	–	6,578
Swaps	12,395	19,508	58	31,961
Options purchased	–	336	–	336
Options written	–	864	–	864
Other derivatives	–	144	–	144
	<u>12,395</u>	<u>397,233</u>	<u>423,070</u>	<u>832,698</u>
2006				
Exchange rate contracts				
Forwards	–	814	443,889	444,703
Cross currency swaps	–	523	–	523
Options purchased	–	7,082	–	7,082
Options written	–	7,082	–	7,082
Interest rate contracts				
Forwards	–	2,075	–	2,075
Swaps	14,722	25,419	334	40,475
Options purchased	–	3,029	–	3,029
Options written	–	3,029	–	3,029
Other derivatives	–	135	–	135
	<u>14,722</u>	<u>49,188</u>	<u>444,223</u>	<u>508,133</u>

Bank

	2007			
	Qualifying for hedge accounting HK\$'M	Managed in conjunction with financial instruments designated at fair value through profit or loss HK\$'M	Others, including held for trading HK\$'M	Total HK\$'M
Exchange rate contracts				
Forwards	–	114	423,012	423,126
Cross currency swaps	–	–	–	–
Options purchased	–	185,321	–	185,321
Options written	–	184,368	–	184,368
Interest rate contracts				
Forwards	–	6,578	–	6,578
Swaps	12,395	19,508	58	31,961
Options purchased	–	336	–	336
Options written	–	864	–	864
Other derivatives				
	–	144	–	144
	<u>12,395</u>	<u>397,233</u>	<u>423,070</u>	<u>832,698</u>
2006				
Exchange rate contracts				
Forwards	–	814	443,889	444,703
Cross currency swaps	–	523	–	523
Options purchased	–	7,082	–	7,082
Options written	–	7,082	–	7,082
Interest rate contracts				
Forwards	–	2,075	–	2,075
Swaps	14,722	24,968	334	40,024
Options purchased	–	3,029	–	3,029
Options written	–	3,029	–	3,029
Other derivatives				
	–	135	–	135
	<u>14,722</u>	<u>48,737</u>	<u>444,223</u>	<u>507,682</u>

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

	Consolidated					
	2007			2006		
	Fair value assets HK\$'M	Fair value liabilities HK\$'M	Credit risk weighted amount HK\$'M	Fair value assets HK\$'M	Fair value liabilities HK\$'M	Credit risk weighted amount HK\$'M
Exchange rate contracts	2,141	1,744	4,449	3,680	3,649	1,818
Interest rate contracts	170	168	255	355	444	385
Other derivatives	3	5	–	1	1	9
	<u>2,314</u>	<u>1,917</u>	<u>4,704</u>	<u>4,036</u>	<u>4,094</u>	<u>2,212</u>

	Bank					
	2007			2006		
	Fair value assets HK\$'M	Fair value liabilities HK\$'M	Credit risk weighted amount HK\$'M	Fair value assets HK\$'M	Fair value liabilities HK\$'M	Credit risk weighted amount HK\$'M
Exchange rate contracts	2,141	1,744	4,449	3,680	3,649	1,818
Interest rate contracts	170	168	255	354	443	385
Other derivatives	3	5	–	1	1	9
	<u>2,314</u>	<u>1,917</u>	<u>4,704</u>	<u>4,035</u>	<u>4,093</u>	<u>2,212</u>

Credit risk weighted amount refers to the amount as computed in accordance with the Banking (Capital) Rules issued by the HKMA which became effective on 1 January 2007. The corresponding amounts as at 31 December 2006 have been recalculated in accordance with the Banking (Capital) Rules. The amount calculated is dependent upon the status of the counterparty and maturity characteristics of each type of contract.

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

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

The following is a summary of the fair values of derivatives held for hedging purposes by product type entered into by the Bank and its subsidiaries as at 31 December 2007:

	<i>Consolidated and Bank</i>	
	<i>Assets</i>	<i>Liabilities</i>
	<i>(Included in Other assets)</i>	<i>(Included in Other liabilities)</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Interest rate contracts	63	15

The following is a summary of the fair values of derivatives held for hedging purposes by product type entered into by the Bank and its subsidiaries as at 31 December 2006:

	<i>Consolidated and Bank</i>	
	<i>Assets</i>	<i>Liabilities</i>
	<i>(Included in Other assets)</i>	<i>(Included in Other liabilities)</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Interest rate contracts	35	126

Fair value hedges

The fair value hedges principally consist of interest rate swaps that are used to protect against changes in the fair value of certain fixed rate liabilities due to movements in market interest rates. At 31 December 2007, the net fair value of interest rate swaps held as fair value hedges was HK\$5 million (2006: HK\$85 million) comprising assets of HK\$8 million (2006: HK\$ Nil) and liabilities of HK\$3 million (2006: HK\$85 million). The gains on the hedging instruments were HK\$90 million (2006: HK\$10 million). The losses on the hedged item attributable to the hedged risk were HK\$90 million (2006: HK\$10 million).

Cash flow hedges

The cash flow hedges principally consist of interest rate swaps that are used to hedge against the variability in cash flows of certain floating rate assets or liabilities. At 31 December 2007, the net fair value of interest rate swaps held as cash flow hedges was HK\$43 million (2006: HK\$6 million) comprising assets of HK\$55 million (2006: HK\$35 million) and liabilities of HK\$12 million (2006: HK\$41 million). The interest rate swaps will mature within 3 years (2006: 3 years) from the balance sheet date. During the year, there was no ineffectiveness recognised in the income statement that arose from cash flow hedges (2006: HK\$ Nil).

35 Contingent liabilities and commitments

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

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2007</i> <i>HK\$'M</i>	<i>2006</i> <i>HK\$'M</i>	<i>2007</i> <i>HK\$'M</i>	<i>2006</i> <i>HK\$'M</i>
Direct credit substitutes	12,219	28,153	12,219	28,153
Transaction-related contingencies	11,400	8,104	11,400	8,104
Trade-related contingencies	18,720	15,324	18,720	15,324
Forward asset purchases	144	12	144	12
Forward forward deposits placed	597	679	597	679
Other commitments:				
which are not unconditionally cancellable:				
with original maturity of not more than one year	2,206	4,285	2,206	4,285
with original maturity of more than one year	10,816	10,330	10,816	10,330
which are unconditionally cancellable	177,487	127,169	177,487	127,158
	<u>233,589</u>	<u>194,056</u>	<u>233,589</u>	<u>194,045</u>
Credit risk weighted amount	<u>19,124</u>	<u>26,234</u>	<u>19,124</u>	<u>26,234</u>

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

(b) Capital commitments

Capital commitments outstanding at 31 December not provided for in the financial statements were as follows:

	<i>Consolidated and Bank</i>	
	<i>2007</i> <i>HK\$'M</i>	<i>2006</i> <i>HK\$'M</i>
Contracted for	31	3
Authorised but not contracted for	63	21
	<u>94</u>	<u>24</u>

(c) Lease commitments

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

	<i>Consolidated and Bank</i>	
	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Within 1 year	397	371
After 1 year but within 5 years	751	631
After 5 years	2	85
	<u>1,150</u>	<u>1,087</u>

(d) Contingencies

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

36 Risk management**(a) Credit risk**

Credit risk arises from the possibility that the counterparty in a transaction may default. It arises from lending, trade finance, treasury and other activities. Credit exposures include both individual borrowers and groups of connected counterparties, and portfolios in the trading and non-trading books. The Bank has dedicated standards, policies and procedures to monitor and control credit risk.

The Bank has put in place a credit control structure and effective credit risk management tools to ensure proper management of the quality of its credit portfolio. The Bank's credit policies and procedures define credit extension criteria, credit approval authorities delegated from the Board, credit monitoring processes, the loan grading system and provisioning policy. It also takes into account the requirements of the Hong Kong Banking Ordinance and the guidelines issued by the HKMA with respect to large exposures and provisioning requirements. The Bank's policy is not to have significant concentrations of exposure to individual counterparties or individual overseas countries.

The Group Risk Committee ("GRC") has clear responsibility for credit risk. Standards are approved by the GRC, which oversees the delegation of credit authorities. The GRC's main responsibilities are to supervise and direct the management of credit, market, country, operational, compliance and reputational risk within the Standard Chartered Bank Group (the "SCB Group") and to ensure that processes and procedures are in place for the monitoring and control of risk to meet the standards set down in internal procedures and external regulatory requirements.

Procedures for managing credit risk are determined at the business levels, with specific policies and procedures being adapted to different risk environments and business goals. Risk officers are located in the businesses to maximise the efficiency of decision making, but have a reporting line which is separate from the business lines into the Group Chief Risk Officer.

The businesses working with the Risk Officer take responsibility for managing pricing for risk, portfolio diversification and overall asset quality within the requirements of Group standards, policies and business strategy.

Credit Approval

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

Risk Mitigation

Collateral types which are eligible for risk mitigation include cash, residential, commercial and industrial properties, marketable securities, commodities, and other assets such as aircrafts and plant and machinery in addition to bank guarantees and letters of credit.

Collateral is valued in accordance with the SCB Group's Risk Mitigation Policy, which prescribes the frequency of valuation for different collateral types. The frequency is driven by the level of price volatility in each class of collateral.

Collateral held against impaired loans is maintained at fair value. The valuation of collateral is monitored regularly and is backtested at least annually.

Concentration Risk

Concentration risk in the Wholesale Banking loan portfolio is managed through the Credit Issues Forum which is chaired by the Chief Risk Officer and comprises members of senior management from Credit and Business. Various concentration measures are evaluated including industry sector, geographical spread, credit rating and customer segment.

Concentration risk in Consumer Banking is managed within the exposure limits and concentration limits for each product segment.

Derivatives

In respect of credit risk arising from the use of derivatives, the group sets limits on net open positions. The amount of credit risk is the current positive fair value (asset) of the underlying contract together with potential exposures from future market movements. The credit risk is managed as part of the overall lending limits to banks and customers. The Bank further limits its exposure to credit losses in the event of default by entering into master netting agreements with certain market counterparties. As required by IAS 32, exposures are not presented net in these accounts as transactions are not usually settled on a net basis.

Where appropriate, derivatives are also used to reduce credit risks in the loan portfolios. Due to the income statement volatility which can result, derivatives are only used in a controlled manner and within a pre-defined volatility expectation.

Securities

Within the Wholesale Banking business, Markets & Institution Risk Management (“MIRM”) manages credit risk in respect of the Group’s debt securities portfolio.

Wholesale Banking

Credit risk is managed through a well laid out credit framework. This comprises locally adopted credit policies and processes, measurement of credit risk not just by nominal amount but also by expected loss, segregation of duties between originator of the deals and their approvers, independent large exposures’ controls and approvals by approvers with the right level of delegated authorities and portfolio reviews by the Risk Committee on a frequent basis.

An alphanumeric grading system is used for quantifying the risk associated with a counterparty. The grading is based on a probability of default measure, with customers analysed against a range of quantitative and qualitative measures. The numeric grades run from 1 to 14. Counterparties with lower credit grades are assessed as being less likely to default. An A to C scale is assigned to the original numeric rating scale, to enable more granular mapping of the probability of default, which results in more refined risk assessment, risk control and pricing. A counterparty with an A suffix has a lower probability of default than a counterparty with a C suffix. Credit grades 1A to credit grade 12C are assigned to performing customers while credit grades 13 and 14 are assigned to non-performing (or defaulted) customers.

There is no direct relationship between SCB internal credit grades and those used by external rating agencies. The SCB Group’s credit grades are not intended to replicate external credit grades, although as the factors used to grade a borrower are often similar, a borrower rated poorly by an external rating agency would be expected to be rated in the lower rank of the SCB Group’s internal credit grades.

In addition to nominal aggregate exposure, expected loss is used in the assessment of individual exposures and for portfolio analysis. Expected loss is the long-run average credit loss across a range of typical economic conditions. It is used in the delegation of credit approval authority and must be calculated for every transaction to determine the appropriate level of approval. Significant exposures are reviewed and approved centrally through the SCB Group or regional level credit committee. These committees derive their authority from GRC.

To assist risk officers in monitoring the portfolio, various internal risk management reports are available on a regular basis, providing individual counterparty, counterparty group and portfolio exposure information, credit grade migration information, the status of accounts showing signs of weakness or financial deterioration and updates on credit markets. Internal Ratings Based (‘IRB’) portfolio metrics are widely used.

Consumer Banking

Credit risk in Consumer Banking is also managed through a framework of policies and procedures. Standard credit application forms are generally used, which are processed in central units using largely automated approval processes. Where appropriate to the customer, the product or the market, a manual approval process is in place. As with Wholesale Banking, origination and approval roles are segregated.

Credit grades are based on a probability of default calculated using portfolio flow rates across delinquency buckets. Regular internal risk management reports typically contain information on key environmental and economic trends across major portfolios and countries, portfolio loan Impairment and delinquency performance.

Maximum exposure to credit risk

The maximum exposures to credit risk of balance sheet and off-balance sheet financial instruments, before taking account of any collateral or other credit enhancements, are as follows:

Consolidated

	2007 HK\$'M	2006 HK\$'M
Cash and balances with banks and other financial institutions	8,113	7,809
Placements with banks and other financial institutions	114,827	49,122
Hong Kong SAR Government certificates of indebtedness	22,321	20,261
Trading assets	26,106	24,239
Advances to customers	179,380	169,569
Amounts due from immediate holding company	48,890	38,099
Amounts due from fellow subsidiaries	17,540	11,941
Investment securities	49,929	57,140
Other assets	9,489	7,834
Financial guarantees and other credit related contingent liabilities	42,339	51,581
Loan commitments and other credit related commitments	13,763	15,306
	<u>532,697</u>	<u>452,901</u>

Bank

	2007 HK\$'M	2006 HK\$'M
Cash and balances with banks and other financial institutions	8,090	7,809
Placements with banks and other financial institutions	114,825	49,118
Hong Kong SAR Government certificates of indebtedness	22,321	20,261
Trading assets	26,106	24,238
Advances to customers	179,380	169,001
Amounts due from immediate holding company	48,889	38,098
Amounts due from fellow subsidiaries	17,532	11,937
Amounts due from subsidiaries	759	782
Investment securities	48,016	56,971
Other assets	9,451	7,753
Financial guarantees and other credit related contingent liabilities	42,339	51,581
Loan commitments and other credit related commitments	13,763	15,306
	<u>531,471</u>	<u>452,855</u>

For on-balance sheet instruments, the maximum exposure to credit risk is the carrying amount reported on the balance sheet. For off-balance sheet instruments, the maximum exposure to credit risk represents the contractual nominal amounts.

Credit quality

(i) *Analysis of the loan portfolio*

Consolidated

	2007		2006	
	<i>Advances to customers</i> HK\$'M	<i>Advances to banks</i> HK\$'M	<i>Advances to customers</i> HK\$'M	<i>Advances to banks</i> HK\$'M
Loans and advances				
– neither past due nor impaired	175,819	114,827	166,043	49,122
– past due but not impaired	3,301	–	3,209	–
– impaired, net of individually assessed impairment charges	588	–	668	–
Less: Collectively assessed impairment charges	(328)	–	(351)	–
	<u>179,380</u>	<u>114,827</u>	<u>169,569</u>	<u>49,122</u>
Fair value of collateral held against:				
– impaired advances	240	–	286	–
– past due but not impaired advances	2,282	–	9,709	–
	<u>2,522</u>	<u>–</u>	<u>10,000</u>	<u>–</u>

Bank

	2007		2006	
	<i>Advances to customers</i> HK\$'M	<i>Advances to banks</i> HK\$'M	<i>Advances to customers</i> HK\$'M	<i>Advances to banks</i> HK\$'M
Loans and advances				
– neither past due nor impaired	175,819	114,825	165,508	49,118
– past due but not impaired	3,301	–	3,176	–
– impaired, net of individually assessed impairment charges	588	–	668	–
Less: Collectively assessed impairment charges	(328)	–	(351)	–
	<u>179,380</u>	<u>114,825</u>	<u>169,001</u>	<u>49,118</u>
Fair value of collateral held against:				
– impaired advances	240	–	286	–
– past due but not impaired advances	2,282	–	9,709	–
	<u>2,522</u>	<u>–</u>	<u>10,000</u>	<u>–</u>

The following tables set out an analysis of the internal credit gradings for advances which are not past due and for which no individual impairment provision has been raised. The credit gradings set out in the tables below are based on a probability of default measure as set out on page 58.

Consolidated

	2007		2006	
	<i>Advances to customers</i> HK\$'M	<i>Advances to banks</i> HK\$'M	<i>Advances to customers</i> HK\$'M	<i>Advances to banks</i> HK\$'M
Credit grades:				
1 to 5	108,138	112,172	103,948	48,846
6 to 8	42,018	2,655	39,949	275
9 to 11	25,316	–	21,746	1
12	347	–	400	–
	<u>175,819</u>	<u>114,827</u>	<u>166,043</u>	<u>49,122</u>

Bank

	2007		2006	
	<i>Advances to customers</i> HK\$'M	<i>Advances to banks</i> HK\$'M	<i>Advances to customers</i> HK\$'M	<i>Advances to banks</i> HK\$'M
Credit grades:				
1 to 5	108,138	112,172	103,414	48,842
6 to 8	42,018	2,653	39,949	275
9 to 11	25,316	–	21,745	1
12	347	–	400	–
	<u>175,819</u>	<u>114,825</u>	<u>165,508</u>	<u>49,118</u>

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

Consolidated

	2007		2006	
	<i>Advances to customers</i> HK\$'M	<i>Advances to banks</i> HK\$'M	<i>Advances to customers</i> HK\$'M	<i>Advances to banks</i> HK\$'M
Past due				
– up to 30 days	2,867	–	2,697	–
– 31-60 days	277	–	342	–
– 61-90 days	96	–	125	–
– 91-120 days	25	–	27	–
– 121-150 days	36	–	18	–
	<u>3,301</u>	<u>–</u>	<u>3,199</u>	<u>–</u>

Bank

	2007		2006	
	Advances to customers HK\$'M	Advances to banks HK\$'M	Advances to customers HK\$'M	Advances to banks HK\$'M
Past due				
– up to 30 days	2,867	–	2,665	–
– 31-60 days	277	–	341	–
– 61-90 days	96	–	125	–
– 91-120 days	25	–	27	–
– 121-150 days	36	–	18	–

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

Consolidated

	2007			
	Treasury bills HK\$'M	Debt securities HK\$'M	Equity shares HK\$'M	Total HK\$'M
Impaired securities	–	43	6	49
Impairment provisions	–	(43)	(5)	(48)
Net impaired securities	–	–	1	1
Securities neither past due nor impaired	24,246	47,383	2,154	73,783

	2006			
	Treasury bills HK\$'M	Debt securities HK\$'M	Equity shares HK\$'M	Total HK\$'M
Impaired securities	–	–	5	5
Impairment provisions	–	–	(5)	(5)
Net impaired securities	–	–	–	–
Securities neither past due nor impaired	24,116	52,807	455	77,378

Bank

	2007			
	Treasury	Debt	Equity	Total
	bills	securities	shares	
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Impaired securities	–	43	6	49
Impairment provisions	–	(43)	(5)	(48)
Net impaired securities	–	–	1	1
Securities neither past due nor impaired	24,246	47,169	455	71,870

	2006			
	Treasury	Debt	Equity	Total
	bills	securities	shares	
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Impaired securities	–	–	5	5
Impairment provisions	–	–	(5)	(5)
Net impaired securities	–	–	–	–
Securities neither past due nor impaired	24,116	52,807	286	77,209

The following table analyses debt securities (including certificates of deposit) and treasury bills which are neither past due or impaired by external credit rating. The standard credit ratings used by the Bank are those used by Standard & Poors or their equivalent. Debt securities held which have a short-term rating are reported against the long-term rating of the issuer.

Consolidated

	2007		2006	
	Treasury	Debt	Treasury	Debt
	bills	securities	bills	securities
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
AAA	–	6,643	167	8,472
AA - to AA +	24,246	28,365	23,949	33,956
A - to A +	–	8,025	–	8,072
Lower than A-	–	2,034	–	2,124
Unrated	–	2,316	–	183
	24,246	47,383	24,116	52,807

Bank

	2007		2006	
	Treasury	Debt	Treasury	Debt
	bills	securities	bills	securities
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
AAA	–	6,643	167	8,472
AA - to AA +	24,246	28,365	23,949	33,956
A - to A +	–	8,025	–	8,072
Lower than A-	–	2,034	–	2,124
Unrated	–	2,102	–	183
	24,246	47,169	24,116	52,807

Reposessed Collateral

During the year, the Bank obtained assets by taking possession of collateral held as security, as follows:

	<i>Consolidated and Bank</i>	
	2007 HK\$'M	2006 HK\$'M
Property, plant and equipment	27	89
Others	–	1
	<u>27</u>	<u>90</u>

As at 31 December 2007, the reposessed assets amounted to HK\$7 million (2006: HK\$61 million).

Assets acquired in exchange for the release in full or in part of the obligations of the borrowers due to restructuring or the inability of borrowers to repay, continue to be recorded as “Advances to customers” in the balance sheet at the lower of fair value (less costs to sell) and the carrying amount of the loan (net of any impairment allowances), until the assets are realised.

Renegotiated loans

There were no renegotiated loans and advances to banks (2006: HK\$ Nil).

Renegotiated advances to customers which were neither past due nor impaired amounted to HK\$386 million (2006: HK\$564 million).

(b) Market risk

The Bank recognises market risk as the exposure created by potential changes in market prices and rates. The Bank is exposed to market risk arising principally from customer driven transactions. The objective of the Bank's market risk policies and processes is therefore to obtain the best balance of risk and return while meeting our customers' requirements.

The Bank transacts in the money market, foreign exchange markets and capital markets giving rise to market risk exposures. Financial instruments transacted include debt and other securities and certain off-balance sheet (“derivative”) financial instruments. Derivative instruments are contracts whose characteristics and value are derived from underlying financial instruments, interest and exchange rates or indices. They include futures, forwards, swaps, and options transactions in the foreign exchange and interest rate markets. The Bank only enters into derivative positions to meet customer demand or for hedging purposes. Derivative contracts entered into by the Bank are primarily over-the-counter derivatives.

The Bank has established market risk management policies and framework, including limits setting, monitoring and reporting and control procedures, which are reviewed regularly by the Risk Committee. Market risk limits are proposed by the business within the terms of the agreed policy. The Market Risk department approves the limits within delegated authorities and monitors exposures against these limits.

Value at Risk

The Bank measures the risk of losses arising from future potential adverse movements in interest rates and exchange rates, prices and volatilities using a Value at Risk ("VaR") methodology.

Historical simulation is used to measure VaR by applying actual historical market rate movements based on a one-day holding period and a 97.5% confidence level. Additional limits are placed on specific instruments and position concentrations where appropriate. Sensitivity measures are used in addition to VaR as part of the overall risk management tools. For example, interest rate sensitivity is measured in terms of exposure to a +0.01% increase in yields.

The Bank recognises that there are limitations to the VaR methodology including the possibility that the historical data may not be the best proxy for future price movements.

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

VaR is complemented by regular stress tests on market risk exposures to highlight potential risk that may arise from extreme market events that are rare but plausible. Stress testing is an integral part of the market risk management framework and considers both historical market events and forward looking scenarios. A consistent stress testing methodology is applied to trading and non-trading books. Ad hoc scenarios are also prepared reflecting specific market conditions. Stress scenarios are regularly updated to reflect changes in risk profile and economic events. The Risk Committee reviews stress test results on a regular basis.

Total Trading and Non-trading

Value at risk (HK\$'M):	2007				2006			
	Average	High	Low	Actual [^]	Average	High	Low	Actual [^]
Interest rate risk	29.1	36.8	24.3	35.4	33.4	45.4	24.2	24.2
Foreign exchange risk	1.1	3.5	0.2	0.9	1.5	4.3	0.3	0.3
Total*	29.2	37.1	24.4	35.5	33.5	44.8	24.1	24.1

Trading

Value at risk (HK\$'M):	2007				2006			
	Average	High	Low	Actual [^]	Average	High	Low	Actual [^]
Interest rate risk	10.7	15.5	5.7	8.1	10.4	20.0	5.0	5.0
Foreign exchange risk	1.1	3.5	0.2	0.9	1.5	4.3	0.3	0.3
Total *	10.7	16.0	5.5	8.2	10.5	19.3	4.8	5.0

* The total trading book VaR shown in the table above is not a sum of the component risks due to offsets between them.

[^] This represents the actual one day VaR as at 31 December.

	2007 HK\$'M	2006 HK\$'M
<i>The average daily income earned from market risk related activities is as follows:</i>		
Interest rate risk	0.9	0.2
Foreign exchange risk	4.5	2.4
Total	<u>5.4</u>	<u>2.6</u>

Non-trading

Value at risk (HK\$'M):

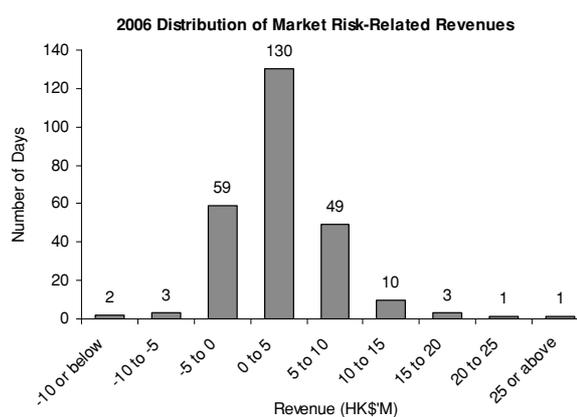
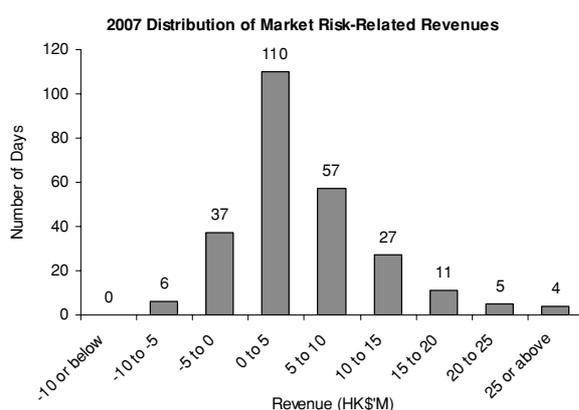
	2007				2006			
	Average	High	Low	Actual ^	Average	High	Low	Actual ^
Interest rate risk	<u>20.4</u>	<u>25.7</u>	<u>17.4</u>	<u>25.7</u>	<u>24.0</u>	<u>28.0</u>	<u>19.9</u>	<u>19.9</u>

	2007 HK\$'M	2006 HK\$'M
<i>The average daily income earned from non-trading market risk related activities is as follows:</i>		
Interest rate risk	<u>2.1</u>	<u>1.8</u>

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

Structural FX risks are not included within the VaR and arise from net investments in non-HKD currency entities. These are managed separately under ALCO by Group Treasury.

An analysis of the daily distribution of market risk-related revenues is as follows:



(c) Foreign exchange risk

The Bank's foreign exchange positions arise from foreign exchange trading and commercial banking operations. Foreign exchange trading exposures are principally derived from customer driven transactions. Market Risk department approves foreign exchange limits within delegated authorities and monitors exposures against these limits. The Bank's application in using VaR methodology for measuring and monitoring foreign exchange risk is discussed under "Market Risk".

(d) Interest rate risk

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

The Bank has established principles, policies and techniques for managing interest rate risk. Interest rate risk management is governed by the Asset and Liability Committee ("ALCO"). The Bank's application in using VaR methodology for measuring and monitoring interest rate risk is discussed under "Market Risk".

(e) Liquidity risk

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

The Bank has established principles, policies and techniques for managing liquidity risk. Liquidity risk management is governed by the ALCO. The tools used for the management of liquidity risk, range from key balance sheet ratios and medium-term funding requirements to ensure balance sheets are not developing structural imbalances, to short term cash flow limits and controls on borrowing in the wholesale markets. They are supplemented by the establishment of a liquidity crisis contingency plan and regular stress test on liquidity positions.

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

Customer deposits form a significant part of the Bank's overall funding. Its composition has remained relatively diversified and stable. Professional markets are accessed for the purposes of providing additional funding, maintaining a presence in local money markets and optimising asset and liability maturities.

(i) Analysis of assets and liabilities by remaining maturity

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

Consolidated

	2007						Undated HK\$'M	Total HK\$'M
	Repayable on demand HK\$'M	Due within 1 month HK\$'M	Due between 1 month to 3 months HK\$'M	Due between 3 months to 1 year HK\$'M	Due between 1 year to 5 years HK\$'M	Due after 5 years HK\$'M		
Assets								
Cash and balances with banks and other financial institutions	8,113	–	–	–	–	–	–	8,113
Placements with banks and other financial institutions	190	89,650	19,781	5,088	118	–	–	114,827
Hong Kong SAR Government certificates of indebtedness	–	–	–	–	–	–	22,321	22,321
Trading assets	–	1,148	6,637	11,106	6,106	1,109	–	26,106
Advances to customers	6,108	38,801	21,994	17,293	31,490	64,600	(906)	179,380
Investment securities	409	7,010	12,303	18,779	6,687	2,586	2,155	49,929
Amounts due from group companies	7,453	20,717	25,354	9,195	3,711	–	–	66,430
Others	88	6,161	2,384	311	222	–	5,454	14,620
Total Assets	22,361	163,487	88,453	61,772	48,334	68,295	29,024	481,726
Liabilities								
Hong Kong SAR currency notes in circulation	–	–	–	–	–	–	22,321	22,321
Deposits and balances of banks and other financial institutions	9,134	6,876	15	12	–	–	–	16,037
Deposits from customers	199,456	8,545	143,848	6,684	51	–	–	358,584
Trading liabilities	–	4,857	5,248	4,558	2,130	1,156	–	17,949
Financial liabilities designated at fair value	–	723	799	1,012	1,700	205	–	4,439
Debt securities in issue	–	–	210	1,138	30	922	–	2,300
Amounts due to group companies	3,051	3,962	20	49	278	16	–	7,376
Subordinated liabilities	–	–	–	–	–	6,234	–	6,234
Others	5,760	5,699	1,068	885	471	–	2,577	16,460
Total Liabilities	217,401	30,662	151,208	14,338	4,660	8,533	24,898	451,700

Consolidated

	2006							Total HK\$'M
	Repayable on demand HK\$'M	Due	Due	Due	Due	Due	Undated HK\$'M	
		within 1 month HK\$'M	between 1 month to 3 months HK\$'M	between 3 months to 1 year HK\$'M	between 1 year to 5 years HK\$'M	between 5 years after 5 years HK\$'M		
Assets								
Cash and balances with banks and other financial institutions	7,809	–	–	–	–	–	–	7,809
Placements with banks and other financial institutions	1,000	34,823	8,886	4,413	–	–	–	49,122
Hong Kong SAR Government certificates of indebtedness	–	–	–	–	–	–	20,261	20,261
Trading assets	–	2,773	4,384	12,117	4,121	844	–	24,239
Advances to customers	6,474	24,474	31,924	15,202	33,188	59,882	(1,575)	169,569
Investment securities	–	7,333	13,663	22,780	10,720	2,189	455	57,140
Amounts due from group companies	2,822	31,525	4,918	9,583	1,192	–	–	50,040
Others	2	4,550	2,586	317	124	1	5,282	12,862
Total Assets	18,107	105,478	66,361	64,412	49,345	62,916	24,423	391,042
Liabilities								
Hong Kong SAR currency notes in circulation	–	–	–	–	–	–	20,261	20,261
Deposits and balances of banks and other financial institutions	6,153	1,073	165	123	–	–	–	7,514
Deposits from customers	150,690	101,281	28,207	8,069	68	198	–	288,513
Trading liabilities	–	2,634	2,827	8,304	1,398	691	–	15,854
Financial liabilities designated at fair value	–	265	1,013	5,749	2,226	261	–	9,514
Debt securities in issue	–	101	5	1,193	1,378	30	–	2,707
Amounts due to group companies	1,398	1,209	169	22	370	20	–	3,188
Subordinated liabilities	–	–	–	–	–	3,756	–	3,756
Others	3,096	1,405	1,226	976	23	–	3,108	9,834
Total Liabilities	161,337	107,968	33,612	24,436	5,463	4,956	23,369	361,141

Bank

	2007							Total HK\$'M
	Repayable on demand HK\$'M	Due	Due	Due	Due	Due	Undated HK\$'M	
		within 1 month HK\$'M	between 1 month to 3 months HK\$'M	between 3 months to 1 year HK\$'M	between 1 year to 5 years HK\$'M	between 5 years after 5 years HK\$'M		
Assets								
Cash and balances with banks and other financial institutions	8,090	–	–	–	–	–	–	8,090
Placements with banks and other financial institutions	188	89,650	19,781	5,088	118	–	–	114,825
Hong Kong SAR Government certificates of indebtedness	–	–	–	–	–	–	22,321	22,321
Trading assets	–	1,148	6,637	11,106	6,106	1,109	–	26,106
Advances to customers	6,108	38,801	21,994	17,293	31,490	64,600	(906)	179,380
Investment securities	409	7,010	12,303	18,779	6,473	2,586	456	48,016
Amounts due from group companies	7,506	20,717	25,354	9,892	3,711	–	–	67,180
Others	88	6,157	2,384	306	195	–	5,639	14,769
Total Assets	22,389	163,483	88,453	62,464	48,093	68,295	27,510	480,687
Liabilities								
Hong Kong SAR currency notes in circulation	–	–	–	–	–	–	22,321	22,321
Deposits and balances of banks and other financial institutions	9,134	6,876	15	12	–	–	–	16,037
Deposits from customers	199,456	8,545	143,848	6,684	51	–	–	358,584
Trading liabilities	–	4,857	5,248	4,558	2,130	1,156	–	17,949
Financial liabilities designated at fair value	–	723	799	1,012	1,700	205	–	4,439
Debt securities in issue	–	–	210	1,138	30	922	–	2,300
Amounts due to group companies	3,373	3,962	20	49	278	–	–	7,682
Subordinated liabilities	–	–	–	–	–	6,234	–	6,234
Others	5,760	5,679	1,068	886	73	–	2,558	16,024
Total Liabilities	217,723	30,642	151,208	14,339	4,262	8,517	24,879	451,570

Bank

	2006							Total HK\$'M
	Repayable on demand HK\$'M	Due within 1 month HK\$'M	Due between 1 month to 3 months HK\$'M	Due between 3 months to 1 year HK\$'M	Due between 1 year to 5 years HK\$'M	Due after 5 years HK\$'M	Undated HK\$'M	
Assets								
Cash and balances with banks and other financial institutions	7,809	–	–	–	–	–	–	7,809
Placements with banks and other financial institutions	996	34,823	8,886	4,413	–	–	–	49,118
Hong Kong SAR Government certificates of indebtedness	–	–	–	–	–	–	20,261	20,261
Trading assets	–	2,773	4,383	12,117	4,121	844	–	24,238
Advances to customers	6,474	24,451	31,879	15,022	32,868	59,882	(1,575)	169,001
Investment securities	–	7,333	13,663	22,780	10,720	2,189	286	56,971
Amounts due from group companies	2,823	32,302	4,917	9,583	1,192	–	–	50,817
Others	2	4,550	2,574	317	55	1	5,531	13,030
Total Assets	18,104	106,232	66,302	64,232	48,956	62,916	24,503	391,245
Liabilities								
Hong Kong SAR currency notes in circulation	–	–	–	–	–	–	20,261	20,261
Deposits and balances of banks and other financial institutions	6,153	1,073	165	123	–	–	–	7,514
Deposits from customers	150,690	101,281	28,207	8,069	68	198	–	288,513
Trading liabilities	–	2,633	2,827	8,304	1,398	691	–	15,853
Financial liabilities designated at fair value	–	265	1,013	5,749	2,226	261	–	9,514
Debt securities in issue	–	101	5	1,193	1,378	30	–	2,707
Amounts due to group companies	1,381	1,593	169	17	296	16	–	3,472
Subordinated liabilities	–	–	–	–	–	3,756	–	3,756
Others	3,096	1,396	1,227	974	–	–	3,096	9,789
Total Liabilities	161,320	108,342	33,613	24,429	5,366	4,952	23,357	361,379

(f) Operational risk

Operational risk is the risk of direct or indirect loss due to an event or action resulting from the failure of internal processes, people, and systems, or from external events. The Bank seeks to ensure that key operational risks are managed in a timely and effective manner through a framework of policies, procedures and tools to identify, assess, monitor, control, and report such risks.

The Country Operational Risk Group ("CORG") has been established to supervise and direct the management of operational risks across the Bank. CORG is also responsible for ensuring adequate and appropriate policies and procedures are in place for the identification, assessment, monitoring, control and reporting of operational risks.

An operational risk function, independent from the businesses is responsible for establishing and maintaining the overall operational risk framework, and for monitoring the Bank's key operational risk exposures. This unit is supported by Wholesale Banking and Consumer Banking Operational Risk units. These units are responsible for ensuring compliance with policies and procedures in the business, monitoring key operational risk exposures, and the provision of guidance to the respective business areas on operational risk.

Compliance with operational risk policies and procedures is the responsibility of all managers. The CORG has in-country governance responsibility for ensuring that an appropriate and robust risk management framework is in place to monitor and manage operational risk.

(g) Capital management

The HKMA sets and monitors capital requirements for the Bank and certain of its subsidiaries specified by the HKMA. In implementing current capital requirements, the HKMA requires the Bank to maintain a prescribed ratio of total capital to total risk-weighted assets. The Bank calculated its consolidated capital adequacy ratios as at 31 December 2007 in accordance with the Banking (Capital) Rules of the Hong Kong Banking Ordinance which became effective on 1 January 2007 and the capital ratios as at 31 December 2006 have been recalculated in accordance with the Capital Rules.

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

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

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

The Bank and its individually regulated subsidiary have complied with all externally imposed capital requirements throughout the years ended 31 December 2007 and 2006 .

37 Fair value information

(a) Estimation of fair values

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 and deposits, direct market prices are not available, the fair value of such instruments was therefore calculated on the basis of 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.

These techniques involve uncertainties and are significantly affected by the assumptions used and judgements made regarding risk characteristics of various financial instruments, discount rates, estimates of future cash flows, future expected loss experiences and other factors. Changes in assumptions could significantly affect these estimates and the resulting fair values. Derived fair value estimates cannot necessarily be substantiated by comparison to independent markets and, in many cases, could not be realised in an immediate sale of the instruments.

(b) Fair value

All financial instruments are stated at fair value or carried at amounts not materially different from their fair values as at 31 December 2007 and 2006 unless otherwise stated.

(i) Financial assets

The Bank's financial assets mainly include cash, amounts due from banks and other financial institutions, loans and advances to customers, and investments.

Amounts due from banks and other financial institutions, loans and advances to customers

Amounts due from banks and other financial institutions and loans and advances to customers are mainly priced at market interest rates or mature within one year. Accordingly, the carrying values approximate the fair values.

Investments

Available-for-sale securities and trading securities are stated at fair value in the financial statements.

(ii) Financial liabilities

The Bank's financial liabilities mainly include amounts due to banks and other financial institutions, deposits from customers and debt securities in issue which are mainly priced at market rates or mature within one year. Accordingly, the carrying values approximate the fair values.

38 Assets pledged as security for liabilities

The Bank maintains pledged cash and securities accounts with financial institutions to secure any borrowings or other obligations resulting from the Bank's use of clearing systems and to cover short positions. As at 31 December 2007, the Bank did not have borrowings due to the financial institutions and had securities amounting to HK\$16,047 million (2006: HK\$11,886 million) to cover short positions.

39 Material related party transactions

In addition to the transactions and balances disclosed elsewhere in these financial statements, the Bank and its subsidiaries entered into the following material related party transactions. The transactions of the Bank are materially the same as for those appearing in the consolidated financial statements in 2007 and 2006.

(a) Key management personnel remuneration

Remuneration for key management personnel, including amounts paid to the Bank's directors as disclosed in note 7 is as follows:

	<i>Consolidated</i>	
	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Short-term employee benefits	69	87
Post-employment benefits	4	6
Equity compensation benefits	18	4
	<u>91</u>	<u>97</u>

Total remuneration is included in staff costs (see note 3(g)).

(b) Credit facilities and loans to key management personnel

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

	<i>Consolidated</i>	
	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Loan balances:		
At 1 January	<u>1,391</u>	<u>1,585</u>
At 31 December	<u>341</u>	<u>1,391</u>
Average balance during the year	<u>870</u>	<u>1,079</u>
Income earned	<u>38</u>	<u>50</u>

(c) Share based payments

The Standard Chartered PLC Group (the "Group") operates a number of share based payment schemes for its directors and employees in which the Bank's employees participate.

1997/2006 Restricted Share Scheme

The Group operates a discretionary Restricted Share Scheme for high performing and high potential staff at any level of the organisation whom the Group wish to motivate and retain. Except upon appointment when an executive director may be granted an award of restricted shares, the Restricted Share Scheme is not applicable to executive directors, as it has no performance conditions attached to it. Fifty per cent of the award vests two years after the date of grant and the balance after three years. The value of shares awarded in any year to any individual may not exceed two times their base salary.

2000 Executive Share Option Scheme

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

Executive share options to purchase ordinary shares in the Ultimate Holding Company are exercisable after the third, but before the tenth, anniversary of the date of grant. The exercise price per share is the share price at the date of grant and options can normally only be exercised if a performance condition is satisfied.

2001 Performance Share Plan

The Performance Share Plan is designed to be an intrinsic part of total remuneration for the Group's executive directors and for a small number of the group's most senior executives. It is an internationally competitive long-term incentive plan that focuses executives on meeting and exceeding the long-term performance targets of the Group. Awards of nil price options to acquire shares are granted to the individual and will normally be exercised between three and ten years after the date of grant if the individual is still employed by the Group. There is provision for earlier exercise in certain limited circumstances.

All Employee Sharesave Schemes

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

2004 Deferred Bonus Plan

Under the 2004 Deferred Bonus Plan, shares are conditionally awarded instead of all or part of the executive directors' and certain senior executives' annual cash bonus.

1994 Executive Share Option Scheme (closed)

No awards have been made under this scheme since August 1999 as the scheme was replaced by the 2000 Executive Share Option Scheme. Executive share options to purchase ordinary shares in the Group are exercisable after the third, but before the tenth anniversary of the date of grant. The exercise price is the share price at the date of grant and options can only be exercised if EPS increases by at least 15 per cent over three consecutive years.

2000 Executive Share Option Scheme

No options under the 2000 Executive Share Option Scheme were granted in 2007 and 2006.

A reconciliation of option movements for the year ended 31 December 2007 is shown below:

	2007		2006	
	No. of shares	Weighted average exercise price	No. of shares	Weighted average exercise price
Outstanding at 1 January	2,919,609	£8.22	3,901,637	£8.03
Granted	—	—	—	—
Lapsed	(193,045)	£7.20	(22,997)	£9.36
Exercised	(1,221,614)	£8.54	(959,031)	£7.41
Outstanding at 31 December	1,504,950	£8.09	2,919,609	£8.22
Exercisable at 31 December	1,504,950	£8.09	2,246,119	£7.88

Range of exercise price	2007			2006		
	Weighted average exercise price	No. of shares	Weighted average contractual life	Weighted average exercise price	No. of shares	Weighted average contractual life
£6.905/£10.395	£8.09	1,504,950	4.5 years	£8.22	2,919,609	5.5 years

2001 Performance Share Plan

Valuation

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

Grant Date	2007		2006		
	17 September	12 March	12 September	11 May	14 March
Share price at grant date	£14.69	£14.51	£13.17	£14.60	£14.35
Shares granted	34,805	202,247	9,453	3,766	163,214
Vesting period (years)	3	3	3	3	3
Expected dividends (yield) (%)	2.9	2.8	3-3.2	3-3.2	3-3.2
Fair value (EPS) (£)	6.74	6.68	6.00	6.67	6.56
Fair value (TSR) (£)	2.92	2.89	2.60	2.89	2.84

The expected dividend yield is based on the historical dividend yield over the last three years or the three years prior to grant. The EPS and TSR fair value relates to certain performance criteria to be satisfied. The TSR fair value is derived by discounting 50 per cent of the award which is subject to the TSR condition by the loss of expected dividends over the performance period, and the likelihood of meeting the TSR condition which is calculated by the area under the TSR vesting schedule curve.

A reconciliation of movements for the year ended 31 December 2007 is shown below:

	2007	2006
	<i>No. of shares</i>	<i>No. of shares</i>
Outstanding at 1 January	382,618	342,968
Granted	237,052	176,433
Lapsed	(48,292)	(63,220)
Exercised	(100,617)	(73,563)
Outstanding at 31 December	470,761	382,618
Weighted average contractual life	8.5 years	8.1 years
Exercisable at 31 December	6,763	71,866

1997/2006 Restricted Share Scheme

Valuation

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

<i>Grant Date</i>	2007		2006	
	<i>17 September</i>	<i>12 March</i>	<i>12 September</i>	<i>14 March</i>
Share price at grant date	£14.69	£14.51	£13.17	£14.35
Shares granted	64,461	291,256	34,316	227,807
Vesting period (years)	2/3	2/3	2/3	2/3
Expected dividends (yield) (%)	2.9	2.8	3.2	3
Fair value (£)	13.49	13.36	12.00	13.12

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

A reconciliation of movements for the year ended 31 December 2007 is shown below:

	2007	2006
	<i>No. of shares</i>	<i>No. of shares</i>
Outstanding at 1 January	992,302	1,012,199
Granted	400,757	262,123
Lapsed	(102,478)	(41,276)
Exercised	(296,688)	(240,744)
Outstanding at 31 December	993,893	992,302
Weighted average contractual life	4.4 years	4.8 years
Exercisable at 31 December	299,570	293,214

2004 Sharesave

Valuation

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

Grant Date	2007	2006
	1 October	12 September
Share price at grant date	£15.88	£13.03
Exercise price	£12.43	£10.64
Shares granted	813,838	800,945
Vesting period (years)	3/5	3/5
Expected volatility (%)	21-24	20-29
Expected option life (years)	3.33/5.33	3.33/5.33
Risk free rate (%)	4.9-5.0	4.8-5.1
Expected dividends (yield) (%)	2.9-3.3	3-3.6
Fair value (£)	4.4-4.9	3.39-4.30

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

A reconciliation of option movements for the year ended 31 December 2007 is shown below:

	2007		2006	
	No. of shares	Weighted average exercise price	No. of shares	Weighted average exercise price
Outstanding at 1 January	1,863,709	£9.60	1,196,185	£8.82
Granted	813,838	£12.43	800,945	£10.64
Lapsed	(188,748)	£9.84	(128,906)	£8.86
Exercised	(318,744)	£7.45	(4,515)	£7.93
Outstanding at 31 December	2,170,055	£10.96	1,863,709	£9.60
Exercisable at 31 December	69,036	£7.43	–	–

Range of exercise price	2007			2006		
	Weighted average exercise price	No. of shares	Weighted average contractual life	Weighted average exercise price	No. of shares	Weighted average contractual life
£7.43/£10.64	–	–	–	£9.60	1,863,709	2.8 years
£7.43/£12.43	£10.96	2,170,055	2.7 years	–	–	–

2004 Deferred Bonus Plan

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

A reconciliation of share movements for the year ended 31 December 2007 and 2006 is shown below:

	<u>2007</u>	<u>2006</u>
	<i>No. of shares</i>	<i>No. of shares</i>
Outstanding at 1 January	14,506	–
Shares vested	(13,194)	–
Shares awarded	17,476	14,506
Shares lapsed	(1,423)	–
Outstanding at 31 December	17,365	14,506

1994 Executive Share Option Scheme

Awards made under this scheme are not subject to the valuation criteria of HKFRS 2 as all awards are granted prior to 7 November 2002 and are all vested as at that date.

A reconciliation of option movements for the year ended 31 December 2007 and 2006 is shown below:

	<u>2007</u>		<u>2006</u>	
	<i>No. of shares</i>	<i>Weighted average exercise price</i>	<i>No. of shares</i>	<i>Weighted average exercise price</i>
Outstanding at 1 January	106,365	£8.68	197,348	£7.89
Lapsed	(5,000)	£8.50	–	–
Exercised	(101,365)	£8.69	(90,983)	£6.97
Outstanding at 31 December	–	–	106,365	£8.68
Exercisable at 31 December	–	–	106,365	£8.68

	<u>2007</u>		<u>2006</u>	
<i>Range of exercise price</i>	<i>Weighted average exercise price</i>	<i>Weighted average contractual life</i>	<i>Weighted average exercise price</i>	<i>Weighted average contractual life</i>
£8.5/£8.88	–	–	–	–
£6.20/£8.88	–	–	£8.68	1.6 years

(d) Loans to officers

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

	2007 HK\$'M	2006 HK\$'M
Aggregate amount of relevant loans by the Bank outstanding at 31 December	<u>32</u>	<u>21</u>
Maximum aggregate amount of relevant loans by the Bank outstanding during the year	<u>46</u>	<u>25</u>

40 Ultimate holding company

The Bank's ultimate holding company is Standard Chartered PLC, a company registered in England and Wales. Standard Chartered PLC has dual primary listings on the London Stock Exchange and the Stock Exchange of Hong Kong.

41 Comparative figures

In 2007, interest relating to short positions in securities has been classified under interest expense in the consolidated income statement. An amount of HK\$299 million in respect of 2006 was therefore reclassified from interest income to interest expense to conform to the current year presentation. In 2007, certain income relating to the Global Markets business has been classified under fee and commission income in the consolidated income statement. An amount of HK\$573 million in respect of 2006 has therefore been reclassified from trading income to fee and commission income to conform to the current year presentation. These reclassifications provide a better reflection of the underlying transactions.

The 2006 consolidated cash flow statement has been restated to include debt securities with an original maturity within three months of HK\$10,000 million as cash and cash equivalents to better reflect the underlying nature of these securities. Previously these debt securities had been included as part of the Bank's and its subsidiaries' operating assets.

42 Changes in accounting policies

The IASB has issued a number of new and revised IFRSs and Interpretations that are first effective for the current accounting period commencing 1 January 2007 or are available for early adoption. The equivalent new and revised HKFRSs and Interpretations consequently issued by HKICPA have the same effective date as those issued by the IASB and are in all material respects identical to the pronouncements issued by the IASB. There have been no other material changes to HKFRSs.

These developments have not resulted in any significant changes to the accounting policies applied in these financial statements compared to those applied in the Bank and its subsidiaries' financial statements for the year ended 31 December 2006. However, as a result of the adoption of HKFRS 7, Financial instruments: Disclosures and the amendments to HKAS 1, Presentation of financial statements: Capital disclosures, these financial statements include certain additional disclosures which are explained as follows.

As a result of the adoption of HKFRS 7 (which is equivalent to IFRS 7), the financial statements include expanded disclosure about the significance of the Bank and its subsidiaries' financial instruments and the nature and extent of risks arising from those instruments, compared with the information previously required to be disclosed by HKAS 32, Financial instruments: Disclosure and presentation. These disclosures are provided throughout these financial statements.

The amendment to HKAS 1 (which is equivalent to the amendment to IAS 1) introduces additional disclosure requirements to provide information about the level of capital and the Bank's and its subsidiaries' objectives, policies and processes for managing capital. These new disclosures are set out in note 36(g).

Both HKFRS 7 and the amendments to HKAS 1 do not have any impact on the classification, recognition and measurement of the amounts recognized in the financial statements.

The Bank and its subsidiaries have not applied any new standard or interpretation that is not yet effective for the current accounting period.

43 Significant accounting estimates and judgements

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

Pensions

Actuarial assumptions are made in valuing future pension obligations as set out in note 29 and are updated periodically.

Taxes

Determining income tax provisions involves judgement on the future tax treatment of certain transactions. Deferred tax liabilities are recognised on all temporary differences and deferred tax assets are recognised on temporary differences where it is probable that there will be taxable revenue against which these can be offset.

Impairment of financial assets

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

44 Possible impact of amendments, new standards and interpretations issued but not yet effective for the annual accounting period ended 31 December 2007

Up to the date of issue of the financial statements, the IASB and HKICPA have issued a number of amendments, new standards and interpretations which are not yet effective for the accounting year ended 31 December 2007 and which have not been adopted in these financial statements.

The Bank and its subsidiaries are in the process of making an assessment of what the impact of these amendments, new standards and new interpretations is expected to be in the period of initial application.

So far, it has concluded that the adoption of them is unlikely to have a significant impact on the Bank and its subsidiaries' results of operations and financial positions.

In addition, HKFRS 8, Operating segments (which is equivalent to IFRS 8), which is effective for annual periods beginning on or after 1 January 2009, may result in new or amended disclosures in the financial statements.

Unaudited supplementary financial information

These notes set out on pages 84 to 97 are supplementary to and should be read in conjunction with the consolidated financial statements set out on pages 5 to 83. The consolidated financial statements and these unaudited supplementary financial information (“supplementary notes”) taken together comply with the Banking (Disclosure) Rules (“Rules”) made under section 60A of the Banking Ordinance.

Basis of preparation

- (i) Except where indicated otherwise, the financial information contained in these supplementary notes has been prepared on a consolidated basis in accordance with Hong Kong Financial Reporting Standards. Some parts of these supplementary notes, however, are required by the Rules to be prepared on a different basis. In such cases, the Rules require that certain information is prepared on a basis which excluded some of the subsidiaries of the Bank. Further information regarding subsidiaries that are not included in the consolidation for regulatory purposes is set out in note (a) to the supplementary notes.
- (ii) The accounting policies applied in preparing these supplementary notes are the same as those applied in preparing the consolidated financial statements for the year ended 31 December 2007 as set out in note 2 to the financial statements.

(a) Capital adequacy ratios

	2007	2006 (restated)
	%	%
Capital adequacy ratio as at 31 December	<u>13.2%</u>	<u>13.8%</u>
Core capital ratio as at 31 December	<u>10.5%</u>	<u>12.0%</u>

The consolidated capital adequacy and core capital ratios were calculated in accordance with the Banking (Capital) Rules of the Hong Kong Banking Ordinance which became effective on 1 January 2007 and the capital ratios as at 31 December 2006 have been recalculated in accordance with the Capital Rules.

The basis of consolidation for calculation of the capital ratios under the Capital Rules includes the Bank’s major subsidiaries but excludes certain subsidiaries including SCL Consulting (Shanghai) Company Limited, Standard Chartered Corporate Advisory Company Limited, SCOPE International (China) Company Limited and Standard Chartered Investment Services Limited. The investment cost of these subsidiaries are therefore deducted from capital.

The Bank uses the basic approach to calculate its credit risk for non-securitization exposures and the standardized (securitization) approach to calculate the credit risk for securitization exposures. For the calculation of its capital charge for market risk, the Bank uses an internal models approach for two guaranteed funds and the standardized (market risk) approach for other exposures. In addition, the Bank adopts the standardized (operational risk) approach for operational risk.

The Bank applies the Internal Capital Adequacy Assessment Process (“ICAAP”) to assess the capital demand on a current, planned and stressed basis. The assessment covers the major risks faced by the Bank, in addition to credit, market and operational risks that are covered under the minimum capital requirements. The ICAAP has been approved by the Asset and Liability Committee (“ALCO”), the Executive Committee (“EXCO”) and the Board of Directors.

The Board has the responsibility to ensure that the Bank is adequately capitalized with respect to risks inherent in the business activities and the day-to-day management of the risks is delegated to a number of committees. The risk profiles and capital related matters are reviewed by the Board on a regular basis.

	<i>Consolidated</i>	
	2007	2006
		<i>(restated)</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Core capital:		
Paid up ordinary share capital	97	101
Irredeemable non-cumulative preference shares	–	3,800
Share premium	12,477	12,477
Reserves	8,157	6,758
Current year profit	7,425	6,070
Minority interests	–	51
Deduct:		
Goodwill	(611)	(611)
Other intangible assets	(172)	(127)
Deferred tax assets	(43)	(56)
	<u>27,330</u>	<u>28,463</u>
Deductions from core capital	<u>(1,536)</u>	<u>(761)</u>
Core capital after deductions	<u>25,794</u>	<u>27,702</u>
Supplementary capital:		
Available-for-sale securities revaluation reserve and others	627	55
Regulatory reserve	914	552
Collective impairment allowances for impaired assets	328	351
Term subordinated debt	6,234	3,756
	<u>8,103</u>	<u>4,714</u>
Deductions from supplementary capital	<u>(1,536)</u>	<u>(761)</u>
Supplementary capital after deductions	<u>6,567</u>	<u>3,953</u>
Total capital base before deductions	35,433	33,177
Deductions from total capital base	<u>(3,072)</u>	<u>(1,522)</u>
Total capital base	<u>32,361</u>	<u>31,655</u>

The Bank's capital charge for credit, market and operational risks is summarized as follows:

	<i>Consolidated</i>	
	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Credit risk		
– Non-securitization exposures	17,055	16,295
– Securitization exposures	45	35
Market risk		
– Standardised approach		
• Interest rate exposures	542	463
• Foreign exchange exposures	19	45
– Internal models approach	28	28
Operational risk	<u>1,876</u>	<u>1,550</u>

At the end of 2007, the total deductions from the Bank's core capital and supplementary capital amounted to HK\$3,898 million (2006: HK\$2,316 million).

(b) Liquidity ratio

	<i>Bank</i>	
	<i>2007</i>	<i>2006</i>
	<i>%</i>	<i>%</i>
Average liquidity ratio for the year	<u>44.3%</u>	<u>44.0%</u>

The average liquidity ratio is computed as the simple average of each calendar month's average ratio and is in accordance with the Fourth Schedule to the Hong Kong Banking Ordinance.

(c) Analysis of fee and commission income

The products constituting not less than 10% of the total amount of fee and commission income are as follows:

	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Credit cards	1,042	1,020
Trade products	795	758
Global market products	1,313	763
Investment services	<u>1,321</u>	<u>791</u>

(d) Advances to customers analysed by industry sector

The analysis of gross advances to customers by industry sector is based on the categories used by the Hong Kong Monetary Authority.

	2007 HK\$'M	Consolidated % of advances covered by collateral or other securities	2006 HK\$'M	% of advances covered by collateral or other securities
Gross advances for use in Hong Kong				
<i>Industrial, commercial and financial</i>				
– Property development	3,612	33%	3,715	38%
– Property investment	17,756	92%	16,685	91%
– Financial concerns	9,773	40%	10,691	25%
– Stockbrokers	1,939	38%	804	34%
– Wholesale and retail trade	4,214	27%	5,655	16%
– Manufacturing	8,369	25%	7,168	32%
– Transport and transport equipment	2,047	3%	3,853	4%
– Others	7,359	19%	6,829	16%
<i>Individuals</i>				
– Advances for the purchase of flats in the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	1,406	100%	1,852	100%
– Advances for the purchase of other residential properties	82,682	99%	79,313	99%
– Credit card advances	9,003	–	9,575	–
– Others	8,219	–	6,614	4%
Total gross advances for use in Hong Kong	156,379		152,754	
Trade finance	15,834	28%	13,949	28%
Trade bills	2,852	–	2,674	–
Gross advances for use outside Hong Kong	5,221	–	1,767	2%
Gross advances to customers	180,286	67%	171,144	65%

	2007 HK\$M	% of advances covered by collateral or other securities	Bank 2006 HK\$M	% of advances covered by collateral or other securities
Gross advances for use in Hong Kong				
<i>Industrial, commercial and financial</i>				
– Property development	3,612	33%	3,715	38%
– Property investment	17,756	92%	16,685	91%
– Financial concerns	9,773	40%	10,691	25%
– Stockbrokers	1,939	38%	804	34%
– Wholesale and retail trade	4,214	27%	5,655	16%
– Manufacturing	8,369	25%	7,168	32%
– Transport and transport equipment	2,047	3%	3,285	5%
– Others	7,359	19%	6,829	16%
<i>Individuals</i>				
– Advances for the purchase of flats in the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	1,406	100%	1,852	100%
– Advances for the purchase of other residential properties	82,682	99%	79,313	99%
– Credit card advances	9,003	–	9,575	–
– Others	8,219	–	6,614	4%
Total gross advances for use in Hong Kong	156,379		152,186	
Trade finance	15,834	28%	13,949	28%
Trade bills	2,852	–	2,674	–
Gross advances for use outside Hong Kong	5,221	–	1,767	2%
Gross advances to customers	180,286	67%	170,576	65%

Advances to customers by geographical area are classified according to the location of the counterparties after taking into account the transfer of risk. As at 31 December 2007 and 31 December 2006, over 90 per cent of the Bank's and its subsidiaries' advances to customers were classified under the area of Hong Kong.

The amount of impaired and overdue advances to customers and individually and collectively assessed impairment allowances for industry sectors which constitute not less than 10% of the Bank's and its subsidiaries' total advances to customers are as follows:

	<i>Impaired advances to customers</i>	<i>Overdue advances to customers</i>	<i>Individually assessed impairment allowances</i>	<i>Collectively assessed impairment allowances</i>	<i>New provision charge</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
<u>As at 31 December 2007</u>					
Advances for the purchase of other residential properties	219	88	11	11	28
<u>As at 31 December 2006</u>					
Advances for the purchase of other residential properties	318	111	21	17	48

(e) Overdue and rescheduled assets

(i) Overdue advances to customers

	2007		Consolidated 2006	
	<i>HK\$'M</i>	<i>% of advances</i>	<i>HK\$'M</i>	<i>% of advances</i>
Gross advances to customers which have been overdue with respect to either principal or interest for periods of:				
– 6 months or less but over 3 months	176	0.1%	141	0.1%
– 1 year or less but over 6 months	69	–	156	0.1%
– over 1 year	339	0.2%	974	0.6%
	<u>584</u>	<u>0.3%</u>	<u>1,271</u>	<u>0.8%</u>

	2007 HK\$'M	2006 HK\$'M
Fair value of collateral held against the covered portion of overdue advances to customers	<u>178</u>	<u>246</u>
Covered portion of overdue advances to customers	86	136
Uncovered portion of overdue advances to customers	<u>498</u>	<u>1,135</u>

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

The collateral held in respect of the overdue advances consists of cash, properties and securities.

Individually assessed impairment charges against overdue advances to customers	<u>389</u>	<u>1,062</u>
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As at 31 December 2007 and 31 December 2006, there were no overdue advances to banks and other financial institutions.

(ii) *Rescheduled advances to customers*

	<i>Consolidated</i>			
	2007 HK\$'M	% of advances	2006 HK\$'M	% of advances
Rescheduled advances	<u>498</u>	<u>0.3%</u>	<u>443</u>	<u>0.3%</u>

Rescheduled advances are those advances, which have been restructured or renegotiated because of a deterioration in the financial position of the borrowers, or the inability of the borrowers to meet the original repayment schedule and for which the revised repayment terms are non-commercial to the Bank. Rescheduled advances to customers are stated net of any advances that have subsequently become overdue for over 3 months and reported as overdue advances in note(e)(i) above.

There were no rescheduled advances to banks and other financial institutions as at 31 December 2007 and 31 December 2006.

(f) Currency risk

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

	<i>2007</i> <i>HK\$'M</i>	<i>2006</i> <i>HK\$'M</i>
US dollar exposure		
Spot assets	158,055	122,020
Spot liabilities	(124,741)	(92,110)
Forward purchases	229,941	257,586
Forward sales	<u>(263,945)</u>	<u>(287,725)</u>
Net short non-structural position	<u>(690)</u>	<u>(229)</u>
Euro exposure		
Spot assets	7,212	5,404
Spot liabilities	(7,619)	(6,571)
Forward purchases	6,529	35,923
Forward sales	<u>(6,262)</u>	<u>(35,060)</u>
Net short non-structural position	<u>(140)</u>	<u>(304)</u>
Swiss francs exposure		
Spot assets	933	110
Spot liabilities	(1,814)	(394)
Forward purchases	1,697	3,518
Forward sales	<u>(885)</u>	<u>(3,309)</u>
Net short non-structural position	<u>(69)</u>	<u>(75)</u>

The Bank had the following structural foreign currency positions which exceed 10% of the net structural position in all foreign currencies:

	<i>2007</i> <i>HK\$'M</i>	<i>2006</i> <i>HK\$'M</i>
Chinese Renminbi	1,067	995
United Arab Emirates Dirham	488	498
Vietnamese Dong	<u>394</u>	<u>238</u>
	<u>1,949</u>	<u>1,731</u>

(g) Cross border claims

Cross border claims are on-balance sheet exposures of counterparties based on the location of those counterparties after taking into account the transfer of risk. For a claim guaranteed by a party situated in a country different from the counterparty, risk will be transferred to the country of the guarantor. For a claim on the branch of a bank or other financial institution, the risk will be transferred to the country where its head office is situated. Claims on individual countries or area, after risk transfer, amounting to 10% or more of the aggregate cross border claims are shown as follows:

	<i>Consolidated</i>			
	<i>2007</i>			
	<i>Banks and other financial institutions HK\$'M</i>	<i>Public sector entities HK\$'M</i>	<i>Other HK\$'M</i>	<i>Total HK\$'M</i>
Asia Pacific excluding Hong Kong	30,862	–	10,080	40,942
Western Europe				
– United Kingdom	80,564	–	3,196	83,760
– Others	49,990	518	1,947	52,455
	<u>130,554</u>	<u>518</u>	<u>5,143</u>	<u>136,215</u>
	<i>Consolidated</i>			
	<i>2006</i>			
	<i>Banks and other financial institutions HK\$'M</i>	<i>Public sector entities HK\$'M</i>	<i>Other HK\$'M</i>	<i>Total HK\$'M</i>
Asia Pacific excluding Hong Kong	31,547	–	8,790	40,337
Western Europe				
– United Kingdom	43,750	–	2,528	46,278
– Others	48,750	464	4,333	53,547
	<u>92,500</u>	<u>464</u>	<u>6,861</u>	<u>99,825</u>

(h) Non-bank Mainland China exposure

	<i>On-balance sheet exposure HK\$'M</i>	<i>Off-balance sheet exposure HK\$'M</i>	<i>Total HK\$'M</i>	<i>Individually assessed impairment allowances HK\$'M</i>
<u>As at 31 December 2007</u>				
Mainland China entities	2,850	6,431	9,281	122
Companies and individuals outside Mainland China where the credit is granted for use in Mainland China	3,050	14,862	17,912	3
Other counterparties where the exposure is considered by the Bank to be non-bank Mainland China exposure	14	102	116	–
<u>As at 31 December 2006</u>				
Mainland China entities	2,051	4,868	6,919	129
Companies and individuals outside Mainland China where the credit is granted for use in Mainland China	2,792	11,250	14,042	3
Other counterparties where the exposure is considered by the Bank to be non-bank Mainland China exposure	58	84	142	20

The off-balance sheet exposure represents the amount at risk should the contract be fully drawn upon and the client defaults. As the facilities may expire without being drawn upon, the contractual amounts do not represent expected future cash flows.

(i) Corporate governance

The Bank is committed to high standards of corporate governance, and has fully complied throughout the year with the guideline on “Corporate Governance of Locally Incorporated Authorised Institutions” under the Supervisory Policy Manual issued by the HKMA.

Board committees

The Board has established various committees while reserving key strategic matters for its own approval. The major committees are detailed below:

(i) Audit Committee

The Audit Committee meets regularly with Internal Audit and the external auditors to review and discuss the Bank’s internal financial controls, internal controls, compliance and risk management systems. The Committee also discusses matters raised by the internal and external auditors and ensures that audit recommendations are implemented appropriately. The Committee comprises of at least 3 non-executive directors, the majority of whom are independent.

(ii) *Executive Committee (“EXCO”)*

The EXCO operates under the direct authority of the Board and meets regularly in relation to the day to day management, operation and control of the business. It also sub-delegates to various committees certain aspects of the conduct of the business as detailed below. The EXCO comprises the Chief Executive Officer, the Chief Financial Officer and the heads of various business functions.

(iii) *Risk Committee*

The Risk Committee is responsible for assisting the Board to supervise and direct the management of credit, market, country, operational, compliance and reputational risk within the Bank. It also ensures that processes and procedures in place for monitoring and control of risk meet the standards set down in internal procedures and external regulatory requirements.

The Committee meets regularly and comprises the Chief Risk Officer, the Chief Financial Officer, heads of Credit and representatives from other relevant units. It has appointed various sub-committees to supervise and review specific areas of risk, including the Portfolio Management Committee, the Early Alert Committee, the Group Special Asset Management Committee, the Excess Approval Committee and the Country Operational Risk Group.

(iv) *Asset and Liability Committee (“ALCO”)*

The ALCO is appointed by the EXCO. It is chaired by the Chief Executive Officer, and with authority derived from the Board, is responsible for both statutory and prudential liquidity. It is also responsible to ensure that the management of the balance sheet is in compliance with regulatory requirements relating to management of liquidity, capital adequacy and structural market risks. These are managed through the provision of liquidity policies and guidelines agreed in ALCO. The members of the ALCO include the Chief Executive Officer, the Chief Financial Officer and key business and risk management heads.

(v) *Country Operational Risk Group (“CORG”)*

CORG is appointed by the Risk Committee to review the country Operational Risk Profile with the objective to provide a forum for the management oversight of country and business level Operational Risk (“OR”) trends and issues arising from control lapses/failures, regulatory breaches, policy non-compliance, as well as exceptions and weaknesses identified through the self-assessment processes, risk toolkits, compliance and business reviews, internal and external audits and external developments/changes. Its main responsibilities include reviewing of the Country OR Profile. This entails deliberating the root causes of risk issues, appropriateness of risk rating, as well as the adequacy and effectiveness of remedial actions. The CORG comprises the Chief Executive Officer, Manager, Operational Risk and representatives from other relevant units.

Internal Audit

Group Internal Audit is a separate function that reports to the Standard Chartered PLC Group Chief Executive and the Group Audit and Risk Committee. Group Internal Audit provides independent confirmation that Bank and business standards, policies and procedures are being complied with. Where necessary, corrective action is recommended.

(j) Market risk exposure management

The capital charge for the Bank's guaranteed retirement funds is based on the potential shortfall between the estimated returns from the funds and the guaranteed returns in the next 12 months. The projected returns are estimated using a simulation approach with a 99% confidence level. The model is back-tested against actual results.

(k) Counterparty credit risk exposures

For counterparty credit risk arising from OTC derivative transactions booked in the banking or trading book (referred as "relevant transactions" in this section), the Bank assigns internal capital following the regulatory capital requirements for counterparty credit risk in accordance with the Basic Approach under the Capital Rules. The internal capital for credit risk assigned to the relevant transactions is made by multiplying the risk-weighted amounts derived from the relevant calculation approach by 8%.

For assignment of credit limits to counterparty credit exposures arising from the relevant transactions, the Bank uses its internal methodology as developed by Group Markets & Institution Risk Management ("MIRM"). The limit setting is based on potential future exposure as estimated by internal models utilizing Monte Carlo simulation.

The Bank's policies for securing collateral and establishing provisions are discussed in note 36(a) - Credit Risk - Risk Mitigation and note 2(k) - Impairment of financial assets.

The following table summarises the Bank's credit exposure arising from OTC derivative transactions. As at 31 December 2007 and 2006, the Bank did not have any outstanding repo-style transactions or credit derivative contracts.

	<i>Consolidated</i>	
	<i>2007</i>	<i>2006</i>
	<i>HK\$M</i>	<i>HK\$M</i>
Gross total positive fair value	2,039	3,781
Credit equivalent amount	19,241	8,397
Recognised collateral held		
– Cash	55	26
Credit equivalent amounts net of recognised collateral held	19,186	8,371
Risk weighted amounts	<u>4,704</u>	<u>2,212</u>

An analysis of the notional amounts, credit equivalent amounts and the risk-weighted amounts for OTC derivatives by counterparty type is summarised as follows:

	<i>Consolidated</i>	
	<i>2007</i>	<i>2006</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Notional amounts:		
– Banks	750,362	443,593
– Corporates	63,033	54,429
	<u>813,395</u>	<u>498,022</u>
Credit equivalent amounts:		
– Banks	18,103	7,699
– Corporates	1,138	698
	<u>19,241</u>	<u>8,397</u>
Risk-weighted amounts:		
– Banks	3,621	1,540
– Corporates	1,083	672
	<u>4,704</u>	<u>2,212</u>

(I) Asset securitization

The Bank uses the standardized (securitization) approach to calculate the credit risk for securitization exposures in which it is an investing institution. There was no asset securitization for which the Bank was an originating institution.

The Bank uses the following external credit assessment institutions to calculate the capital adequacy requirements: Standard & Poor's Ratings Services, Moody's Investors Service, Fitch Ratings and Rating and Investment Information Inc.

	<i>Consolidated</i>				
	<i>2007</i>				
	<i>Exposures deducted from capital</i>				
	<i>Outstanding</i>	<i>Risk-</i>	<i>Capital</i>	<i>Core</i>	<i>Supplementary</i>
	<i>amounts</i>	<i>weighted</i>	<i>requirements</i>	<i>Capital</i>	<i>Capital</i>
	<i>HK\$'M</i>	<i>amount</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Traditional securitization					
– Home equity	<u>2,586</u>	<u>561</u>	<u>45</u>	<u>39</u>	<u>39</u>
	<i>2006</i>				
	<i>Exposures deducted from capital</i>				
	<i>Outstanding</i>	<i>Risk-</i>	<i>Capital</i>	<i>Core</i>	<i>Supplementary</i>
	<i>amounts</i>	<i>weighted</i>	<i>requirements</i>	<i>Capital</i>	<i>Capital</i>
	<i>HK\$'M</i>	<i>amount</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Traditional securitization					
– Home equity	<u>2,084</u>	<u>440</u>	<u>35</u>	<u>39</u>	<u>39</u>

(m) Equity exposure in the banking book

All equity instruments are held in the Bank's banking book and classified as available-for-sale financial assets.

	<i>2007</i> <i>HK\$M</i>	<i>2006</i> <i>HK\$M</i>
Cumulative realised gains on disposal	180	24
Unrealised gains:		
– recognised in reserves but not through the income statement	1,396	157
– included in supplementary capital for capital adequacy ratio purpose	628	71

(n) Interest rate exposure in the banking book

As at the balance sheet date, the variation in the Bank's earnings for a 200 basis points interest rate increase, broken down by currency, is shown as follows (in HK\$ million):

	<i>HKD</i>	<i>USD</i>	<i>AUD</i>	<i>EUR</i>	<i>JPY</i>
2007	<u>(432)</u>	<u>184</u>	<u>(24)</u>	<u>(13)</u>	<u>(61)</u>
2006	<u>(462)</u>	<u>(26)</u>	<u>(41)</u>	<u>(48)</u>	<u>2</u>

The above analysis is based on the methodology as set out by the HKMA in the completion instructions for the "Return of Interest Rate Risk Exposure".