

星展銀行（香港）有限公司  
**DBS BANK (HONG KONG) LIMITED**  
(Incorporated in Hong Kong with limited liability)

**Annual Report 2014**

*DBS Bank (Hong Kong) Limited and its Subsidiaries*

# CONTENTS

	Page(s)
Report of the directors	1
Independent auditor's report	4
Consolidated income statement	5
Consolidated statement of comprehensive income	6
Consolidated balance sheet	7
Bank level balance sheet	8
Consolidated statement of changes in equity	9
Consolidated cash flow statement	10
Notes to the financial statements	11
Unaudited supplementary information	59
Corporate governance report	74

*DBS Bank (Hong Kong) Limited and its Subsidiaries*

# REPORT OF THE DIRECTORS

The directors of DBS Bank (Hong Kong) Limited (the "Bank") submit their report together with the audited financial statements of the Bank and its subsidiaries (together the "Group") for the year ended 31 December 2014.

## **Principal activities**

The principal activity of the Bank is the provision of banking and related financial services. The principal activities of the subsidiaries are shown in Note 23 of the financial statements.

## **Results and appropriations**

The results of the Group for the year ended 31 December 2014 are set out in the consolidated income statement on page 5.

The first interim dividend of HK\$0.143 per share totalling HK\$1,000 million and the second interim dividend of HK\$0.071 per share totalling HK\$500 million were paid on 9 June 2014 and 30 September 2014 respectively for the year ended 31 December 2014 (2013: HK\$1,200 million).

The directors do not recommend the payment of a final dividend for the year ended 31 December 2014 (2013: Nil).

## **Reserves**

Details of the movements in the reserves of the Bank and the Group during the year are set out in Note 33 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 33 to the financial statements.

## **Properties and other fixed assets**

Details of the movements in properties and other fixed assets during the year are set out in Note 27 to the financial statements.

## **Donations**

Donations made by the Group during the year amounted to HK\$724,000 (2013: HK\$3,363,000).

## **Directors**

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

Seah Lim Huat, Peter – Chairman  
Piyush Gupta – Vice Chairman  
J. E. Sebastian Paredes Muirragui – Chief Executive  
Alexander Reid Hamilton  
Dominic Chiu Fai Ho  
Ng Chee Siong, Robert  
Kwok Kwok Chuen  
Yip Dicky Peter

In accordance with Article 98 of the Bank's Articles of Association, Mr. Seah Lim Huat, Peter, Mr. Piyush Gupta, Mr. J. E. Sebastian Paredes Muirragui, Mr. Dominic Chiu Fai Ho, Mr. Ng Chee Siong, Robert, Mr. Kwok Kwok Chuen and Mr. Yip Dicky Peter will retire from office at the forthcoming Annual General Meeting and, being eligible, offer themselves for re-election.

**Directors' interests in contracts**

In 2013, the Bank has granted a banking facility of HK\$500 million to Central Wisdom Limited, which is a wholly-owned subsidiary of Sino Land Company Limited, in the ordinary course of business and on normal commercial terms. Mr. Ng Chee Siong, Robert was interested in the contract between the Bank and Central Wisdom Limited as he is the Chairman and a substantial shareholder of Sino Land Company Limited. This banking facility was cancelled in 2014.

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

**Arrangements to acquire shares**

The following were arrangements which subsisted at the end of the year or at any time during the year which enabled a director of the Bank to acquire benefits by means of the acquisition of shares of DBS Group Holdings Ltd ("DBSH"), the ultimate holding company of the Bank, or to be awarded shares of DBSH (or their equivalent cash value).

***DBSH Share Plan***

The DBSH Share Plan (the "Share Plan") is granted to DBSH Group executives as determined by the Compensation and Management Development Committee ("CMDC") of DBSH appointed to administer the Share Plan from time to time. Participants are awarded shares of DBSH, their equivalent cash value or a combination of both.

Awards consist of the main award and the retention award (being 20% of the main award). The vesting of the main award is staggered between two to four years after grant, i.e. 33% of the shares comprised in the main award will vest 2 years after grant; another 33% will vest in the third year; and the remainder 34% plus the retention award will vest four years after grant. The fair value of the shares awarded is computed based on the market price of the ordinary shares at the time of the award.

During the year, the following directors were eligible to receive awards under the Share Plan as set out below:

- 1) A total of 31,845 share awards were granted to Mr. Seah Lim Huat, Peter and 44,297 share awards were vested in him;
- 2) A total of 326,124 share awards were granted to Mr. Piyush Gupta and 203,709 share awards were vested in him;
- 3) A total of 90,455 share awards were granted to Mr. J. E. Sebastian Paredes Muirragui and 19,222 share awards were vested in him.

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

**Management contracts**

On 31 October 2012, the Bank renewed a service agreement in relation to certain information technology and related services. The agreement commenced on 12 December 2012 and continues until 12 December 2017.

Apart from the foregoing, no contract concerning the management and administration of the whole or any substantial part of the business of the Bank was entered into or existed during the year.

**Auditor**

The financial statements have been audited by PricewaterhouseCoopers who will retire at the forthcoming Annual General Meeting and eligible, offer themselves for re-appointment.

On behalf of the Board

**Seah Lim Huat, Peter**

Chairman

Hong Kong, 23 January 2015

*DBS Bank (Hong Kong) Limited and its Subsidiaries*

# INDEPENDENT AUDITOR'S REPORT

## **TO THE SHAREHOLDERS OF DBS BANK (HONG KONG) LIMITED**

(incorporated in Hong Kong with limited liability)

We have audited the consolidated financial statements of DBS Bank (Hong Kong) Limited (the "Bank") and its subsidiaries (together, the "Group") set out on pages 5 to 58, which comprise the consolidated and company balance sheets as at 31 December 2014, and the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

### **Directors' responsibility for the consolidated financial statements**

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

### **Auditor's responsibility**

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with section 80 of Schedule 11 to the Hong Kong Companies Ordinance and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

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

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

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

### **Opinion**

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Bank and of the Group as at 31 December 2014, and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

### **PricewaterhouseCoopers**

Certified Public Accountants

Hong Kong, 23 January 2015

*DBS Bank (Hong Kong) Limited and its Subsidiaries*

# CONSOLIDATED INCOME STATEMENT

*for the year ended 31 December 2014*

In HK\$ millions	Note	2014	2013
Interest income		<b>6,828</b>	6,310
Interest expense		<b>(2,203)</b>	(1,884)
Net interest income	4	<b>4,625</b>	4,426
Net fee and commission income	5	<b>1,733</b>	1,610
Net income from financial instruments at fair value through profit or loss	6	<b>1,389</b>	1,694
Net income from investment securities	7	<b>180</b>	79
Other income	8	<b>118</b>	387
Total income		<b>8,045</b>	8,196
Total expenses	9	<b>(4,043)</b>	(3,766)
Profit before allowances for credit losses		<b>4,002</b>	4,430
Allowances for credit losses	10	<b>(350)</b>	(302)
Profit before income tax		<b>3,652</b>	4,128
Income tax expense	12	<b>(595)</b>	(604)
Profit attributable to shareholders	13	<b>3,057</b>	3,524

*The notes on pages 11 to 58 form part of these financial statements.*

*DBS Bank (Hong Kong) Limited and its Subsidiaries*

# CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

*for the year ended 31 December 2014*

In HK\$ millions	2014	2013
<b>Profit attributable to shareholders</b>	<b>3,057</b>	3,524
<b>Other comprehensive income</b>		
Available-for-sale financial investments		
– Net valuation taken to equity	<b>159</b>	(36)
– Amortisation of reserve to income statement arising from reclassification of available-for-sale financial investments to loans and receivables	<b>1</b>	1
– Transferred to income statement	<b>(152)</b>	(50)
– Deferred income tax (charged) / credited to equity	<b>(1)</b>	13
<b>Other comprehensive income attributable to shareholders, net of tax</b>	<b>7</b>	(72)
<b>Total comprehensive income attributable to shareholders</b>	<b>3,064</b>	3,452

*Items recorded in "Other comprehensive income" above will be reclassified subsequently to the income statement when specific conditions are met, e.g. when available-for-sale financial investments are disposed.*

*The notes on pages 11 to 58 form part of these financial statements.*

*DBS Bank (Hong Kong) Limited and its Subsidiaries*

# CONSOLIDATED BALANCE SHEET

*as at 31 December 2014*

In HK\$ millions	Note	2014	2013
<b>Assets</b>			
Cash and balances with central banks	16	<b>1,969</b>	995
Government securities and treasury bills	17	<b>22,913</b>	16,106
Due from banks	18	<b>79,478</b>	62,341
Derivatives		<b>5,094</b>	9,084
Bank and corporate securities	19	<b>11,891</b>	12,732
Loans and advances to customers	20	<b>184,569</b>	200,254
Other assets	22	<b>4,645</b>	4,157
Interest in a joint venture	24	–	364
Properties and other fixed assets	27	<b>2,684</b>	2,626
Goodwill and Intangibles	26	<b>197</b>	–
<b>Total assets</b>		<b>313,440</b>	308,659
<b>Liabilities</b>			
Due to banks		<b>4,277</b>	4,751
Deposits and balances from customers	28	<b>252,259</b>	238,391
Derivatives		<b>5,216</b>	9,091
Certificates of deposit issued	29	<b>4,961</b>	7,564
Other liabilities	30	<b>9,707</b>	13,408
Subordinated liability	32	<b>4,189</b>	4,187
<b>Total liabilities</b>		<b>280,609</b>	277,392
<b>Equity</b>			
Share capital	33	<b>7,595</b>	7,000
Reserves	33	<b>25,236</b>	24,267
<b>Total equity</b>		<b>32,831</b>	31,267
<b>Total liabilities and equity</b>		<b>313,440</b>	308,659

*The notes on pages 11 to 58 form part of these financial statements.*

**Dominic Chiu Fai Ho**

*Director*

**Piyush Gupta**

*Director*

**J. E. Sebastian Paredes Muirragui**

*Director*

**Alexander Reid Hamilton**

*Director*

*DBS Bank (Hong Kong) Limited and its Subsidiaries*

# BANK LEVEL BALANCE SHEET

*as at 31 December 2014*

In HK\$ millions	Note	2014	2013
<b>Assets</b>			
Cash and balances with central banks	16	1,969	995
Government securities and treasury bills	17	22,913	16,106
Due from banks	18	79,478	62,338
Derivatives		5,094	9,084
Bank and corporate securities	19	11,891	12,732
Loans and advances to customers	20	184,569	200,254
Other assets	22	4,641	4,157
Interest in a joint venture	24	–	1
Subsidiaries	23	615	48
Properties and other fixed assets	27	2,684	2,626
<b>Total assets</b>		<b>313,854</b>	<b>308,341</b>
<b>Liabilities</b>			
Due to banks		4,277	4,751
Deposits and balances from customers	28	252,259	238,391
Derivatives		5,216	9,091
Certificates of deposit issued	29	4,961	7,564
Other liabilities	30	9,704	13,406
Amounts due to subsidiaries	23	874	83
Subordinated liability	32	4,189	4,187
<b>Total liabilities</b>		<b>281,480</b>	<b>277,473</b>
<b>Equity</b>			
Share capital	33	7,595	7,000
Reserves	33	24,779	23,868
<b>Total equity</b>		<b>32,374</b>	<b>30,868</b>
<b>Total liabilities and equity</b>		<b>313,854</b>	<b>308,341</b>

*The notes on pages 11 to 58 form part of these financial statements.*

**Dominic Chiu Fai Ho**  
*Director*

**Piyush Gupta**  
*Director*

**J. E. Sebastian Paredes Muirragui**  
*Director*

**Alexander Reid Hamilton**  
*Director*

*DBS Bank (Hong Kong) Limited and its Subsidiaries*

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

*for the year ended 31 December 2014*

<b>In HK\$ millions</b>	<b>Share capital</b>	<b>Share premium</b>	<b>Other reserves</b>	<b>Retained earnings</b>	<b>Total equity</b>
Balance as at 1 January 2013	7,000	595	2,635	18,785	29,015
Total comprehensive income	–	–	(72)	3,524	3,452
Dividend	–	–	–	(1,200)	(1,200)
Balance as at 31 December 2013	7,000	595	2,563	21,109	31,267
Balance as at 1 January 2014	<b>7,000</b>	<b>595</b>	<b>2,563</b>	<b>21,109</b>	<b>31,267</b>
Transition to no-par value regime	<b>595</b>	<b>(595)</b>	–	–	–
Total comprehensive income	–	–	<b>7</b>	<b>3,057</b>	<b>3,064</b>
Dividend	–	–	–	<b>(1,500)</b>	<b>(1,500)</b>
Balance as at 31 December 2014	<b>7,595</b>	<b>–</b>	<b>2,570</b>	<b>22,666</b>	<b>32,831</b>

*The notes on pages 11 to 58 form part of these financial statements.*

DBS Bank (Hong Kong) Limited and its Subsidiaries

# CONSOLIDATED CASH FLOW STATEMENT

for the year ended 31 December 2014

In HK\$ millions	Note	2014	2013
<b>Cash flows from operating activities</b>			
Profit before income tax		3,652	4,128
<b>Adjustments for non-cash items:</b>			
Net gain on disposal of properties and other fixed assets		–	(275)
Fair value adjustment on investment properties		(9)	(34)
Allowances for credit losses		350	302
Write-off of properties and other fixed assets		2	5
Depreciation and amortisation		201	220
Fair value adjustment on interest in a joint venture		(17)	–
Advances written off net of recoveries		(547)	(357)
Revaluation for certificates of deposit issued		(5)	(179)
Amortisation of discount on certificates of deposit issued		9	4
Interest expense for certificates of deposit issued		157	163
Interest expense for subordinated liability		116	118
Share of profit of a joint venture		(20)	(34)
Profit before changes in operating assets and liabilities		3,889	4,061
<b>Increase / (decrease) in:</b>			
Due to banks		(474)	(4,605)
Deposits and balances from customers		9,738	24,287
Other liabilities and derivatives		(6,625)	938
<b>(Increase) / decrease in:</b>			
Due from banks		(5,216)	18,121
Government securities and treasury bills		(5,273)	4,217
Loans and advances to customers		18,953	(24,548)
Bank and corporate securities		829	(3,287)
Other assets and derivatives		3,509	(3,833)
Net cash generated from operating activities before income tax		19,330	15,351
Hong Kong profits tax paid		(744)	(588)
Overseas tax paid		(7)	(6)
<b>Net cash generated from operating activities</b>		<b>18,579</b>	<b>14,757</b>
<b>Cash flows from investing activities</b>			
Purchase of fixed assets		(244)	(194)
Proceeds from disposal of properties and other fixed assets		–	320
Net cash received from asset transfers		461	–
<b>Net cash generated from investing activities</b>		<b>217</b>	<b>126</b>
<b>Cash flows from financing activities</b>			
Dividend paid		(1,500)	(1,200)
Interest paid for certificates of deposits issued		(166)	(187)
Interest paid for subordinated liability		(116)	(118)
Issuance of certificates of deposit	35(a)	2,213	2,230
Redemption of certificates of deposit issued	35(a)	(4,820)	(1,784)
<b>Net cash used in financing activities</b>		<b>(4,389)</b>	<b>(1,059)</b>
Exchange differences and other adjustments		2	3
<b>Net change in cash and cash equivalents</b>		<b>14,409</b>	<b>13,827</b>
<b>Cash and cash equivalents as at 1 January</b>		<b>41,157</b>	<b>27,330</b>
<b>Cash and cash equivalents as at 31 December</b>	35(b)	<b>55,566</b>	<b>41,157</b>

The notes on pages 11 to 58 form part of these financial statements.

*DBS Bank (Hong Kong) Limited and its Subsidiaries*

# NOTES TO THE FINANCIAL STATEMENTS

*for the year ended 31 December 2014*

## 1 GENERAL INFORMATION

The principal activities of DBS Bank (Hong Kong) Limited (the "Bank") and its subsidiaries (together the "Group") are the provision of banking and related financial services. The Bank is a limited company incorporated and domiciled in Hong Kong. The address of its registered office is 11th Floor, The Center, 99 Queen's Road Central, Hong Kong.

The ultimate holding company is DBS Group Holdings Ltd ("DBSH") which is listed, incorporated and domiciled in the Republic of Singapore. The address of its registered office is 12 Marina Boulevard, Marina Bay Financial Centre Tower 3, Singapore 018982.

The consolidated financial statements were approved for issue by the Board of Directors on 23 January 2015.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following is a summary of the principal accounting policies applied by the Group and, except where noted, are consistent with those applied in the previous financial year.

### (a) Basis of preparation

The consolidated financial statements are prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA").

In accordance with the transitional and saving arrangements for Part 9 of the Hong Kong Companies Ordinance (Cap. 622), "Accounts and Audit" as set out in section 76 to 87 of Schedule 11 to the Hong Kong Companies Ordinance (Cap. 622), the consolidated financial statements are prepared in accordance with the applicable requirements of the predecessor Companies Ordinance (Cap. 32) for this financial year and the comparative period.

The consolidated financial statements are presented in Hong Kong dollars and rounded to the nearest million, unless otherwise stated.

The preparation of financial statements requires management to exercise judgement, use estimates and make assumptions that affect the application of policies and reported amounts in the financial statements. Although these estimates are based on management's best knowledge of current events and actions, actual results may differ from these estimates. Critical accounting estimates and assumptions used that are significant to the financial statements, and areas involving a higher degree of judgement and complexity, are disclosed in Note 3.

### (b) Change in balance sheet presentation

The presentation of the Group's and the Bank's balance sheet has been changed to focus on the most material assets and liabilities. The current presentation also reflects the guidance under HKFRS to arrange balance sheet item broadly by their nature.

### (c) Adoption of new and revised accounting standards

On 1 January 2014, the Group adopted the following new or revised HKFRSs that are issued by HKICPA and relevant for the Group. The adoption of these HKFRSs has no significant impact on the financial statements of the Group.

#### **Amendments to HKAS 32: Offsetting Financial Assets and Liabilities**

The amendments to HKAS 32 clarify the offsetting criteria in HKAS 32 by explaining when an entity has a legally enforceable right to set-off and when gross settlement is equivalent to net settlement.

#### **HK(IFRIC) 21: Levies**

HK(IFRIC) 21 sets out the accounting for an obligation to pay a levy that is not income tax.

In addition to the above, a number of new standards and amendments to standards are effective for annual periods beginning after 1 January 2014. The Group has not applied these standards or amended standards in preparing these financial statements. Other than the following, none of these is expected to have a significant effect on the financial statements of the Group and the Bank.

#### **HKFRS 9: Financial Instruments**

HKFRS 9 replaces the existing guidance in HKAS 39 Financial Instruments: Recognition and Measurement. It includes revised guidance on the classification and measurement of financial instruments, introduces a new expected credit loss model for impairment of financial assets as well as new requirements for general hedge accounting. The standard is effective for annual reporting periods beginning on or after 1 January 2018. Early adoption is permitted.

A summary of the most significant group accounting policies is described further below starting with those relating to the entire financial statements followed by those relating to the income statement, the balance sheet and other specific topics. This does not reflect the relative importance of these policies to the Group.

## **General Accounting Policies**

### **(d) Group accounting**

#### **Subsidiaries**

Subsidiaries are entities (including structured entities) over which the Group has control. The Group controls an entity when it is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are consolidated from the date control is transferred to the Group to the date control ceases.

The acquisition method is used to account for business combinations. Refer to Note 2(j) for the Group's accounting policy on goodwill.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

#### **Joint venture**

Joint ventures are arrangements in which the Group has joint control. The Group has rights to the net assets of the arrangement, rather than rights to its assets and obligations from its liabilities. Joint ventures are accounted for using the equity method.

#### **Investment cost at Bank level**

Investments in subsidiaries and a joint venture are stated at cost less accumulated impairment losses in the Bank's balance sheet. On disposal of investments in subsidiaries and joint venture, the difference between the net proceeds and the carrying amounts of the investments is taken to the income statement.

### **(e) Foreign currency treatment**

#### **(i) Functional and presentation currency**

Items in the financial statements are measured using the functional currency of each entity in the Group, being the currency of the primary economic environment in which the entity operates. The Group's financial statements are presented in Hong Kong dollars, which is its functional currency of the Bank.

#### **(ii) Foreign currency transactions and balances**

Transactions in foreign currencies are measured using exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into Hong Kong dollars at the exchange rate as at the balance sheet date. Foreign exchange differences arising from this translation are recognised in the income statement.

Non-monetary assets and liabilities measured at cost in a foreign currency are translated using the exchange rate at the date of the transaction.

#### **(iii) Subsidiaries and branches**

The results and financial positions of subsidiaries and branches whose functional currency is not Hong Kong dollars ("foreign operations") are translated into Hong Kong dollars in the following manner:

- Assets and liabilities are translated at the exchange rates as at the balance sheet date;
- Income and expenses in the income statement are translated at exchange rates prevailing at each month-end, approximating the exchange rates at the dates of the transactions; and
- All resulting exchange differences are recognised in other comprehensive income and accumulated under capital reserves in equity. When a foreign operation is disposed of, such currency translation differences are recognised in the income statement as part of the gain or loss on disposal.

## **Income Statement**

### **(f) Income recognition**

#### **(i) Interest income and interest expense**

Interest income and interest expense as presented in Note 4 respectively represent the income on all assets and liabilities regardless of the classification and measurement of the assets and liabilities on amortised cost or at fair value, with the exception of the Group's structured investment deposits which are carried at fair value through profit or loss. Interest expense on such structured investment deposits are presented together with other fair value changes in "Net income from financial instruments at fair value through profit or loss".

Interest income and interest expense are recognised on a time-proportionate basis using the effective interest method as prescribed by HKFRS. The calculation includes significant fees and transaction costs that are integral to the effective interest rate, as well as premiums or discounts.

#### **(ii) Fee and commission income**

The Group earns fee and commission income from a diverse range of products and services provided to its customers.

Fee and commission income is generally recognised on the completion of a transaction. Such fees include underwriting fees, brokerage fees and fees related to completion of corporate finance transactions. For a service that is provided over a period of time, fee and commission income is recognised over the period during which the related service is provided or credit risk is undertaken. Such fees include the income from issuance of financial guarantee.

Fee and commission income is recorded net of incremental expenses that are directly related to generating it. These expenses typically include brokerage fees paid, card-related expenses and sales commissions, but do not include expenses for services delivered over a period (such as service contracts) and other expenses that are not specifically related to fee and commission income transactions.

(iii) Dividend income

Dividend income is recognised when the right to receive payment is established. This is generally the ex-dividend date for listed equity securities, and usually the date when shareholders approve the dividend for unlisted equity securities. Dividend income arising from held-for-trading financial assets is recognised in "Net income from financial instruments at fair value through profit or loss", and dividend arising from available-for-sale financial assets is recognised in "Net income from investment securities".

(iv) Rental income

Rental income from operating leases on properties is recognised on a straight-line basis over the lease term.

(v) Allowances for credit losses

Please refer to Note 2(i) for the accounting policy on impairment of financial assets including loan loss provisions.

## Balance Sheet

### (g) Financial assets

#### Initial recognition

Purchases and sales of all financial assets, even if their classification and measurement are subsequently changed, are recognised on the date that the Group enters into the contractual arrangements with counterparties. When the Group as trustee or in a fiduciary capacity for assets it does not directly control or benefit from, the assets and the corresponding income belonging to a customer are excluded from the financial statements.

Financial assets are initially recognised at fair value, which is generally the transaction price.

#### Classification and subsequent measurement

The Group classifies and measures financial assets based on their nature and the purpose for which they are acquired. This generally corresponds to the business models in which they are applied and how management monitors performance, as follows:

- Financial assets (other than derivatives) that are managed mainly for longer-term holding and collection of payments are classified as loans and receivables. These assets have fixed or determinable payments, are not quoted in an active market. Loans and receivables are carried at amortised cost and using the effective interest method.
- Financial assets that are managed on a fair value basis, are classified as financial assets at fair value through profit or loss. Such assets include instruments held for the purpose of short term selling and market making ("Held for trading"), or designated under the fair value option if doing so eliminates or significantly reduces measurement or recognition inconsistencies that would otherwise arise, or if the financial asset contains an embedded derivative that would otherwise need to be separately recorded ("Designated at fair value through profit or loss").

Realised or unrealised gains or losses on such financial assets, except interest income, are taken to "Net income from financial instruments at fair value through profit or loss" in the income statement in the period they arise.

- Derivatives (including derivatives embedded in other contracts but separated for account purposes) are also categorised as "held for trading" unless they are designated as hedges in accordance with Note 2(p). Derivatives are classified as assets when the fair value is positive and as liabilities when the fair value is negative. Changes in the fair value of derivatives other than those designated as hedges are included in "Net income from financial instruments at fair value through profit or loss".
- The Group also holds other financial assets for the purpose of investment or satisfying regulatory liquidity requirements. Such assets are held for an indefinite period and may be sold in response to needs for liquidity or changes in interest rates, credit spreads, exchange rates or equity prices. These assets are classified as available-for-sale and initially and subsequently measured at fair value.

Unrealised gains or losses arising from changes in fair value are recognised in other comprehensive income and accumulated in investments revaluation reserve. When sold or impaired, the accumulated fair value adjustments in the investments revaluation reserves are reclassified to the income statement. Unquoted equity investments classified as available-for-sale for which fair values cannot be reliably determined are carried at cost, less impairment.

Where the classification and measurement of financial assets do not reflect the management of the financial assets (or financial liabilities), the Group may apply hedge accounting where permissible and relevant to better reflect the management of the financial assets. Please refer Note 2(p) for details on hedging and hedge accounting.

Please refer to Note 15 for further details on the types of financial assets classified and measured as above.

#### **Reclassification of financial assets**

When the purpose for holding a financial asset changes, or when HKFRS otherwise requires it, non-derivative financial assets are reclassified accordingly. Financial assets may be classified out of the fair value through profit or loss or available-for-sale categories only in particular circumstances as prescribed by HKAS 39.

Reclassifications are made at fair value as of the reclassification date. The fair value becomes the new cost or amortised cost as applicable. Any gain or loss already recognised in the income statement before the reclassification date is not reversed.

#### **Determination of fair value**

The fair value of financial assets is the price that would be received if the asset is sold in an orderly transaction between market participants at the measurement date. Fair value is generally estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments. Where applicable, a valuation reserve or pricing adjustment is applied to arrive at the fair value. The determination of fair value is considered a significant accounting policy for the Group and further details are disclosed in Note 34 on fair value measurements.

#### **Offsetting**

Financial assets and liabilities are presented net when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle them on a net basis, or realise the asset and settle the liability simultaneously.

#### **Derecognition**

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or when they have been transferred together with substantially all risks and rewards of ownership.

The Group enters into certain transactions where it transfers financial assets recognised on its balance sheet but retains either all or a portion of the risks and rewards of the transferred financial assets. In such cases, the transferred financial assets are not derecognised from the balance sheet. Such transactions include repurchase transactions. They also include certain transactions where control over the financial asset is retained, for example, by a simultaneous transaction (such as options) with the same counterparty to which the asset is transferred. In such cases, the Group continues to recognise the asset to the

extent of its continuing involvement and by the extent to which it is exposed to changes in the value of the transferred asset.

Please refer to Note 39 for disclosures on transfers of financial assets.

#### **(h) 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, balances with banks, placements with and advances to banks and short-term bills and notes classified as held-for-trading and available-for-sale financial assets which are readily convertible into cash.

#### **(i) Impairment of financial assets**

##### **Financial assets carried at amortised cost**

The Group assesses at each balance sheet date whether there is evidence that a financial asset or a group of financial assets is impaired. Impairment allowance is made when there is objective evidence of impairment as a result of the occurrence of loss events that will have an impact on the estimated future cash flows. The Group 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 Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

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

- Significant financial difficulty of the issuer or obligor, including breach of covenants and / or financial conditions;
- A breach of contract, such as a default or delinquency in interest or principal payments;
- Granting of a concession to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, that the entity would not otherwise consider; and
- High probability of bankruptcy or other financial reorganisation of the borrower.

Individual impairment allowances are assessed using the discounted cash flow method. Individual impairment allowances are measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the original effective interest rate. If a financial asset has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

Collective impairment allowances are assessed on the basis of contractual cash flows and historical loss experience adjusted for current conditions.

The carrying amount of the asset is reduced through the use of an allowance account and the amount of the allowance is recognised in the income statement.

If, in a subsequent period, the amount of the impairment decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment allowances are reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

When a loan is uncollectible, it is written off against the related allowances 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 reduce the amount of the allowances for loan impairment in the income statement.

#### **Financial assets classified as available-for-sale**

The Group assesses at each balance sheet date whether there is evidence that an available-for-sale financial assets is impaired. In the case of an equity investment, a significant or prolonged decline in the fair value of security below its cost is a factor in determining whether the asset is impaired. When there is evidence of an impairment of an available-for-sale financial asset, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in the income statement – is reclassified from the investments revaluation reserve within equity to the income statement. For equity investments, impairment losses are not reversed until they are disposed of. For impaired debt instruments that subsequently recover in value, the impairment losses are reversed through the income statement if there has been an identifiable event that led to the recovery.

#### **(j) Goodwill**

Goodwill arising from business combinations generally represents the excess of the acquisition cost over the fair value of the identifiable assets acquired and liabilities and contingent liabilities assumed on acquisition date. Goodwill is stated at cost less impairment losses and it is tested at least annually for impairment.

At the acquisition date, any goodwill acquired is allocated to each of the cash-generating units (CGU) or group of CGUs expected to benefit from the combination's synergies.

An impairment loss is recognised when the carrying amount of a CGU, or a group of CGUs, including the goodwill, exceeds the applicable recoverable amount. The recoverable amount of a CGU or CGU group is the higher of the CGU's or CGU group's

fair value less cost to sell and its value-in-use. An impairment loss on goodwill is recognised in the income statement and cannot be reversed in subsequent periods.

#### **(k) Properties and other fixed assets**

##### **(i) Investment properties**

Investment properties are carried at fair value, representing estimated open market value determined by independent qualified valuers. The changes in fair value are recognised in the income statement.

Investment properties include land held under finance leases and self-owned buildings.

If a property becomes an investment property because its use has changed, any difference resulting between the carrying amount and the fair value of the property at the date of transfer is recognised in properties revaluation reserve under HKAS 16 Property, Plant and Equipment. On subsequent disposal of the investment property, the properties revaluation reserve is transferred to retained earnings.

##### **(ii) Properties and other fixed assets**

Properties and other fixed assets are stated at cost less accumulated depreciation and impairment losses. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets. Generally, the useful lives are as follows:

Freehold land	Not depreciated
Land	Over the remaining lease period
Buildings	Over the remaining lease period of the land on which it is situated or 50 years, whichever is shorter
Leasehold improvements	Over the lease term of the leased properties or 5 years, whichever is shorter
Furniture, fixtures and equipment	3 – 8 years

Subsequent expenditure relating to properties and other fixed assets that has already been recognised is added to the carrying amount of the asset only when it is probable that future economic benefit associated with the item can be measured reliably. Other subsequent expenditure is recognised as hire and maintenance expense in the income statement during the financial year in which it is incurred.

Property and other fixed assets are subject to an impairment review if there are events or changes in circumstances which indicate that the carrying amount may not be recoverable.

Upon disposal, the difference between the net disposal proceeds and its carrying amount is taken to the income statement.

Please refer to Note 27 for the details of properties and other fixed assets and their movements during the year.

### **(l) Financial liabilities**

#### **Initial recognition, classification and subsequent measurement**

Financial liabilities are initially recognised at fair value. The Group generally classifies and measures its financial liabilities in accordance with the purpose for which the financial liabilities are incurred and managed. Accordingly:

- Financial liabilities are classified as financial liabilities at fair value through profit or loss if they are incurred for the purpose of repurchasing in the near term (held-for-trading), and this may include debt securities issued and short positions in securities for the purpose of ongoing market-making or trading. Financial liabilities at the fair value through profit or loss can also be designated by management on initial recognition (designated under the fair value option).

Realised or unrealised gains or losses on financial liabilities held for trading and financial liabilities designated under the fair value option, except interest expense, are taken to "Net income from financial instruments at fair value through profit or loss" in the income statement in the period they arise. Interest expense on structured investment deposits at fair value through profit or loss are also presented together with other fair value changes in "Net income from financial instruments at fair value through profit or loss".

- Derivative liabilities are treated consistently with derivative assets. Please refer to Note 2(g) for the accounting policy on derivatives.
- Other financial liabilities are carried at amortised cost using the effective interest method. These comprise predominantly the Group's deposit portfolio under "Deposits and balances from customers" and "Due to banks" and those under "Other liabilities".

Please refer to Note 15 for further details on the types of financial liabilities classified and measured as above.

#### **Determination of fair value**

The fair value of financial liabilities is the price that would be paid to transfer the liability in an orderly transaction between market participants at the measurement date.

Please refer also to Note 34 for further fair value measurement disclosures.

#### **Derecognition**

A financial liability is derecognised from the balance sheet when the obligation specified in the contract is discharged, cancelled or expired.

#### **(m) Loan commitments, letters of credit and financial guarantees**

##### **Loan Commitments**

Loan commitments are typically not financial instruments and are not recognised on balance sheet but are disclosed as off-balance sheet in accordance with HKAS 37. They form part of the disclosures in Note 37. Upon a loan draw-down, the amount of the loan is accounted for under "loans and receivables" as described in Note 2(g).

##### **Letters of Credit**

Letters of credit are recorded off-balance sheet as contingent liabilities upon issuance, and the corresponding payables to the beneficiaries and receivables from the applicants are recognised on-balance sheet upon acceptance of the underlying documents.

##### **Financial Guarantees**

A financial guarantee is initially recognised in the financial statements at fair value on the date the guarantee is given. This is generally the amount (fee) paid by the counterparty. Subsequently, the fee is recognised over time as income in accordance with the principles in Note 2(f).

Off-balance sheet credit exposures are managed for credit risk in the same manner as financial assets.

#### **(n) Provisions and other liabilities**

Provisions for other liabilities of uncertain timing and amounts are recognised when:

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

The amount recognised as a provision is the best estimate of the expenditure required to settle the present obligation at the balance sheet date.

#### **(o) Share capital**

Ordinary shares are classified as equity. Incremental external costs directly attributable to the issuance of new ordinary shares are accounted for as a deduction from the share capital account.

Interim dividends are recorded during the financial year in which they are declared payable. Final dividends are recorded during the financial year in which the dividends are approved by the shareholders at the Annual General Meeting.

### Other Specific Topics

#### **(p) Hedging and hedge accounting**

The Group uses derivative contracts mainly as part of its risk management strategies for hedging interest rate risk arising from maturity mismatches or for hedging currency risk arising from currency mismatches and cash flows in foreign currencies.

In some cases, where the strict criteria in HKAS 39 are met, hedge accounting is applied as set out in subsequent paragraphs. At the inception of each hedging relationship, the Group documents the relationship between the hedging instrument and hedged item; the risk management objective for undertaking the hedge transactions and the methods used to assess the effectiveness of the hedge. At inception and on an on-going basis, the Group also documents its assessment, of whether the hedging instrument is highly effective in offsetting changes in the fair value or cash flows of the hedged item.

#### **Fair value hedge**

The Group's fair value hedges consist principally of interest rate swaps used for managing the interest rate gaps that naturally arise from its purchases or issues of debt securities, and where a mismatch in the measurement between the hedging derivative and the hedged item exists.

For a qualifying fair value hedge, the changes in the fair value of the hedging derivative are recorded in the income statement, together with any changes in the fair value of the hedged item attributable to the hedged risk. Gain or loss arising from hedge ineffectiveness is recognised in the income statement under "Net income from financial instruments at fair value through profit or loss".

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item is amortised to the income statement over its remaining maturity, using the effective interest method.

#### **Economic hedges which do not qualify for hedge accounting**

Some derivatives may be transacted as economic hedges as part of the Group's risk management but do not qualify for hedge accounting under HKAS 39. This includes swaps and other derivatives (e.g. futures and options) that the Group transacts to manage interest rate, foreign exchange and other risks. Such derivatives are treated in the same way as derivative held for trading purposes, i.e. realised and unrealised gains and losses are recognised in "Net income from financial instruments at fair value through profit or loss". In some cases, the hedged

exposures are designated at fair value through profit or loss, thereby achieving some measure of offset in the income statement.

Please refer to Note 36 for disclosures on hedging derivatives.

#### **(q) Employee benefits**

Employee benefits, which include base pay, cash bonuses, share-based compensation, contribution to defined contribution plans and other staff related allowances, are recognised in the income statement when incurred. For defined contribution plans, contributions are made to publicly or privately administered funds on a mandatory, contractual or voluntary basis. Once the contributions have been paid, the Group has no further payment obligations.

Employee entitlement to annual leave is recognised when they accrue to employees. A provision is made for the estimated liability for annual unutilised leave as a result of services rendered by employees up to the balance sheet date.

#### **(r) Share-based compensation**

Employee benefits also include share-based compensation, namely, the DBSH Share Option Plan, the DBSH Share Plan and the DBSH Employee Share Plan run by DBSH, the ultimate holding company of the Bank. The details of the Plans are described in Note 43.

These share-based compensation expenses, which are measured at their fair values at grant date, are cash-settled with DBSH, amortised and recognised in the income statement over the relevant vesting periods. Non-market vesting conditions are taken into account in determining the number of shares to be granted or number of options that are expected to become exercisable on vesting dates. The impact of subsequent revision of original estimates, if any, is recognised in the income statement.

#### **(s) Current and deferred taxes**

Current income tax for current and prior periods is recognised as the amount expected to be paid or recovered from the tax authorities, using the tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date.

Deferred income tax is provided on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted by the balance sheet date.

The amount of deferred tax assets recognised takes into account the likelihood the amount that can be used to offset payables taxes for future profits.

Deferred tax related to fair value re-measurement of available-for-sale investments, which are recognised outside the income statement, is also recognised outside the income statement i.e. in other comprehensive income and accumulated in the investments revaluation reserve.

**(t) Leases**

(i) Finance leases

Leases where substantially all the risks and rewards of ownership are transferred to the Group are accounted for as finance leases. Finance leases are capitalised at the commencement of the leases at the lower of the fair values of the leased assets and the present values of the minimum lease payments. The Group's interests in leasehold land are accounted for as finance leases.

Where the Group is a lessor under finance leases and hire purchase transactions, the amounts due under the leases, net of unearned finance income, are recognised as receivables and included in "Loans and advances to customers". Finance income implicit in rentals receivable is credited to the income statement over the lease period so as to produce an approximately constant periodic rate of return on the net investments outstanding for each financial period.

(ii) Operating leases

Leases where substantially all the risks and rewards of ownership of assets remain with the lessor are accounted for as operating leases. Operating leases are charged to the income statement on a straight-line basis over the period of the lease. When an operating lease is terminated before the lease period has expired, any payment that has to be made to the lessor is recognised as an expense in the period the termination takes place.

Where the Group is a lessor under operating leases, rentals receivable under operating leases is credited to the income statement on a straight-line basis over the lease term.

**3 CRITICAL ACCOUNTING ESTIMATES**

The Group's accounting policies and use of estimates are integral to the reported results. Certain accounting estimates require management's judgement in determining the appropriate methodology for valuation of assets and liabilities. Procedures are in place to ensure that methodologies are reviewed and revised as appropriate. The Group believes its estimates for determining the valuation of its assets and liabilities are appropriate.

The following is a brief description of the Group's critical accounting estimates that involve management's valuation judgement.

**(a) Impairment allowances**

The Group establishes, through charges against profit, impairment allowances in respect of estimated loss in loans and advances to customers. The allowances consist of individual impairment allowances and collective impairment allowances. The overall impairment allowances should represent the aggregate amount by which management considers it necessary to write down its loan portfolio in order to state it in the balance sheet at its estimated ultimate net realisable value.

In determining individual impairment allowances, management considers objective evidence of impairment. When an advance to customer is impaired, an individual impairment allowance is assessed by a discounted cash flow method, measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the effective interest rate. The quantum of the allowance is also impacted by the collateral value and this in turn, may be discounted in certain circumstances to recognise the impact of forced sale or quick liquidation. In determining collective impairment allowances, management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows.

The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

**(b) Fair value of financial instruments**

The majority of the Group's financial instruments reported at fair value are based on quoted and observable market prices or on internally developed models that are based on independently sourced market parameters.

The fair value of financial instruments without an observable market price in a liquid market may be determined using valuation models. The choice of model requires significant judgment for complex products.

Policies and procedures have been established to facilitate the exercise of judgement in determining the risk characteristics of various financial instruments, discount rates, estimates of future cash flows and other factors used in the valuation process.

Please refer to Note 34 for details on valuation process and the fair value hierarchy of the Group's financial instruments measured at fair value.

**(c) Goodwill**

The Group performs an impairment review to ensure that the carrying amount of the CGU to which goodwill is allocated, does not exceed the recoverable amount of the CGU. Note 26 provides details of goodwill as of the reporting date.

The recoverable amount represents the present value of the estimated future cash flows expected to arise from continuing operations. Therefore, in arriving at the recoverable amount, management exercises judgment in estimating the future cash flows, growth rate and discount rate.

#### (d) Income taxes

Judgement is involved in determining the group-wide provision for income taxes. The Group recognises liabilities for expected tax issues based on reasonable estimates of whether additional taxes will be due. Note 31 provides details of the Group's deferred tax assets / liabilities.

#### (e) Provisions

Judgement is needed to determine if provision for compensation to certain customers who had bought structured investments from the Group should be recorded in accordance with the requirements in HKAS 37 Provisions, Contingent Liabilities and Contingent Assets. In making this judgement, the Group evaluates the likelihood and estimated amount of outflow of resources which will be required to settle the obligation with reference to factors such as historical settlement experience, arrangement with regulators and advice from legal counsel.

### 4 NET INTEREST INCOME

In HK\$ millions	2014	2013
Interest income on listed investments	295	357
Interest income on unlisted investments	182	121
Other interest income	6,351	5,832
Total interest income (a)	6,828	6,310
Interest expense on subordinated liability (Note 32)	116	118
Other interest expense	2,087	1,766
Total interest expense (b)	2,203	1,884
Net interest income	4,625	4,426

(a) Interest income recognised on financial assets that are not at fair value through profit or loss amounted to HK\$6,729 million (2013: HK\$6,257 million).

(b) Interest expense recognised on financial liabilities that are not at fair value through profit or loss amounted to HK\$2,189 million (2013: HK\$1,860 million).

### 5 NET FEE AND COMMISSION INCOME

In HK\$ millions	2014	2013
Fee and commission income	2,047	1,868
Less: Fee and commission expense	(314)	(258)
Net fee and commission income	1,733	1,610
Comprising:		
– Wealth Management	580	567
– Trade and transaction services (a)	482	464
– Loan Related	274	246
– Cards (b)	284	224
– Stock broking	39	40
– Investment banking	8	10
– Others	66	59
Total net fee and commission income	1,733	1,610

(a) Trade and transaction services includes trade & remittances, guarantees and deposit-related fees

(b) Gross cards fees are net of interchange fees paid

Of which:

Fee and commission income arising from:

– Financial assets or financial liabilities not at fair value through profit or loss	822	704
– Trust or other fiduciary activities	17	23

Fee and commission expense arising from:

– Financial assets or financial liabilities not at fair value through profit or loss	236	199
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### 6 NET INCOME FROM FINANCIAL INSTRUMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS

In HK\$ millions	2014	2013
Net trading income		
– Foreign exchange	1,368	1,483
– Interest rates, credit, equities and others	58	343
	1,426	1,826
Net loss from financial instruments designated at fair value through profit or loss	(37)	(132)
	1,389	1,694

**7 NET INCOME FROM INVESTMENT SECURITIES**

In HK\$ millions	2014	2013
Debt securities		
– Available-for-sale	127	14
– Loans and receivables	2	–
Equity securities	51	65
	<b>180</b>	79
Of which dividend income from:		
– Listed investments	5	2
– Unlisted investments	18	17
	<b>23</b>	19

**8 OTHER INCOME**

In HK\$ millions	2014	2013
Rental income	36	32
Fair value adjustment on investment properties (Note 27(a))	9	34
Net gain on disposal of properties and other fixed assets	–	275
Share of profit of a joint venture (a)	20	34
Others	53	12
	<b>118</b>	387

(a) The share of profit of a joint venture has been grouped under "Other income" in the current year.

**9 TOTAL EXPENSES**

In HK\$ millions	2014	2013
Employee benefits		
– Salaries and other short term employee benefits	2,209	1,969
– Pensions	127	112
– Share-based compensation	46	34
Premises and equipment expenses excluding depreciation		
– Rental of premises	224	214
– Others	253	253
Depreciation (Note 27(a))	196	220
Auditor's remuneration	10	10
Computerisation expenses	375	356
Other operating expenses	603	598
	<b>4,043</b>	3,766

**10 ALLOWANCES FOR CREDIT LOSSES**

In HK\$ millions	2014	2013
Individual impairment allowances on loans and advances to customers (Note 21)	134	112
Collective impairment allowances on loans and advances to customers (Note 21)	216	190
	<b>350</b>	302
Individual impairment allowances on loans and advances to customers		
– New allowances	244	247
– Release	(104)	(120)
– Recoveries	(6)	(15)
	<b>134</b>	112
Collective impairment allowances on loans and advances to customers		
– New allowances	343	272
– Releases	(96)	(60)
– Recoveries	(31)	(22)
	<b>216</b>	190

**11 DIRECTORS' EMOLUMENTS**

The aggregate amounts of emoluments paid or payable to directors of the Bank during the year are as follows:

In HK\$ millions	2014	2013
Fees (a)	3	3
Salaries, housing and other allowances and benefits (b)	21	18
Pensions	1	1
	<b>25</b>	22

(a) The Directors' fees are payable in 2015 to eligible persons who acted as Directors of DBS Bank (Hong Kong) Limited during the year ended 31 December 2014. Such fees are subject to the approval of the shareholders of DBS Bank (Hong Kong) Limited.

(b) The amount included cash bonus accrued during the year, to be paid in the following year. Such cash bonus is subject to the approval of DBSH Board of Directors.

**12 INCOME TAX EXPENSE****(a) Income tax expense in the consolidated income statement is comprised of:**

In HK\$ millions	2014	2013
Hong Kong profits tax		
– Current year	<b>591</b>	632
– Overprovision in prior years	<b>(14)</b>	(27)
Overseas tax		
– Current year	<b>16</b>	6
Current income tax	<b>593</b>	611
Deferred income tax (Note 31(b))	<b>2</b>	(7)
	<b>595</b>	604

Hong Kong profits tax has been provided at 16.5% (2013: 16.5%) on the estimated assessable profits for the year. Taxation for overseas subsidiaries and branch are charged at the appropriate current rates of taxation ruling in the countries in which they operate.

**(b) The deferred income tax charged / (credited) to the consolidated income statement comprises the following temporary differences:**

In HK\$ millions	2014	2013
Accelerated depreciation allowances	<b>14</b>	7
Impairment allowances	<b>(8)</b>	(6)
Share-based compensation	<b>(5)</b>	–
Accrued expenses	<b>1</b>	(8)
	<b>2</b>	(7)

**(c) The tax on the Group's profit before income tax differs from the theoretical amount that would arise using the Hong Kong profits tax rate of 16.5% (2013: 16.5%) is as follows:**

In HK\$ millions	2014	2013
Profit before income tax	<b>3,652</b>	4,128
Tax calculated at tax rate of 16.5% (2013: 16.5%)	<b>603</b>	681
Effect of different tax rates in other countries	<b>(3)</b>	(2)
Income not subject to tax	<b>(10)</b>	(53)
Expenses not deductible for tax purposes	<b>17</b>	19
Overprovision in prior years	<b>(14)</b>	(27)
Others	<b>2</b>	(14)
Income tax expense	<b>595</b>	604

**13 PROFIT ATTRIBUTABLE TO SHAREHOLDERS**

The profit attributable to shareholders is dealt with in the financial statements of the Bank to the extent of HK\$2,999 million (2013: HK\$3,537 million).

**14 DIVIDEND**

In HK\$ millions	2014	2013
First interim dividend paid of HK\$0.143 per share (2013: HK\$0.171 per share)	<b>1,000</b>	1,200
Second interim dividend paid of HK\$0.071 per share	<b>500</b>	–
	<b>1,500</b>	1,200

## 15 CLASSIFICATION OF FINANCIAL INSTRUMENTS

In HK\$ millions	Group					Total
	Held for trading	Designated at fair value through profit or loss	Available-for-sale	Loans and receivables/ amortised cost	Hedging derivatives	
<b>2014</b>						
<b>Assets</b>						
Cash and balances with central banks	-	-	-	1,969	-	1,969
Government securities and treasury bills	4,196	-	18,717	-	-	22,913
Due from banks	-	-	-	79,478	-	79,478
Derivatives	4,906	-	-	-	188	5,094
Bank and corporate securities	2,338	-	7,673	1,880	-	11,891
Loans and advances to customers	-	-	-	184,569	-	184,569
Other financial assets	-	-	-	4,600	-	4,600
Total financial assets	11,440	-	26,390	272,496	188	310,514
Non-financial assets						2,926 (a)
Total assets						313,440
<b>Liabilities</b>						
Due to banks	-	-	-	4,277	-	4,277
Deposits and balances from customers	-	4,079	-	248,180	-	252,259
Derivatives	5,136	-	-	-	80	5,216
Other financial liabilities	3,738	-	-	5,955	-	9,693
Certificates of deposit issued	-	-	-	4,961	-	4,961
Subordinated liability	-	-	-	4,189	-	4,189
Total financial liabilities	8,874	4,079	-	267,562	80	280,595
Non-financial liabilities						14 (b)
Total liabilities						280,609

(a) Includes goodwill and intangibles, properties and other assets, current tax assets and deferred tax assets

(b) Includes current tax liabilities

In HK\$ millions	Bank					Total
	Held for trading	Designated at fair value through profit or loss	Available-for-sale	Loans and receivables/ amortised cost	Hedging derivatives	
<b>2014</b>						
<b>Assets</b>						
Cash and balances with central banks	-	-	-	1,969	-	1,969
Government securities and treasury bills	4,196	-	18,717	-	-	22,913
Due from banks	-	-	-	79,478	-	79,478
Derivatives	4,906	-	-	-	188	5,094
Bank and corporate securities	2,338	-	7,673	1,880	-	11,891
Loans and advances to customers	-	-	-	184,569	-	184,569
Other financial assets	-	-	-	4,608	-	4,608
Total financial assets	11,440	-	26,390	272,504	188	310,522
Non-financial assets						3,332 (a)
Total assets						313,854
<b>Liabilities</b>						
Due to banks	-	-	-	4,277	-	4,277
Deposits and balances from customers	-	4,079	-	248,180	-	252,259
Derivatives	5,136	-	-	-	80	5,216
Other financial liabilities	3,738	-	-	6,826	-	10,564
Certificates of deposit issued	-	-	-	4,961	-	4,961
Subordinated liability	-	-	-	4,189	-	4,189
Total financial liabilities	8,874	4,079	-	268,433	80	281,466
Non-financial liabilities						14 (b)
Total liabilities						281,480

(a) Includes investment in subsidiaries, properties and other assets and deferred tax assets

(b) Includes current tax liabilities

In HK\$ millions	Group					Total
	Held for trading	Designated at fair value through profit or loss	Available-for-sale	Loans and receivables/ amortised cost	Hedging derivatives	
<b>2013</b>						
<b>Assets</b>						
Cash and balances with central banks	–	–	–	995	–	995
Government securities and treasury bills	3,448	–	12,658	–	–	16,106
Due from banks	–	–	–	62,341	–	62,341
Derivatives	8,889	–	–	–	195	9,084
Bank and corporate securities	854	–	9,707	2,171	–	12,732
Loans and advances to customers	–	–	–	200,254	–	200,254
Other financial assets	–	–	–	4,118	–	4,118
Total financial assets	13,191	–	22,365	269,879	195	305,630
Non-financial assets						3,029 (a)
Total assets						308,659
<b>Liabilities</b>						
Due to banks	–	–	–	4,751	–	4,751
Deposits and balances from customers	–	8,122	–	230,269	–	238,391
Derivatives	8,944	–	–	–	147	9,091
Other financial liabilities	3,122	–	–	10,118	–	13,240
Certificates of deposit issued	–	–	–	7,564	–	7,564
Subordinated liability	–	–	–	4,187	–	4,187
Total financial liabilities	12,066	8,122	–	256,889	147	277,224
Non-financial liabilities						168 (b)
Total liabilities						277,392

(a) Includes investment in a joint venture, properties and other assets and deferred tax assets

(b) Includes current tax liabilities

In HK\$ millions	Bank					Total
	Held for trading	Designated at fair value through profit or loss	Available-for-sale	Loans and receivables/ amortised cost	Hedging derivatives	
<b>2013</b>						
<b>Assets</b>						
Cash and balances with central banks	–	–	–	995	–	995
Government securities and treasury bills	3,448	–	12,658	–	–	16,106
Due from banks	–	–	–	62,338	–	62,338
Derivatives	8,889	–	–	–	195	9,084
Bank and corporate securities	854	–	9,707	2,171	–	12,732
Loans and advances to customers	–	–	–	200,254	–	200,254
Other financial assets	–	–	–	4,127	–	4,127
Total financial assets	13,191	–	22,365	269,885	195	305,636
Non-financial assets						2,705 (a)
Total assets						308,341
<b>Liabilities</b>						
Due to banks	–	–	–	4,751	–	4,751
Deposits and balances from customers	–	8,122	–	230,269	–	238,391
Derivatives	8,944	–	–	–	147	9,091
Other financial liabilities	3,122	–	–	10,199	–	13,321
Certificates of deposit issued	–	–	–	7,564	–	7,564
Subordinated liability	–	–	–	4,187	–	4,187
Total financial liabilities	12,066	8,122	–	256,970	147	277,305
Non-financial liabilities						168 (b)
Total liabilities						277,473

(a) Includes investment in subsidiaries and a joint venture, properties and other assets and deferred tax assets

(b) Includes current tax liabilities

**16 CASH AND BALANCES WITH CENTRAL BANKS**

In HK\$ millions	Group and Bank	
	2014	2013
Cash in hand	<b>483</b>	503
Balances with central banks	<b>1,486</b>	492
	<b>1,969</b>	995

**17 GOVERNMENT SECURITIES AND TREASURY BILLS**

In HK\$ millions	Group and Bank		Total
	Held for trading	Available-for-sale	
<b>2014</b>			
Treasury bills	<b>2,591</b>	<b>11,621</b>	<b>14,212</b>
Other debt securities	<b>1,605</b>	<b>7,096</b>	<b>8,701</b>
	<b>4,196</b>	<b>18,717</b>	<b>22,913</b>

Of which:

– listed in Hong Kong, at fair value	<b>1,253</b>	<b>137</b>	<b>1,390</b>
– listed outside Hong Kong, at fair value	<b>3</b>	<b>1,917</b>	<b>1,920</b>
– unlisted, at fair value	<b>2,940</b>	<b>16,663</b>	<b>19,603</b>
	<b>4,196</b>	<b>18,717</b>	<b>22,913</b>

Analysed by issuer as follows:

– Sovereigns	<b>4,196</b>	<b>18,717</b>	<b>22,913</b>
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Analysed by rating agency designation as follows:

– AAA	–	<b>3,150</b>	<b>3,150</b>
– AA- to AA+	<b>4,196</b>	<b>15,286</b>	<b>19,482</b>
– Unrated	–	<b>281</b>	<b>281</b>
	<b>4,196</b>	<b>18,717</b>	<b>22,913</b>

In HK\$ millions	Group and Bank		Total
	Held for trading	Available-for-sale	
2013			
Treasury bills	1,652	9,264	10,916
Other debt securities	1,796	3,394	5,190
	3,448	12,658	16,106

Of which:

– listed in Hong Kong, at fair value	1,661	187	1,848
– listed outside Hong Kong, at fair value	40	1,984	2,024
– unlisted, at fair value	1,747	10,487	12,234
	3,448	12,658	16,106

Analysed by issuer as follows:

– Sovereigns	3,448	12,658	16,106
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Analysed by rating agency designation as follows:

– AAA	–	1,984	1,984
– AA- to AA+	3,448	10,305	13,753
– Unrated	–	369	369
	3,448	12,658	16,106

The ratings refer to Standard & Poor's ratings (or their equivalent) to the respective issues of the securities, while in the absence of such issue ratings, ratings designated for the issuers are reported.

As at 31 December 2014 and 2013, there were no impaired, overdue, or rescheduled available-for-sale financial assets.

**18 DUE FROM BANKS**

In HK\$ millions	Group		Bank	
	2014	2013	2014	2013
Balances with banks	<b>4,234</b>	4,836	<b>4,234</b>	4,836
Placements with and advances to banks				
Remaining maturity				
– Within one month	<b>27,696</b>	22,455	<b>27,696</b>	22,452
– One year or less but over one month	<b>46,300</b>	35,050	<b>46,300</b>	35,050
– Over one year	<b>1,248</b>	–	<b>1,248</b>	–
	<b>75,244</b>	57,505	<b>75,244</b>	57,502
Total	<b>79,478</b>	62,341	<b>79,478</b>	62,338

## 19 BANK AND CORPORATE SECURITIES

In HK\$ millions	Held for trading	Group and Bank Available-for-sale	Loans and receivables	Total
<b>2014</b>				
Certificate of deposit held	688	–	–	688
Other debt securities	1,650	7,643	1,880	11,173
Debt securities	2,338	7,643	1,880	11,861
Equity securities	–	30	–	30
	2,338	7,673	1,880	11,891
Of which:				
Debt securities				
– Listed in Hong Kong, at fair value	724	1,086	–	1,810
– Listed outside Hong Kong, at fair value	609	3,539	–	4,148
– Listed outside Hong Kong, at cost	–	–	1,880	1,880
– Unlisted, at fair value	1,005	3,002	–	4,007
– Unlisted, at cost	–	16	–	16
	2,338	7,643	1,880	11,861
Equity securities				
– Unlisted, at cost	–	30	–	30
	–	30	–	30
	2,338	7,673	1,880	11,891
Analysed by issuer as follows:				
– Public sector entities	–	429	1,762	2,191
– Banks	1,649	4,883	–	6,532
– Corporates	689	2,345	118	3,152
– Others	–	16	–	16
	2,338	7,673	1,880	11,891
Analysed by rating agency designation as follows:				
– AAA	–	4,581	–	4,581
– AA- to AA+	443	544	–	987
– A- to A+	1,353	2,082	–	3,435
– BBB to BBB+	205	233	118	556
– Unrated	337	203	1,762	2,302
	2,338	7,643	1,880	11,861

In HK\$ millions	Held for trading	Group and Bank Available-for-sale	Loans and receivables	Total
2013				
Certificate of deposit held	38	1,804	–	1,842
Other debt securities	816	7,833	2,171	10,820
Debt securities	854	9,637	2,171	12,662
Equity securities	–	70	–	70
	854	9,707	2,171	12,732
Of which:				
Debt securities				
– Listed in Hong Kong, at fair value	238	980	–	1,218
– Listed outside Hong Kong, at fair value	331	4,158	–	4,489
– Listed outside Hong Kong, at cost	–	–	1,968	1,968
– Unlisted, at fair value	285	4,484	–	4,769
– Unlisted, at cost	–	15	203	218
	854	9,637	2,171	12,662
Equity securities				
– Listed in Hong Kong, at fair value	–	40	–	40
– Unlisted, at cost	–	30	–	30
	–	70	–	70
	854	9,707	2,171	12,732
Analysed by issuer as follows:				
– Public sector entities	–	650	1,847	2,497
– Banks	270	7,017	–	7,287
– Corporates	584	2,025	324	2,933
– Others	–	15	–	15
	854	9,707	2,171	12,732
Analysed by rating agency designation as follows:				
– AAA	–	3,465	–	3,465
– AA- to AA+	193	2,190	–	2,383
– A- to A+	186	3,721	–	3,907
– BBB to BBB+	119	60	324	503
– Unrated	356	201	1,847	2,404
	854	9,637	2,171	12,662

The ratings refer to Standard & Poor's ratings (or their equivalent) to the respective issues of the securities, while in the absence of such issue ratings, ratings designated for the issuers are reported.

As at 31 December 2014, the fair value of the above debt securities classified as loans and receivables is HK\$1,887 million (2013: HK\$2,218 million).

In 2008, certain debt securities have been reclassified from available-for-sale category to loans and receivables category, the interest income and exchange gain arising from these debt securities recognised in the income statement for the year ended 31 December 2014 were HK\$10 million (2013: HK\$22 million) and HK\$34,000 (2013: HK\$102,000) respectively. Exchange gain or loss arising from these debt securities was managed in conjunction with matched funding where the resulting net exchange gain or loss was insignificant to the income statement.

The fair value gain that would have been recognised in the other comprehensive income if the debt securities had not been reclassified would be HK\$83,000 (2013: HK\$7 million).

As at 31 December 2014 and 2013, there were no impaired, overdue or rescheduled available-for-sale and loans and receivables financial assets.

## 20 LOANS AND ADVANCES TO CUSTOMERS

In HK\$ millions	Group and Bank	
	2014	2013
Gross loans and advances to customers	<b>185,968</b>	201,760
Less: Impairment allowances		
– Individually assessed (Note 21)	<b>(569)</b>	(793)
– Collectively assessed (Note 21)	<b>(830)</b>	(713)
	<b>184,569</b>	200,254
Comprising:		
– Trade bills	<b>27,078</b>	48,701
– Loans	<b>157,491</b>	151,553
	<b>184,569</b>	200,254

## Loans and advances to customers include finance leases and hire purchase contracts receivables and are analysed as follows:

In HK\$ millions	Group and Bank	
	2014	2013
Gross investments in finance leases and hire purchase contracts receivables:		
– Not later than one year	<b>927</b>	1,077
– Later than one year and not later than five years	<b>2,140</b>	2,411
– Later than five years	<b>6,797</b>	6,839
	<b>9,864</b>	10,327
Unearned future finance income	<b>(16)</b>	(24)
Net investments in finance leases and hire purchase contracts receivables	<b>9,848</b>	10,303
The net investments in finance leases and hire purchase contracts receivables are analysed as follows:		
– Not later than one year	<b>919</b>	1,064
– Later than one year and not later than five years	<b>2,132</b>	2,400
– Later than five years	<b>6,797</b>	6,839
	<b>9,848</b>	10,303

The unguaranteed residual values included in the gross investments in finance leases and hire purchase contracts receivables as at 31 December 2014 and 2013 are not material.

The individual impairment allowances for finance leases and hire purchase contracts receivables amounted to HK\$75 million as at 31 December 2014 (2013: HK\$62 million).

## 21 IMPAIRMENT ALLOWANCES ON LOANS AND ADVANCES TO CUSTOMERS

In HK\$ millions	Individually assessed	Group Collectively assessed	Total
As at 1 January 2014	793	713	1,506
Amounts written off	(353)	(231)	(584)
Recoveries of loans and advances written off in previous years	6	31	37
Net charge to consolidated income statement (Note 10)	134	216	350
Others	(11)	51	40
Additions through acquisition	–	50	50
As at 31 December 2014	569	830	1,399
As at 1 January 2013	899	602	1,501
Amounts written off	(227)	(167)	(394)
Recoveries of loans and advances written off in previous years	15	22	37
Net charge to consolidated income statement (Note 10)	112	190	302
Others	(6)	66	60
As at 31 December 2013	793	713	1,506

In HK\$ millions	Individually assessed	Bank Collectively assessed	Total
As at 1 January 2014	793	713	1,506
Amounts written off	(353)	(220)	(573)
Recoveries of loans and advances written off in previous years	6	31	37
Net charge to consolidated income statement	134	249	383
Others	(11)	57	46
As at 31 December 2014	569	830	1,399
As at 1 January 2013	899	602	1,501
Amounts written off	(227)	(167)	(394)
Recoveries of loans and advances written off in previous years	15	22	37
Net charge to consolidated income statement	112	190	302
Others	(6)	66	60
As at 31 December 2013	793	713	1,506

## 22 OTHER ASSETS

In HK\$ millions	Group		Bank	
	2014	2013	2014	2013
Accrued interest receivables	543	457	543	457
Acceptances	1,871	2,024	1,871	2,024
Current income tax assets (Note 31(a))	4	–	–	–
Deferred tax assets (Note 31(b))	41	39	41	39
Others	2,186	1,637	2,186	1,637
	4,645	4,157	4,641	4,157

## 23 SUBSIDIARIES

In HK\$ millions	Bank	
	2014	2013
Unlisted shares, at cost after impairment	607	39
Amounts due from subsidiaries	8	9
	615	48
Amounts due to subsidiaries	874	83

During the year, the subsidiaries have maintained deposit accounts with the Bank under the normal course of business. The other amounts due from / to subsidiaries are repayable on demand and interest free.

The main operating subsidiaries of the Group, which are wholly and directly owned by the Bank, are listed below:

Name of company	Place of incorporation	Place of operation	Particulars of issued share capital	Principal activities
Ting Hong Nominees Limited	Hong Kong	Hong Kong	10,000 shares	Provision of nominee, trustee and agency services
Overseas Trust Bank Nominees Limited	Hong Kong	Hong Kong	50,000 shares	Provision of nominee services
DBS COMPASS Limited	British Virgin Islands	Hong Kong	500,000 class A shares of HK\$1 each  500,000 class B shares of HK\$1 each	Provision of credit card services

### Acquisition of DBS COMPASS Limited (formerly known as Hutchison DBS Card Limited)

On 16 June 2014, the Group acquired the remaining 50% stake in DBS COMPASS Limited (Note 24) for a cash consideration of HK\$546 million from Whampoa Limited. A goodwill of HK\$168 million and intangible asset of HK\$35 million were recognised on acquisition (Note 26) and a profit of HK\$17 million was recognised on revaluation of the existing stake, as required under HKFRS 3. The Group accounts for the DBS COMPASS Limited using equity method before the acquisition and consolidates the results following the acquisition.

Subsequent to the acquisition, the credit card business of DBS COMPASS Limited was transferred to the Bank.

### Disposal of interests in subsidiaries

During the year, the Group disposed of the following subsidiaries and there has no material impact from these divestments:

DBS Trustee H.K. (Jersey) Limited  
 DBS Corporate Services (Hong Kong) Limited  
 DHJ Management Limited  
 DNZ Limited  
 Kingly Management Limited  
 JT Administration Limited  
 Kenson Asia Limited  
 Market Success Limited  
 Worldson Services Limited

## 24 INTEREST IN A JOINT VENTURE

In HK\$ millions	Group		Bank	
	2014	2013	2014	2013
Unlisted shares, at cost			–	1
Share of net assets	–	364		
Amount due to a joint venture	–	2,887	–	2,887

DBS COMPASS Limited was the only joint venture in which the Group had participated, which is an unlisted corporate entity, whose quoted market price is not available. During the year, the Group has acquired the remaining 50% stake in DBS COMPASS Limited (Note 23).

## 25 ACQUISITIONS

On 17 March 2014, DBS Bank Ltd agreed to acquire the Asian private business of Societe Generale in Singapore and Hong Kong as well as selected parts of its trustee business. The transaction was completed on 6 October 2014 where DBS Bank (Hong Kong) Limited received cash of HK\$1,007 million, being

the difference between the assets of HK\$3,123 million and liabilities of HK\$4,130 million transferred from Societe Generale Hong Kong.

## 26 GOODWILL AND INTANGIBLES

As at 31 December 2014, the carrying value of the Group's goodwill arising from acquisition of subsidiaries is allocated to the Group's cash-generating units (CGUs) or groups of CGUs as follows:

In HK\$ millions	Group 2014
Goodwill	168
Intangibles (a)	29
<b>Total goodwill and Intangibles</b>	<b>197</b>

(a) Customer and merchant relationships, arising from the acquisition of interest in DBS COMPASS Limited, with an estimated useful life of 3.5 years. At 31 December 2014, these have a remaining useful life of 3 years.

The carrying values of the CGUs are reviewed at least once a year to determine if the goodwill associated with them should be impaired. If a CGU's carrying value exceeds its recoverable value, a goodwill impairment charge is recognised in the income statement.

The recoverable value is determined based on a value-in-use calculation. The CGU's five-year projected cash flows, taking into account projected regulatory capital requirements, are discounted by its cost of capital to derive their present value. To derive the value beyond the fifth year, a long-term growth rate is imputed to the fifth-year cash flow and then discounted by the cost of capital to derive the terminal value. The long-term growth rate used does not exceed the historical long-term growth rate of the market the CGU operates in. The recoverable value is the sum of the present value of the five-year cash flows and the terminal value.

A growth rate of 4.5% and discount rate of 9.0% were assumed in the value-in-use calculation.

The process of evaluating goodwill impairment involves management judgement and prudent estimates of various factors including future cash flows as well as the cost of capital and long-term growth rates. The results can be highly sensitive to the assumptions used. Management believes that any reasonably possible change in the key assumptions would not cause the carrying amount of the operating unit to exceed its recoverable amount at 31 December 2014. However, if conditions in Hong Kong and the banking industry deteriorate and turn out to be significantly worse than anticipated in the Group's performance forecast, the goodwill may be impaired in future periods.

## 27 PROPERTIES AND OTHER FIXED ASSETS

### (a) Properties and other fixed assets movements

In HK\$ millions	Freehold land and building	Land and buildings	Group		Investment properties	Total
			Furniture, fixtures and equipment	Subtotal		
Cost or valuation						
As at 1 January 2014	23	2,571	1,258	3,852	510	4,362
Additions	–	9	235	244	–	244
Disposals	–	(10)	(282)	(292)	–	(292)
Additions through acquisition	–	–	75	75	–	75
Fair value adjustment	–	–	–	–	9	9
As at 31 December 2014	23	2,570	1,286	3,879	519	4,398
Accumulated depreciation and impairment						
As at 1 January 2014	17	823	896	1,736	–	1,736
Charge for the year	–	56	140	196	–	196
Disposals	–	(9)	(281)	(290)	–	(290)
Additions through acquisition	–	–	72	72	–	72
As at 31 December 2014	17	870	827	1,714	–	1,714
Net book value						
As at 31 December 2014	6	1,700	459	2,165	519	2,684
The analysis of cost or valuation of the above assets as at 31 December 2014 is as follows:						
At cost	23	2,570	1,286	3,879	–	3,879
At valuation	–	–	–	–	519	519
	23	2,570	1,286	3,879	519	4,398

In HK\$ millions	Freehold land and building	Land and buildings	Bank		Investment properties	Total
			Furniture, fixtures and equipment	Subtotal		
Cost or valuation						
As at 1 January 2014	23	2,571	1,258	3,852	510	4,362
Additions	–	9	235	244	–	244
Disposals	–	(10)	(255)	(265)	–	(265)
Additions through acquisition	–	–	2	2	–	2
Fair value adjustment	–	–	–	–	9	9
As at 31 December 2014	23	2,570	1,240	3,833	519	4,352
Accumulated depreciation and impairment						
As at 1 January 2014	17	823	896	1,736	–	1,736
Charge for the year	–	56	140	196	–	196
Disposals	–	(9)	(255)	(264)	–	(264)
As at 31 December 2014	17	870	781	1,668	–	1,668
Net book value						
As at 31 December 2014	6	1,700	459	2,165	519	2,684
The analysis of cost or valuation of the above assets as at 31 December 2014 is as follows:						
At cost	23	2,570	1,240	3,833	–	3,833
At valuation	–	–	–	–	519	519
	23	2,570	1,240	3,833	519	4,352

In HK\$ millions	Group			Subtotal	Investment properties	Total
	Freehold land and building	Land and buildings	Furniture, fixtures and equipment			
Cost or valuation						
As at 1 January 2013	23	2,636	1,148	3,807	476	4,283
Additions	–	10	184	194	–	194
Disposals	–	(75)	(74)	(149)	–	(149)
Fair value adjustment	–	–	–	–	34	34
As at 31 December 2013	23	2,571	1,258	3,852	510	4,362
Accumulated depreciation and impairment						
As at 1 January 2013	17	797	801	1,615	–	1,615
Charge for the year	–	56	164	220	–	220
Disposals	–	(30)	(69)	(99)	–	(99)
As at 31 December 2013	17	823	896	1,736	–	1,736
Net book value						
As at 31 December 2013	6	1,748	362	2,116	510	2,626
The analysis of cost or valuation of the above assets as at 31 December 2013 is as follows:						
At cost	23	2,571	1,258	3,852	–	3,852
At valuation	–	–	–	–	510	510
	23	2,571	1,258	3,852	510	4,362

In HK\$ millions	Bank			Subtotal	Investment properties	Total
	Freehold land and building	Land and buildings	Furniture, fixtures and equipment			
Cost or valuation						
As at 1 January 2013	23	2,636	1,148	3,807	476	4,283
Additions	–	10	184	194	–	194
Disposals	–	(75)	(74)	(149)	–	(149)
Fair value adjustment	–	–	–	–	34	34
As at 31 December 2013	23	2,571	1,258	3,852	510	4,362
Accumulated depreciation and impairment						
As at 1 January 2013	17	797	801	1,615	–	1,615
Charge for the year	–	56	164	220	–	220
Disposals	–	(30)	(69)	(99)	–	(99)
As at 31 December 2013	17	823	896	1,736	–	1,736
Net book value						
As at 31 December 2013	6	1,748	362	2,116	510	2,626
The analysis of cost or valuation of the above assets as at 31 December 2013 is as follows:						
At cost	23	2,571	1,258	3,852	–	3,852
At valuation	–	–	–	–	510	510
	23	2,571	1,258	3,852	510	4,362

The net book values of land and buildings and investment properties held by the Group and the Bank are as follows:

In HK\$ millions	Group and Bank			
	2014		2013	
	Land and buildings	Investment properties	Land and buildings	Investment properties
Freeholds				
Held outside Hong Kong	6	–	6	–
Leaseholds				
Held in Hong Kong				
– Leases of over 50 years	188	442	187	434
– Leases of between 10 to 50 years	1,510	77	1,559	76
Held outside Hong Kong				
– Leases of between 10 to 50 years	2	–	2	–
	<b>1,700</b>	<b>519</b>	1,748	510

#### (b) Fair value of investment properties

##### (i) Fair value hierarchy

The following table presents the fair value of the Group's investment properties measured at the end of the reporting period on a recurring basis, categorised into the three-level fair value hierarchy as defined by in HKFRS 13. The level into which a fair value measurement is classified, is determined with reference to the observability and significance of the inputs used in the valuation technique as follows:

- Level 1 valuations: Fair value measured using only Level 1 inputs i.e. unadjusted quoted prices in active markets for identical assets or liabilities at the measurement date
- Level 2 valuations: Fair value measured using Level 2 inputs i.e. observable inputs which fail to meet Level 1, and not using significant unobservable inputs. Unobservable inputs are inputs for which market data are not available
- Level 3 valuations: Fair value measured using significant unobservable inputs

In HK\$ millions	Group and Bank			Total
	Level 1	Level 2	Level 3	
<b>2014</b>				
Investment properties	–	–	519	519
<b>2013</b>				
Investment properties	–	100	410	510

During the year, the Group transferred investment properties of HK\$102 million from Level 2 to Level 3 as a result of reduced market activity (2013: Nil). The Group's policy is to recognise transfer between levels of fair value hierarchy as at the end of the reporting period in which they occur.

The fair value of the investment properties has been determined based on valuations performed by A.G. Wilkinson & Associates (Surveyors). The fair value represents the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (i.e. an exit price). It is an estimated amount for which an asset or liability should exchange on the valuation date between a willing buyer and a willing seller in an arm's length transaction after proper marketing where the parties had each acted knowledgeably, prudently and without compulsion.

##### (ii) Valuation techniques and inputs used in Level 2 fair value measurements

The fair value of investment properties is determined using the market comparison method by reference to recent sales price of comparable properties on a price per square foot basis using market data which is publicly available.

##### (iii) Information about Level 3 fair value measurements

The fair value of investment properties is determined using the investment method by capitalising the net rental incomes derived from the existing tenancies with due allowance for reversionary income potential of the property interests. The significant unobservable input used for valuation is the market yield.

The movement during the year in the balance of these Level 3 fair value measurements is as follows:

In HK\$ millions	Group and Bank	
	2014	2013
At 1 January	410	381
Fair value adjustment	7	29
Transfers in	102	–
At 31 December	<b>519</b>	410

Fair value adjustment of investment properties is recognised in the line item "Other income" on the consolidated income statement. All the gains recognised in the income statement for the year arise from the properties held at the end of the reporting period.

**(c) Operating lease arrangements**

The Group leases out investment properties under operating leases. The leases typically run for an initial period of one to five years, and may contain an option to renew the lease after that date at which time terms will be renegotiated. None of the leases include contingent rentals.

During the year, HK\$14 million (2013: HK\$11 million) was recognised as rental income in the income statement in respect of the operating leases.

As at 31 December, the Group and the Bank had future aggregate minimum lease receipts under non-cancellable operating leases as follows:

In HK\$ millions	Group and Bank	
	2014	2013
Not later than one year	13	14
Later than one year and not later than five years	8	21
	<b>21</b>	<b>35</b>

**28 DEPOSITS AND BALANCES FROM CUSTOMERS**

In HK\$ millions	Group and Bank	
	2014	2013
Deposits from customers, at amortised cost	248,180	230,269
Structured investment deposits classified as financial liabilities designated at fair value through profit or loss (a)	4,079	8,122
	<b>252,259</b>	<b>238,391</b>
Analysed by:		
– Demand deposits and current accounts	27,151	23,097
– Savings deposits	86,942	69,739
– Time, call and notice deposits	138,166	145,555
	<b>252,259</b>	<b>238,391</b>

(a) Changes in fair value arising from changes in credit risk are determined as the amount of change in their fair value that is not attributable to changes in market conditions that give rise to market risk. Changes in market conditions that give rise to market risk include changes in benchmark interest rate, foreign exchange rate or index of prices or rates. Changes in fair value arising from changes in credit risk are considered not significant. Net unrealised loss for the financial liabilities designated at fair value through profit or loss amounted to HK\$60 million as at 31 December 2014 (2013: HK\$159 million).

**29 CERTIFICATES OF DEPOSIT ISSUED**

In HK\$ millions	Group and Bank	
	2014	2013
Certificates of deposit issued, measured at amortised cost	4,961	7,564

**30 OTHER LIABILITIES**

In HK\$ millions	Group		Bank	
	2014	2013	2014	2013
Accrued interest payable	394	388	394	388
Acceptances	1,871	2,024	1,871	2,024
Amount due to a joint venture (Note 24)	–	2,887	–	2,887
Current income tax liabilities (Note 31(a))	14	168	14	168
Payable in respect of short sale of securities	3,738	3,122	3,738	3,122
Other liabilities and provisions	3,690	4,819	3,687	4,817
	<b>9,707</b>	<b>13,408</b>	<b>9,704</b>	<b>13,406</b>

**31 TAXATION****(a) Current income tax asset and liabilities**

In HK\$ millions	Group		Bank	
	2014	2013	2014	2013
Current income tax assets				
Hong Kong profits tax recoverable	4	–	–	–
Current income tax liabilities				
Hong Kong profits tax payable	5	162	5	162
Overseas tax payable	9	6	9	6
	<b>14</b>	<b>168</b>	<b>14</b>	<b>168</b>

**(b) Deferred income tax**

The movements on the net deferred tax assets are as follows:

In HK\$ millions	Group		Bank	
	2014	2013	2014	2013
As at 1 January	39	11	39	11
Additions through acquisition	5	–	–	–
Deferred income tax (charged) / credited to income statement (Note 12(a))	(2)	7	3	7
Deferred income tax (charged) / credited to equity (Note 33(b)(ii))	(1)	13	(1)	13
Reversal of previously recognised deferred tax liability	–	8	–	8
As at 31 December	41	39	41	39

Deferred tax assets and liabilities are attributable to the following items:

In HK\$ millions	Group		Bank	
	2014	2013	2014	2013
Deferred tax assets				
Impairment allowances	106	93	106	93
Share-based compensation	13	8	13	8
Accrued expenses	7	8	7	8
	126	109	126	109
Deferred tax liabilities				
Accelerated depreciation allowances	73	59	73	59
Revaluation of investment securities	12	11	12	11
	85	70	85	70

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The deferred tax assets and liabilities are to be recovered and settled after one year and the following amounts, determined after appropriate offsetting, are shown in the balance sheet:

In HK\$ millions	Group		Bank	
	2014	2013	2014	2013
Deferred tax assets	126	109	126	109
Deferred tax liabilities	(85)	(70)	(85)	(70)
	41	39	41	39

**32 SUBORDINATED LIABILITY**

The Bank issued a subordinated loan of US\$540,000,000 to its intermediate holding company, DBS Bank Ltd on 12 December 2012. This subordinated loan will mature on 12 December 2022, with an optional repayment date on 13 December 2017 or any interest payment date thereafter until maturity. Interest is payable quarterly and is charged at USD 3-month LIBOR plus 2.5% per annum. The subordinated loan will be converted into ordinary shares at the point of non-viability as determined by the Hong Kong Monetary Authority.

On 28 August 2014, DBS Bank Ltd assigned the US\$540,000,000 subordinated loan to its parent holding company, DBS Group Holdings Ltd. Other terms and conditions of the subordinated loan facility remain unchanged. The subordinated loan is Basel III-compliant and qualifies as Tier 2 capital for the purpose of computing the Bank's capital adequacy ratios.

**33 CAPITAL AND RESERVES****(a) Share capital**

	Group and Bank			
	2014	2013		
	Number of shares (millions)	HK\$ millions	Number of shares (millions)	HK\$ millions
<b>Authorised: (i)</b>				
Ordinary shares of HK\$1 each (ii)	–	–	12,000	12,000
<b>Ordinary shares, issued and fully paid:</b>				
At 1 January	7,000	7,000	7,000	7,000
Transition to no-par value regime (iii)	–	595	–	–
At 31 December	7,000	7,595	7,000	7,000

- (i) Under the Hong Kong Companies Ordinance (Cap. 622), which commenced operation on 3 March 2014, the concept of authorised share capital no longer exists.
- (ii) In accordance with section 135 of the Hong Kong Companies Ordinance (Cap. 622), the Bank's shares no longer have a par or nominal value with effect from 3 March 2014. There is no impact on the number of shares in issue or the relative entitlement of any of the members as a result of this transition.
- (iii) In accordance with the transitional provisions set out in section 37 of Schedule 11 to Hong Kong Companies Ordinance (Cap. 622), on 3 March 2014, any amount standing to the credit of the share premium account has become part of the Bank's share capital.

**(b) Reserves**

In HK\$ millions	Group		Bank	
	2014	2013	2014	2013
<b>Share premium</b>				
As at 1 January	595	595	595	595
Transition to no-par value regime (Note 33(a)(iii))	(595)	–	(595)	–
As at 31 December	–	595	–	595
<b>Other reserves</b>				
(i) Capital reserve				
As at 1 January and 31 December	12	12	–	–
(ii) Investments revaluation reserve from available-for-sale financial investments				
As at 1 January	54	126	54	126
Net valuation taken to equity	159	(36)	159	(36)
Amortisation of reserve to income statement arising from reclassification of available-for-sale financial investments to loans and receivables	1	1	1	1
Transferred to income statement	(152)	(50)	(152)	(50)
Deferred income tax (charged) / credited to equity	(1)	13	(1)	13
As at 31 December	61	54	61	54
(iii) Properties revaluation reserve				
As at 1 January and 31 December	98	98	98	98
(iv) General reserve				
As at 1 January and 31 December	2,399	2,399	2,285	2,285
<b>Total other reserves</b>	<b>2,570</b>	<b>2,563</b>	<b>2,444</b>	<b>2,437</b>
<b>Retained earnings</b>				
As at 1 January	21,109	18,785	20,836	18,499
Profit attributable to shareholders	3,057	3,524	2,999	3,537
Dividend (Note 14)	(1,500)	(1,200)	(1,500)	(1,200)
As at 31 December	22,666	21,109	22,335	20,836
<b>Total reserves</b>	<b>25,236</b>	<b>24,267</b>	<b>24,779</b>	<b>23,868</b>

The investments revaluation reserve represents the cumulative net change in the fair value of available-for-sale financial investments.

Properties revaluation reserve represents revaluation surplus arising on transfer of the land and buildings to investment properties.

The general reserve is comprised of transfers from the previous years' retained earnings.

As at 31 December 2014, HK\$1,327 million (2013: HK\$1,304 million) was earmarked as the regulatory reserve from the retained earnings. The regulatory reserve is maintained to satisfy the provisions of the Banking Ordinance for prudential supervision purposes. Movements in the reserve are made directly through retained earnings and in consultation with the Hong Kong Monetary Authority.

**34 FAIR VALUE OF FINANCIAL INSTRUMENTS****(a) Valuation process**

The valuation processes used by the Group are governed by the Valuation, the Rates and the Reserves frameworks. These frameworks apply to financial assets and liabilities where mark-to-market or model valuation is required. The overall framework is endorsed by Group Market and Liquidity Risk Committee and Risk Executive Committee before approval by the Board Risk Management Committee.

The Rates framework governs the daily revaluation of all financial assets and liabilities that are fair value measured, covering both market prices as well as model inputs. Financial assets and liabilities are marked directly using reliable and independent market prices or by using reliable and independent market parameters (as model inputs) in conjunction with a valuation model. Products with a liquid market or those traded via an exchange will fall under the former while most over-the-counter ("OTC") exotic products will form the latter.

Valuation models go through an assurance process carried out by the Risk Management Group, independent of the model developers. This assurance process would review the underlying methodology including its logic and conceptual soundness together with the model inputs and outputs. Model assurances are conducted prior to implementation and subject to regular review or when there are significant changes arising from market or portfolio changes. Where necessary, the Group also imposes model reserves and other adjustments in determining fair value. Models are approved by the Group Market and Liquidity Risk Committee.

The majority of OTC derivatives are traded in active markets. Valuations are determined using generally accepted models (discounted cash flows, Black-Scholes model, interpolation techniques) based on quoted market prices for similar instruments or underlyings.

A process of independent price verification (“IPV”) is in place to establish the accuracy of the market parameters used when the marking is performed by the Front Office. The IPV process entails independent checks to compare traders’ marks to independent sources such as broker/dealer sources or market consensus providers. The results of the IPV are reviewed by independent control functions on a monthly basis.

For illiquid complex financial instruments where mark-to-market is not possible, the Group will value these products using an approved valuation model. Prices and parameters used as inputs to the model or to any intermediate technique involving a transformation process must be derived from approved market reliable sources. Where possible, the inputs must be checked against multiple sources for reliability and accuracy. Reliance will be placed on the model assurance framework established by Risk Management Group for assurance of valuation models as fit for purpose.

The Group uses various market accepted benchmark interest rates such as LIBOR and Swap Offer Rates to determine the fair value of the financial instruments.

Where unobservable inputs are used in these models resulting in Level 3 classification, valuation adjustments or reserves will be taken for the purpose of adjusting for uncertainty in valuations. Valuation adjustment or reserve methodologies are used to substantiate the unobservable inputs and attempt to quantify the level of uncertainty in valuations. Such methodologies are governed by the Reserve Framework and require approval by the Group Market and Liquidity Risk Committee.

The main valuation adjustments and reserves are described below:

*Model and Parameter Uncertainty adjustments*

Valuation uncertainties may occur during fair value measurement either due to uncertainties in the required input parameters or uncertainties in the modeling methods used in valuation process. In such situations, adjustments may be necessary to take these factors into account.

For example, where market data such as prices or rates for an instrument are no longer observable after an extended period of time, these inputs used to value the financial instruments may no longer be relevant in the current market conditions. In such situations, adjustments may be necessary to address the pricing uncertainty arising from the use of stale market data inputs.

*Credit risk adjustment*

Credit risk adjustment is incorporated into derivative valuations to reflect the impact on fair value of counterparty credit risk. Credit risk adjustment is based upon the creditworthiness of the counterparties, magnitude of the current or potential exposure

on the underlying transactions, netting arrangements, collateral arrangements, and the maturity of the underlying transactions.

*Day 1 profit or loss (P&L) reserve*

In situations where the market for an instrument is not active and its fair value is established using a valuation model based on significant unobservable market parameters, Day 1 P&L reserve is utilised to defer the P&L arising from the difference between the transaction price and the model value. A market parameter is defined as being significant when its impact on the Day 1 P&L is greater than an internally determined threshold. The Day 1 P&L reserve is released to profit or loss as the parameters become observable or the transaction closed out or amortised over the duration of the transaction. At year end, the unamortised Day 1 P&L is not material.

*Bid Offer adjustment*

The Group often holds, at varying points in time, both long or short positions in financial instruments which are valued using mid market levels. Bid offer adjustments are then made to adjust net open position valuations to the respective bid or offer levels as appropriate.

**(b) Fair value hierarchy**

The fair value hierarchy accords the highest level to observable inputs such as unadjusted quoted prices in active markets for identical assets or liabilities and the lowest level to unobservable inputs. The fair value measurement of each financial instrument is categorised in accordance to the same level of the fair value hierarchy as the input with the lowest level that is significant to the entire measurement. If unobservable inputs are deemed as significant, the financial instrument will be categorised as Level 3.

Financial instruments that are valued using quoted prices in active markets are classified as Level 1 of the valuation hierarchy. These would include government and sovereign securities, listed equities and corporate debt securities which are actively traded. Derivatives contracts which are traded in an active exchange market are also classified as Level 1 of the valuation hierarchy.

Where fair value is determined using quoted market prices in less active markets or quoted prices for similar assets and liabilities, such instruments are generally classified as Level 2. In cases where quoted prices are generally not available, the Group will determine the fair value based on valuation techniques that use market parameters as inputs including but not limited to yield curves, volatilities and foreign exchange rates. The majority of valuation techniques employ only observable market data and so reliability of the fair value measurement is high. These would include corporate debt securities, repurchase, reverse repurchase agreements and most of the Group’s over-the-counter derivatives.

The Group classifies financial instruments as Level 3 when there is reliance on unobservable inputs to the valuation model attributing to a significant contribution to the instrument value. These would include all input parameters which are derived from historical data such as correlation or volatilities as well as unquoted equity securities. The fair value of unquoted equity securities is measured in comparison with recent transactions in the equity of the company in question or comparable companies in similar industries. Level 3 inputs also include all quoted security prices that have not been updated for more than 3 months, quoted proxies in active markets for non-similar asset classes (e.g. bonds marked over credit default swap spreads), as well as prices/valuations that are obtained from counterparties. Valuation reserves or pricing adjustments where applicable will be used to converge to fair value.

The following table presents assets and liabilities measured at fair value, classified by level of the fair value hierarchies:

In HK\$ millions	Group and Bank			Total
	Level 1	Level 2	Level 3	
<b>2014</b>				
<b>Assets</b>				
Financial assets at fair value through profit or loss				
– Government securities and treasury bills	<b>4,196</b>	–	–	<b>4,196</b>
– Bank and corporate debt securities	<b>1,636</b>	<b>702</b>	–	<b>2,338</b>
Available-for-sale financial assets				
– Government securities and treasury bills	<b>18,436</b>	<b>281</b>	–	<b>18,717</b>
– Bank and corporate debt securities	<b>7,627</b>	–	–	<b>7,627</b>
Derivatives	–	<b>5,094</b>	–	<b>5,094</b>
<b>Liabilities</b>				
Payable in respect of short sale of securities	<b>3,738</b>	–	–	<b>3,738</b>
Financial liabilities designated at fair value through profit or loss	–	<b>4,079</b>	–	<b>4,079</b>
Derivatives	–	<b>5,216</b>	–	<b>5,216</b>

In HK\$ millions	Group and Bank			Total
	Level 1	Level 2	Level 3	
<b>2013</b>				
<b>Assets</b>				
Financial assets at fair value through profit or loss				
– Government securities and treasury bills	3,448	–	–	3,448
– Bank and corporate debt securities	842	12	–	854
Available-for-sale financial assets				
– Government securities and treasury bills	12,289	369	–	12,658
– Bank and corporate debt securities	9,252	370	–	9,622
– Equity securities	40	–	–	40
Derivatives	–	9,084	–	9,084
<b>Liabilities</b>				
Payable in respect of short sale of securities	3,122	–	–	3,122
Financial liabilities designated at fair value through profit or loss	–	8,122	–	8,122
Derivatives	–	9,091	–	9,091

During the year, there were no transfers between Level 1 and Level 2, or transfer into or out of Level 3. The Group's policy is to recognise transfers between the levels of the fair value hierarchy as at the end of the reporting period during the change occurred.

**(c) Fair value of financial assets and liabilities not carried at fair value**

For financial assets and liabilities not carried at fair value on the financial statements, the Group has ascertained that their fair values were not materially different from the carrying amounts at year end as shown below. The bases of arriving at their fair values are as follows:

(i) Due from banks

The estimated fair value of placements with and advances to banks is based on the discounted cash flows using the prevailing money market interest rates for placements and advances with similar remaining maturity.

## (ii) Loans and advances to customers

The fair value approximates their carrying amount as majority of the loans and advances to customers are on floating rate terms.

## (iii) Bank and corporate securities – loans and receivables

The fair values are determined based on independent market quotes, where available. Where market prices are not available, fair values are estimated using discounted cash flow method. The fair value is set out in Note 19.

## (iv) Due to banks and deposits and balances from customers

The estimated fair value of deposits with no stated maturity, which includes non-interest-bearing deposits, is the amount repayable on demand. The estimated fair value of deposits and other borrowings with fixed interest rates is based on discounted cash flows using prevailing interest rates with similar remaining maturity.

## (v) Certificates of deposit issued

The estimated fair value of certificates of deposit issued is based on discounted cash flows using the prevailing money market interest rates with similar remaining maturity.

## (vi) Subordinated liability

The fair value of subordinated liability approximates its carrying amount as it is on floating rate term and bears interest at prevailing market interest rate.

**35 NOTES TO CONSOLIDATED CASH FLOW STATEMENT****(a) Analysis of changes in financing activities during the year**

In HK\$ millions	Certificates of deposit issued	Subordinated liability
Balance as at 1 January 2013	7,291	4,186
Cash inflow from financing activities	2,230	–
Cash outflow from financing activities	(1,784)	–
Revaluation	(179)	–
Amortisation of discount	4	–
Exchange differences and other adjustments	2	1
Balance as at 31 December 2013	<b>7,564</b>	<b>4,187</b>
Cash inflow from financing activities	<b>2,213</b>	–
Cash outflow from financing activities	<b>(4,820)</b>	–
Revaluation	<b>(5)</b>	–
Amortisation of discount	<b>9</b>	–
Exchange differences and other adjustments	–	<b>2</b>
Balance as at 31 December 2014	<b>4,961</b>	<b>4,189</b>

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

In HK\$ millions	2014	2013
Cash and balances with central banks	<b>1,969</b>	995
Due from banks		
– Balances with banks	<b>4,234</b>	4,836
– Placements with and advances to banks repayable with original maturity within three months	<b>46,358</b>	33,835
Bills and notes repayable with original maturity within three months	<b>3,005</b>	1,491
	<b>55,566</b>	41,157

**36 DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES****(a) Derivatives**

The Group uses financial derivatives to hedge the positions of the Group. It also trades in financial instruments where it takes positions in traded and over-the-counter instruments, including derivatives, to take advantage of short term market movements in bond price, currency and interest rate. The Group places trading limits on the level of exposure that can be taken in relation to both overnight and intra-day market positions. With the exception of specific hedging arrangements, foreign exchange and interest rate exposures associated with these

derivatives are normally offset by entering into counterbalancing positions, thereby controlling the variability in the net cash amounts required to liquidate market positions.

The following is a summary of each significant type of derivatives:

In HK\$ millions	Contract/ notional amount	Group and Bank Credit risk- weighted amount	Positive fair values	Negative fair values
<b>2014</b>				
<b>Derivatives held for trading</b>				
Foreign exchange derivatives				
– Forwards	208,173	3,998	1,703	1,620
– Swaps	141,063	345	407	637
– Options purchased	171,622	6,329	2,215	312
– Options written	171,150	379	312	2,222
	692,008	11,051	4,637	4,791
Interest rate derivatives				
– Swaps	28,603	220	320	329
– Options purchased	6	–	–	–
– Options written	6	–	–	–
	28,615	220	320	329
Equity derivatives	1,180	37	26	26
Total derivatives held for trading	721,803	11,308	4,983	5,146
<b>Derivatives designated and qualified as fair value hedges</b>				
Interest rate derivatives				
– Swaps	5,648	53	188	80

In HK\$ millions	Contract/ notional amount	Group and Bank Credit risk- weighted amount	Positive fair values	Negative fair values
<b>2013</b>				
Derivatives held for trading				
Foreign exchange derivatives				
– Forwards	203,371	2,863	4,278	3,896
– Swaps	139,087	303	817	1,300
– Options purchased	161,715	7,765	3,447	1
– Options written	160,943	–	1	3,477
	665,116	10,931	8,543	8,674
Interest rate derivatives				
– Futures	55	1	–	1
– Swaps	28,552	325	395	418
– Options purchased	17	–	1	–
– Options written	17	–	–	1
	28,641	326	396	420
Equity derivatives	583	6	4	4
Total derivatives held for trading	694,340	11,263	8,943	9,098
Derivatives designated and qualified as fair value hedges				
Interest rate derivatives				
– Swaps	6,648	55	195	147

The above tables include derivatives and embedded derivatives. The amounts (except credit-risk weighted amounts) are shown on a gross basis and do not take into account the effect of bilateral netting arrangements. The positive and negative fair values of embedded derivatives included in above amounted to HK\$77 million and HK\$10 million respectively (2013: HK\$54 million and HK\$154 million respectively). The contract or notional amounts of these instruments indicate the volume of transactions outstanding as at the balance sheet date; they do not represent amounts at risk.

The credit risk-weighted amounts as at 31 December 2014 and 2013 are the amounts which have been taken into account the effect of bilateral netting arrangements and have been calculated in accordance with the Banking (Capital) Rules.

#### (b) Hedging activities

As at 31 December 2014, the Group has interest rate swap agreements in place with a notional amount of HK\$5,648 million (2013: HK\$6,648 million) to hedge the exposure arising from changes in the fair value as a result of market interest rate

fluctuation of certain financial investments and certificates of deposit issued. The hedging derivatives and hedged items have similar critical terms.

The gains on the hedging instruments are HK\$63 million (2013: losses of HK\$93 million). The losses on the hedged items attributable to the hedged risk are HK\$62 million (2013: gains of HK\$93 million).

### 37 CONTINGENT LIABILITIES AND COMMITMENTS

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

In HK\$ millions	Group and Bank	
	2014	2013
Direct credit substitutes	800	1,046
Transaction-related contingencies	1,346	1,459
Trade-related contingencies	8,455	8,616
Other commitments with an original maturity of not more than one year	1,155	2,082
Other commitments with an original maturity of more than one year	783	498
Other commitments which are unconditionally cancellable	144,656	135,364
	<b>157,195</b>	149,065
Credit risk-weighted amount	<b>15,287</b>	15,430

In October 2012, the Group renewed a five-year outsourcing agreement, with respect to the provision of information technology and related support to the Group's operation in Hong Kong. There are various termination clauses contained within the agreement that under certain circumstances the service company could require the Group to pay termination cost on early termination of the contract. The exact amount of termination cost cannot be reliably determined as it is dependent upon business volumes over the period of the contract and on the timing of the termination itself.

### 38 CAPITAL AND LEASE COMMITMENTS

#### (a) Capital commitments

Capital commitments outstanding at the balance sheet date but not yet incurred are as follows:

In HK\$ millions	Group and Bank	
	2014	2013
Expenditure contracted but not provided for	68	84
Expenditure authorised but not contracted for	18	33
	<b>86</b>	117

#### (b) Lease commitments

At the balance sheet date, the total future minimum lease payments under non-cancellable operating leases are as follows:

In HK\$ millions	Group and Bank			
	2014		2013	
	Properties	Others	Properties	Others
Not later than one year	215	10	211	12
Later than one year and not later than five years	463	–	418	3
Later than five years	7	–	43	–
	<b>685</b>	<b>10</b>	672	15

### 39 SECURITIES PLEDGED AND TRANSFERS OF FINANCIAL ASSETS

The Group enters into transactions in the normal course of business by which it transfers financial assets to third parties or group companies. These transfers may give rise to full or partial derecognition of those financial assets.

The financial assets are primarily the debt securities and treasury bills deposited with central depositories to secure the Group's short position in securities and to facilitate settlement operations, and the transferred securities under securities lending arrangements. These transactions are generally conducted under terms that are in accordance with normal market practice. The Group has determined that it retains substantially all the risks and rewards of these securities and therefore has not derecognised them. In respect of securities lending transactions, the counterparty is allowed to transfer those securities lent, but has an obligation to return the securities at maturity.

The aggregate amount of secured liabilities and the nature and carrying amounts of the assets pledged as security are as follows:

In HK\$ millions	Group and Bank	
	2014	2013
Secured liabilities – short positions in securities (Note 30)	3,738	3,122
Assets pledged as security		
– Treasury bills	2,591	1,983
– Other securities	1,136	1,128
	<b>3,727</b>	3,111

The assets pledged as security included financial assets at fair value through profit or loss of HK\$3,721 million (2013: HK\$2,391 million).

As at 31 December 2013, the Group had HK\$5,150 million of transferred financial assets under securities lending transactions on the balance sheet, which are mostly classified as available-for-sale financial investments. There was no securities lending transaction outstanding as at 31 December 2014.

The fair value of the transferred securities and associated liabilities approximate the carrying amounts.

#### 40 OFFSETTING FINANCIAL ASSETS AND FINANCIAL LIABILITIES

Financial assets and liabilities are presented net when there is a legally enforceable right to set off the recognised amounts, and there is intention to settle them on a net basis or to realise the asset and settle the liability simultaneously. As at 31 December 2014, no financial assets and liabilities were offset on the balance sheet (2013: Nil).

##### Financial assets and liabilities subject to netting agreement but not offset on the balance sheet

The Group enters into master netting arrangements with counterparties where it is appropriate and feasible to do so to mitigate counterparty risk. The credit risk associated with favourable contracts is reduced by a master netting arrangement to the extent that if an event of default occurs, all amounts with the counterparty are settled on a net basis. Master netting arrangements do not result in an offset of financial assets and liabilities on the balance sheet, as the legal right to set off the transactions is conditional upon default.

These agreements include derivative master agreements (including the International Swaps and Derivatives Association (ISDA) Master Agreement, global master repurchase agreements and global securities lending agreements). The collaterals received and posted under these agreements are generally conducted under terms that are in accordance with normal market practice. In these agreements, the counterparty is typically allowed to sell or repledge those non-cash collaterals (i.e. securities) lent or transferred, but has an obligation to return the securities at maturity. If the securities decrease in value, the Group may, in certain circumstances, be required to pay additional cash collateral, and typically the counterparty has recourse only to the securities. Please see Note 41 for additional disclosures. Furthermore, the Group's short position in securities was secured by the deposit of assets under sale and repurchase agreements.

In addition, the Group receives cash and other collaterals such as marketable securities to reduce its credit exposure. The Group also engages in a variety of counterparty credit mitigation strategies in addition to netting and collateral arrangements. Please see Note 41.

The disclosures set out in the tables below pertain to financial assets and liabilities that are not offset in the Group's balance

sheet but are subject to enforceable master netting arrangement or similar agreement that covers similar financial instruments. The disclosures enable the understanding of both the gross and net amounts (for IFRS and US GAAP readers respectively), as well as provide additional information on how such credit risk is mitigated.

In HK\$ millions	Carrying amounts on balance sheet	Financial instruments (including non-cash collateral) <sup>(a)</sup>	Cash collateral received / pledged	Net amounts <sup>(b)</sup> (D)= (A)-(B)-(C)
Types of financial assets/ liabilities	(A)	(B)	(C)	(D)
<b>2014</b>				
<b>Financial assets</b>				
Positive fair values for financial derivatives	5,094	2,036	250	2,808
<b>Financial liabilities</b>				
Negative fair values for financial derivatives	5,216	2,032	–	3,184
Payable in respect of short sale of securities	3,738	3,727	–	11
<b>Total</b>	<b>8,954</b>	<b>5,759</b>	<b>–</b>	<b>3,195</b>

In HK\$ millions	Carrying amounts on balance sheet	Financial instruments (including non-cash collateral) <sup>(a)</sup>	Cash collateral received / pledged	Net amounts <sup>(b)</sup> (D)= (A)-(B)-(C)
Types of financial assets/ liabilities	(A)	(B)	(C)	(D)
<b>2013</b>				
<b>Financial assets</b>				
Positive fair values for financial derivatives	9,084	7,616	36	1,432
<b>Financial liabilities</b>				
Negative fair values for financial derivatives	9,091	7,616	–	1,475
Payable in respect of short sale of securities	3,122	3,111	–	11
<b>Total</b>	<b>12,213</b>	<b>10,727</b>	<b>–</b>	<b>1,486</b>

(a) Amounts under "Financial instruments (including non-cash collateral)" represent the amounts of financial liabilities/assets position and other non-cash collateral that are subject to netting agreement or similar arrangements.

(b) Net amounts represent

- Financial instruments that are not subject to netting agreement or similar arrangements; or
- Financial assets/liabilities that are subject to netting agreement or similar arrangements but the Group's counterparty does not have equivalent financial liabilities/assets position with the Group to offset upon default.

## 41 FINANCIAL RISK MANAGEMENT

### Risk governance

Under the risk governance framework, the Board of Directors, through the Board Risk Management Committee (BRMC), sets risk appetite, oversees the establishment of robust enterprise-wide risk management policies and processes, and set risk limits to guide risk-taking within the Group.

### (a) Credit risk

Credit risk arises out of the Group's daily activities in various areas of business – lending to retail, corporate and institutional customers; trading activities such as foreign exchange, derivatives and debt securities; and settlement of transactions. Credit risk is one of the most significant measurable risks faced by the Group.

Lending exposures are typically represented by the notional value or principal amount of on-balance sheet financial instruments. Financial guarantees and standby letters of credit, which represent undertakings that the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans even though they are contingent in nature. Pre-settlement Credit Exposures (PCE) for trading and securities transactions is measured taking into account collateral and netting arrangements. Settlement risk is the risk of loss due to the counterparty's failure to perform its obligation after the Group has performed its obligation under an exchange of cash or securities.

### Credit Risk Management

The Group's approach to credit risk management is formulated on the following building blocks:

- **Framework**

The Credit Risk Management Framework, approved by DBSH, defines credit risk and the scope of its application; establishes the dimensions of credit risk; and provides a consistent group-wide framework for managing credit risk across the DBSH group.

- **Policies**

Senior management sets the overall direction and policy for managing credit risk at the Group level. DBSH's Core Credit Risk Policy sets forth the principles by which the Group conducts its credit risk management activities. Please refer to the Credit Risk section in the financial statements of DBS Bank Ltd for more details.

The business-specific and/or location-specific credit policies are established to provide greater details on the implementation of the credit principles within the Core Credit Risk Policy and are adapted to reflect different credit environments and portfolio risk profiles.

### Collateral

Where possible, the Group takes collateral as a secondary recourse to the borrower. Collateral includes cash, marketable securities, properties, trade receivables, inventory and equipment and other physical and financial collateral. The Group may also take fixed and floating charges on the assets of borrowers. It has put in place policies to determine the eligibility of collateral for credit risk mitigation, which include requiring specific collaterals to meet minimum operational requirements in order to be considered as effective risk mitigants.

When a collateral arrangement is in place for financial market counterparties covered under market standard documentation (such as Master Repurchase Agreements and International Swaps and Derivatives Association (ISDA) agreements), collateral received is marked to market on a frequency mutually agreed with the counterparties.

Collateral taken for commercial banking is revalued periodically, depending on the type of collateral.

Helping our customers to restructure repayment liabilities, in times of difficulty, is the Group's preferred approach. However, should the need arise, expeditious disposal and recovery processes are in place for disposal of collaterals held by the Group.

### Other Risk Mitigants

The Group manages its credit exposure from derivatives, repo and other repo-style transactions by entering into netting and collateral arrangements with counterparties where it is appropriate and feasible to do so. The credit risk associated with outstanding contracts with positive mark to market is reduced by master netting arrangements to the extent that if an event of default occurs, all amounts with a single counterparty in a netting eligible jurisdiction are settled on a net basis.

The Group also uses guarantees, as credit risk mitigants. While the Group may accept guarantees from any counterparty, it sets internal thresholds for considering guarantors to be eligible for credit risk mitigation.

- **Risk Methodologies**

Managing credit risk is performed through the Group's deep understanding of our customers, the businesses they are in and the economies in which they operate. This is facilitated through the use of credit ratings and lending limits. The Group uses an array of rating models in both the corporate and retail space.

Retail exposures are typically managed on a portfolio basis and assessed based on credit scoring models, credit bureau record, internal and available external customers' behavior records and supplemented by risk acceptance criteria.

Wholesale exposures are assessed using approved credit models, reviewed and analysed by experienced credit risk managers

taking into consideration the relevant credit risk factors. Credit extensions are proposed by the business unit and are approved by the credit risk function based on independent credit assessment, while also taking into account the business strategies determined by senior management.

The Group actively monitors and manages its exposure to counterparties in over-the-counter (OTC) derivative trades to protect its balance sheet in the event of a counterparty default. DBSH has established methodology on wrong-way risk.

### **Concentration Risk Management**

The Group's risk management processes aim to ensure that an acceptable level of risk diversification is maintained across the Group on an ongoing basis. Limits are established and regularly monitored in respect of country exposures and major industry groups, as well as for single counterparty exposures.

### **Country Risk**

Country risk is the risk of loss which is specifically attributed to events in a specific country (or a group of countries). It includes political risk, exchange rate risk, economic risk, sovereign risk and transfer & convertibility (T&C) risk. The Group manages country risk as part of concentration risk management under the risk appetite framework.

### **Stress Testing**

The Bank performs various types of credit stress tests which are directed by the regulators or driven by internal requirements and management. Credit stress tests are performed at a portfolio or sub-portfolio level and are generally meant to assess the impact of changing economic conditions on asset quality, earnings performance, and capital adequacy and liquidity.

- **Processes, Systems and Reports**

The end-to-end credit process is constantly subject to review and improvement through various front-to-back initiatives involving the Business, Risk Management, Operations and other key stakeholders.

### **Non-performing assets**

The Group classifies its credit facilities as 'Performing Assets' or 'Non-performing assets' in accordance with Hong Kong Monetary Authority ("HKMA")'s loan classification framework.

Refer to Note 2(i) for the Group's accounting policies on the impairment of financial assets. In general, impairment allowance is made when there is objective evidence of impairment as a result of the occurrence of loss events that will have an impact on the estimated future cash flows.

When required, the Group will take possession of collateral it holds as securities and will dispose of them as soon as practicable, with the proceeds used to reduce the outstanding indebtedness.

### **Maximum exposure to credit risk**

The maximum exposure to credit risk for financial assets recognised on the balance sheet is the carrying amount. For contingent liabilities, the maximum exposure to credit risk is the maximum amount the Group would have to pay if the instrument is called upon. For undrawn facilities, the maximum exposure to credit risk is the full amount of the undrawn credit facilities granted to customers. Refer to Note 37 for the contractual amounts of each significant class of contingent liabilities and commitments.

The Group's exposures to credit risk, measured using the expected gross credit exposures that will arise upon a default of the end obligor are as shown in the disclosures required under the Banking (Disclosure) Rules.

### **Analysis of Collateral**

The description of collateral for each class of financial asset is set out below:

*Balances with central banks, government securities and treasury bills, due from banks and bank and corporate debt securities*  
Collateral is generally not sought for these assets.

#### *Derivatives*

The Group maintains collateral agreements and enters into master netting agreements with most of the counterparties for derivative transactions. The impact of netting arrangements recognised for the computation of capital adequacy ratio is shown in the disclosures required under the Banking (Disclosure) Rules.

#### *Loans and advances to customers, contingent liabilities and commitments*

Certain loans and advances to customers, contingent liabilities and commitments are typically collateralised to a substantial extent. In particular, residential mortgage exposures are generally fully secured by residential properties. Income-producing real estate, which is a sub-set of the Specialised Lending exposure, are fully secured by the underlying assets financed.

The extent to which credit exposures are covered by eligible collateral under the Banking (Capital) Rules, besides real estate, after the application of the requisite regulatory hair-cuts, is shown in the disclosures required under the Banking (Disclosure) Rules. The amount shown is a sub-set of the actual collateral arrangements entered by the Group as the Banking (Capital) Rules imposes strict legal and operational standards before collateral can be admitted as credit risk mitigants. As a result, certain collateral arrangements which do not meet its criteria will not be included. Certain collateral types which are not permitted as credit risk mitigants for credit exposures under the Standardised Approach are also excluded.

### Loans and advances to customers by credit quality

In HK\$ millions	Group and Bank	
	2014	2013
Neither past due nor impaired	<b>182,218</b>	198,265
Past due but not impaired	<b>2,508</b>	2,277
Impaired	<b>1,242</b>	1,218
	<b>185,968</b>	201,760

Impaired loans and advances to customers are individually assessed customer advances with objective evidence of impairment.

- (i) Analysis of loans and advances to customers that were neither past due nor impaired by reference to the loan gradings under the Hong Kong Monetary Authority guidelines

In HK\$ millions	Pass	Group and Bank	
		Special mention	Total
<b>2014</b>			
Manufacturing	<b>9,728</b>	<b>2,026</b>	<b>11,754</b>
Building and construction	<b>25,021</b>	<b>1,266</b>	<b>26,287</b>
Housing loans	<b>29,386</b>	<b>5</b>	<b>29,391</b>
General commerce	<b>62,189</b>	<b>6,899</b>	<b>69,088</b>
Transportation, storage and communication	<b>10,959</b>	<b>582</b>	<b>11,541</b>
Financial institutions, investments and holding companies	<b>4,960</b>	–	<b>4,960</b>
Professionals and private individuals (except housing loans)	<b>21,485</b>	<b>35</b>	<b>21,520</b>
Others	<b>7,068</b>	<b>609</b>	<b>7,677</b>
	<b>170,796</b>	<b>11,422</b>	<b>182,218</b>

In HK\$ millions	Group and Bank		
	Pass	Special mention	Total
2013			
Manufacturing	9,563	1,428	10,991
Building and construction	26,111	829	26,940
Housing loans	32,779	7	32,786
General commerce	82,609	4,554	87,163
Transportation, storage and communication	11,426	608	12,034
Financial institutions, investments and holding companies	1,588	5	1,593
Professionals and private individuals (except housing loans)	16,818	30	16,848
Others	9,630	280	9,910
	190,524	7,741	198,265

- (ii) Loans and advances to customers that were past due but not impaired

In HK\$ millions	Group and Bank				Total
	Less than 1 month	1-2 months	2-3 months	More than 3 months	
<b>2014</b>					
Manufacturing	52	2	1	–	55
Building and construction	280	10	–	–	290
Housing loans	530	37	–	–	567
General commerce	691	12	2	–	705
Transportation, storage and communication	155	10	8	107	280
Financial institutions, investments and holding companies	–	–	–	–	–
Professionals and private individuals (except housing loans)	283	16	1	300	600
Others	9	2	–	–	11
	2,000	89	12	407	2,508

In HK\$ millions	Group and Bank Past due				Total
	Less than 1 month	1-2 months	2-3 months	More than 3 months	
2013					
Manufacturing	52	3	–	–	55
Building and construction	263	14	–	–	277
Housing loans	859	21	19	–	899
General commerce	195	10	2	–	207
Transportation, storage and communication	117	14	10	66	207
Financial institutions, investments and holding companies	–	–	–	–	–
Professionals and private individuals (except housing loans)	286	15	–	296	597
Others	35	–	–	–	35
	1,807	77	31	362	2,277

Loans and advances to customers that were past due by more than 3 months represent individually insignificant advances which are subject to collective impairment allowances assessment.

(iii) Impaired loans and advances to customers

In HK\$ millions	Group and Bank	
	2014	2013
Manufacturing	273	335
Building and construction	101	45
Housing loans	46	40
General commerce	757	619
Transportation, storage and communication	7	8
Financial institutions, investments and holding companies	–	146
Professionals and private individuals (except housing loans)	27	4
Others	31	21
	1,242	1,218

	Group and Bank		Group and Bank	
	2014	% of gross Loans and advances to customers	2013	% of gross Loans and advances to customers
Gross impaired advances	1,242	0.67	1,218	0.60
Individual impairment allowances	(569)		(793)	
	673		425	
Impaired advances covered by collateral	671		425	

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

### Analysis of individual impairment allowances

In HK\$ millions	Group and Bank					As at 31 December 2014
	As at 1 January 2014	Amounts written off	Recoveries of advances written off in previous years	Net charge to income statement	Others	
Manufacturing	242	(109)	1	18	–	152
Building and construction	9	(1)	–	9	–	17
Housing loans	–	–	3	(3)	–	–
General commerce	363	(140)	1	131	(5)	350
Transportation, storage and communication	1	–	1	5	–	7
Financial institutions, investments and holding companies	103	(103)	–	–	–	–
Professionals and private individuals (except housing loans)	38	–	–	7	(6)	39
Others	37	–	–	(33)	–	4
	<b>793</b>	<b>(353)</b>	<b>6</b>	<b>134</b>	<b>(11)</b>	<b>569</b>

In HK\$ millions	Group and Bank					As at 31 December 2013
	As at 1 January 2013	Amounts written off	Recoveries of advances written off in previous years	Net charge to income statement	Others	
Manufacturing	348	(102)	6	(10)	–	242
Building and construction	39	–	–	(30)	–	9
Housing loans	–	–	4	(4)	–	–
General commerce	365	(119)	2	115	–	363
Transportation, storage and communication	4	(3)	–	–	–	1
Financial institutions, investments and holding companies	102	–	–	1	–	103
Professionals and private individuals (except housing loans)	31	(1)	–	8	–	38
Others	10	(2)	3	32	(6)	37
	<b>899</b>	<b>(227)</b>	<b>15</b>	<b>112</b>	<b>(6)</b>	<b>793</b>

**Analysis of collective impairment allowances**

In HK\$ millions	Group and Bank		
	As at 1 January 2014	Additions/ (Releases)	As at 31 December 2014
Manufacturing	49	17	66
Building and construction	92	5	97
Housing loans	2	(1)	1
General commerce	209	26	235
Transportation, storage and communication	113	20	133
Financial institutions, investments and holding companies	5	(3)	2
Professionals and private individuals (except housing loans)	206	60	266
Others	37	(7)	30
	<b>713</b>	<b>117</b>	<b>830</b>

In HK\$ millions	Group and Bank		
	As at 1 January 2013	Additions/ (Releases)	As at 31 December 2013
Manufacturing	49	–	49
Building and construction	85	7	92
Housing loans	5	(3)	2
General commerce	219	(10)	209
Transportation, storage and communication	37	76	113
Financial institutions, investments and holding companies	4	1	5
Professionals and private individuals (except housing loans)	184	22	206
Others	19	18	37
	<b>602</b>	<b>111</b>	<b>713</b>

**Geographical concentration**

The analysis of the Bank's gross advances to customers by geographical area is based on the location of the counterparty after taking into account the transfer of risk. In general, transfer of risk applies if the claim is guaranteed by a party in a country which is different from that of the counterparty.

In HK\$ millions	Trade Finance (including trade bills)		Total
	Loans		
<b>As at 31 December 2014</b>			
Hong Kong	121,754	21,096	142,850
Mainland China	7,296	27,321	34,617
Others	6,739	1,762	8,501
	<b>135,789</b>	<b>50,179</b>	<b>185,968</b>
<b>As at 31 December 2013</b>			
Hong Kong	118,996	19,861	138,857
Mainland China	7,271	47,870	55,141
Others	5,584	2,178	7,762
	<b>131,851</b>	<b>69,909</b>	<b>201,760</b>

**Analysis of impaired advances, individual and collective impairment allowances for loans and trade finance which accounted for 10% or more of the Bank's gross advances to customers:**

In HK\$ millions	Impaired advances to customers	Individual impairment allowances	Collective impairment allowances
<b>As at 31 December 2014</b>			
Hong Kong	1,072	451	665
Mainland China	108	89	36
<b>As at 31 December 2013</b>			
Hong Kong	1,036	609	578
Mainland China	130	142	32

**(b) Market risk**

The Group's exposure to market risk is categorised into:

- Trading portfolios: Arising from positions taken for (i) market-making (ii) client-facilitation and (iii) benefiting from market opportunities.
- Non-trading portfolios: Arising from (i) positions taken to manage the interest rate risk of the Group's retail and commercial banking assets and liabilities (ii) debt securities comprising of investments held for yield and/or liquidity risk management (iii) strategic stakes in entities and (iv) structural foreign exchange risk arising mainly from the Group's strategic investments which are denominated in currencies other than the Hong Kong dollar.

### Market Risk Management

The Group's approach to market risk management is formulated on the following building blocks:

- **Framework**

The Market Risk Framework, approved by the BRMC, sets out the Group's overall approach towards market risk management.

- **Policies**

The Core Market Risk Policy ("CMRP") establishes the base standards for market risk management within the Group. The Policy Implementation Guidance and Requirements ("PIGR") complements the CMRP and sets out guidance and requirements with more details for specific subject matters. Both CMRP and PIGR facilitate the identification, measurement, control, monitoring and reporting of market risk in a consistent manner within the Group.

- **Risk Methodologies**

Value-at-Risk (VaR) is a method that computes the potential losses on risk positions as a result of movements in market rates and prices, over a specified time horizon and to a given level of confidence. Our VaR model is based on historical simulation with a one-day holding period and a 95% level of confidence. Tail VaR (TVaR), which is an average of the potential losses beyond the given 95% level of confidence, is used by the Group to monitor and limit market risk exposures. TVaR is supplemented by risk control metrics such as sensitivities to risk factors and loss triggers for management action.

We conduct backtesting to verify the predictiveness of the VaR model. For backtesting, VaR at the 99% level of confidence and over a one-day holding period is used.

VaR models such as historical simulation VaR permit the estimation of the aggregate portfolio market risk potential loss, due to a range of market risk factors and instruments. VaR models have limitations which include but are not limited to: (i) past changes in market risk factors may not provide accurate predictions of the future market movements and (ii) may understate the risk arising from severe market risk related events.

To monitor our vulnerability to unexpected but plausible extreme market risk related events, we have implemented an extensive stress testing policy for market risk where regular and multiple stress tests were run covering trading and non-trading portfolios through a combination of historical and hypothetical scenarios depicting risk factors movement.

TVaR is the key risk metric used to manage our assets and liabilities' except for credit spread risk under Loans and Receivables where it is under the credit framework. We manage banking book interest rate risk arising from mismatches in the interest rate profile of assets, liabilities and capital instruments (and associated hedges), including basis risk arising from different interest rate benchmarks, interest rate re-pricing risk, yield curve risks and embedded optionality.

- **Processes, Systems and Reports**

Robust internal control processes and systems are designed and implemented to support the Group's approach for market risk management. Additionally, Internal Audit conducts regular independent reviews of these control processes and systems. These reviews provide senior management with objective and timely assessments of the control processes and systems' appropriateness and effectiveness.

The day-to-day market risk monitoring, control and analysis is managed by the RMG Market and Liquidity Risk unit – an independent market risk management function that reports to the Senior Risk Executive. DBS Bank Ltd provides RMG Market and Liquidity Risk with model analytics, risk infrastructure and risk report production support.

### Market Risk Metrics

The Group level TVaR considers both trading and non-trading portfolios. The Group level TVaR is tabulated below, showing the period-end, average, high and low TVaR.

In HK\$ millions	As at 31 Dec 2014	Group 1 Jan 2014 to 31 Dec 2014		
		Average	High	Low
Total	36.3	36.7	47.5	27.5

In HK\$ millions	As at 31 Dec 2013	Group 1 Jan 2013 to 31 Dec 2013		
		Average	High	Low
Total	33.5	20.3	33.5	13.0

*Note: TVaR is computed in Singapore dollars and translated into Hong Kong dollars using the prevailing rates on the reporting dates for presentation purpose.*

The average Group level TVaR in 2014 was higher than that in 2013, due to (i) an increase in risk positions of the trading portfolios and (ii) an increase in government securities holding and interest risk exposures in CNH and USD of the non-trading portfolios.

The following table shows the trading portfolios, the period-end, average, high and low TVaR:

In HK\$ millions	As at 31 Dec 2014	Group		
		Average	High	Low
Total	6.9	7.7	15.7	3.2

In HK\$ millions	As at 31 Dec 2013	Group		
		Average	High	Low
Total	4.2	3.5	7.1	1.8

Note: TVaR is computed in Singapore dollars and translated into Hong Kong dollars using the prevailing rates on the reporting dates for presentation purpose.

In the Group, the main risk factors driving trading portfolios in 2014 were interest rates, foreign exchange and credit spreads. Trading portfolios' average TVaR increased by HK\$4.3 million (123%), contributed largely by an increase in interest rate risk positions.

Trading portfolio experienced 2 backtesting exceptions in 2014 compared with 4 in 2013. The exceptions occurred in October and December when there was pronounced market volatility.

The key market risk drivers of the Group's non-trading portfolios are CNH, HKD and USD interest rate positions. The economic value impact of changes in interest rates is simulated under various assumptions for the non-trading risk portfolio. The simulated economic value changes are negative HK\$557 million and HK\$1,103 million (2013: negative \$422 million and \$838 million) based on parallel shocks to all yield curves of 100 basis points and 200 basis points respectively. The reported figures are based on the worst case of an upward and downward parallel shift in the yield curves.

Equity price risk arises from the Group's strategic investments which are overseen by the Hong Kong Management Committee. The Group's equity exposures booked in its banking book portfolio as at 31 December 2014 and 2013 were not material and were held for long term investment purpose. They were reported as bank and corporate securities in Note 19 to the financial statements and are subject to the accounting and valuation policies set out in Notes 2(g) and 2(i) to the financial statements.

### (c) Liquidity risk

The Group's liquidity risk arises from its obligations to honour withdrawals of deposits, repayments of borrowed funds at maturity, and commitments to extend credit and support working capital needs.

The Group seeks to manage its liquidity in a manner that ensures that its liquidity obligations would continue to be honoured under normal as well as adverse circumstances.

## Liquidity Risk Management

### Liquidity Management and Funding Strategy

The Group strives to develop a diversified funding base with access to funding sources across retail and wholesale channels. In particular, the Group has continuously made inroads in growing, deepening and diversifying its deposit base, spanning retail, wealth management, corporate and institutional customers across markets that it operates in. Supplementing the deposit base, the Group continues to maintain access to wholesale channels, to support the growth of its investor base, as well as to increase flexibility and reduce funding cost in capitalising on business opportunities.

In deploying the funds, the Group aims to predominantly fund its lending activities via customer deposits and borrowings. In the event where market conditions lead to insufficient or prohibitively expensive customer funding, flexibility is maintained to fund lending growth with duration matched wholesale funding. With increasing diversification of funding sources, optimising the mismatch in fund deployments against sources with respect to pricing, size, currency and tenor remains challenging. To this end, the Group actively makes use of the swap markets in the conversion of funds across currencies to deploy surplus funds, where practicable.

The Assets and Liabilities Committee regularly reviews the growth in loans and deposits, momentum in business activities, market competition, economic outlooks, market conditions and other factors that may affect liquidity in the continual refinement of the Group's funding strategy.

### Approach to Liquidity Risk Management

The Group's approach to liquidity risk management is formulated on the following building blocks:

- **Framework**

The Liquidity Risk Framework, approved by the BRMC, sets out the Group's overall approach towards liquidity risk management. The Framework describes the range of strategies employed by the Group to manage its liquidity. These include maintaining an adequate counterbalancing capacity (comprising liquid assets, the capacity to borrow from the money markets as well as forms of managerial interventions that improve liquidity) to address potential cashflow shortfalls and maintaining diversified sources of liquidity. In the event of a potential or actual crisis, the Group has in place a set of liquidity contingency and recovery plans to ensure that decisive actions are taken to ensure the Group maintains adequate liquidity.

- **Policies**

The Core Liquidity Risk Policy establishes the baseline standards for liquidity risk management within the Group. Policies and guidance documents communicate the base standards and detailed requirements throughout the Group and enhance the ability of the Group to manage its liquidity risk.

- **Risk Methodologies**

The primary measure used to manage liquidity within the tolerance defined by the Board is the cashflow maturity mismatch analysis. The analysis is performed on a regular basis under normal and adverse scenarios, and assesses the adequacy of the counterbalancing capacity to fund or mitigate any cashflow shortfalls that may occur as forecasted in the cashflow movements across successive time bands. To ensure that liquidity is managed in line with the risk tolerance, core parameters underpinning the performance of the analysis, such as the types of scenarios, the survival period and the minimum level of liquid assets, are pre-specified for monitoring and control at the Group. Any occurrences of forecasted shortfalls that cannot be covered by the counterbalancing capacity would be escalated to the relevant committees for deliberation and actions.

Stress testing is performed mainly under the cashflow maturity mismatch analysis, and covers adverse scenarios involving shocks that are general market and/or bank-specific in nature to assess the vulnerability when runoffs in liabilities increase, rollovers of assets increase and/or liquidity assets buffer reduce. In addition, ad-hoc stress tests are performed in the formulation of the Group's internal capital adequacy assessment process.

Liquidity risk control measures, such as liquidity-related ratios and balance sheet analysis, are complementary tools to the cashflow maturity mismatch analysis and are performed regularly to obtain deeper insights and finer control over the liquidity profile across the Group.

- **Processes, Systems and Reports**

Robust internal control processes and systems underlie the overall approach to identifying, measuring, aggregating, controlling and monitoring liquidity risk across the Group.

The day-to-day liquidity risk monitoring, control, reporting and analysis are managed by the RMG Market and Liquidity Risk unit – an independent liquidity risk management function that reports to the Senior Risk Executive. This group comprises of risk control, production and reporting members.

**Liquidity Risk Metrics**

The table below analyses assets and liabilities of the Group as at 31 December based on the remaining period as at balance sheet date to the contractual maturity dates:

In HK\$ millions	Repayable on demand	Less than 1 month	3 months or less but over 1 month	Group		After 5 years	Undated	Total
				1 year or less but over 3 months	5 years or less but over 1 year			
<b>2014</b>								
<b>Assets</b>								
– Cash and balances with central banks	1,969	–	–	–	–	–	–	1,969
– Government securities and treasury bills, classified as								
– Held-for-trading	–	985	1,375	1,475	331	30	–	4,196
– Available-for-sale	–	1,781	5,895	4,599	6,207	235	–	18,717
– Due from banks	4,234	27,696	36,456	9,844	1,248	–	–	79,478
– Bank and corporate securities								
– Debt securities classified as held-for- trading	–	560	71	208	1,499	–	–	2,338
– Debt securities classified as available- for-sale	–	175	247	398	6,388	419	16	7,643
– Debt securities classified as loans and receivables	–	–	–	118	1,762	–	–	1,880
– Equity securities	–	–	–	–	–	–	30	30
– Loans and advances to customers	9,234	34,931	33,692	35,455	30,551	39,629	1,077	184,569
– Others	39	5,745	1,961	60	145	6	4,664	12,620
<b>Total assets</b>	<b>15,476</b>	<b>71,873</b>	<b>79,697</b>	<b>52,157</b>	<b>48,131</b>	<b>40,319</b>	<b>5,787</b>	<b>313,440</b>
<b>Liabilities</b>								
– Due to banks	3,781	479	8	9	–	–	–	4,277
– Deposits and balances from customers	114,187	60,760	49,855	27,332	125	–	–	252,259
– Certificates of deposit issued	–	63	–	890	2,796	1,212	–	4,961
– Subordinated liability	–	–	–	–	–	4,189	–	4,189
– Others	322	7,348	3,809	1,600	123	15	1,706	14,923
<b>Total liabilities</b>	<b>118,290</b>	<b>68,650</b>	<b>53,672</b>	<b>29,831</b>	<b>3,044</b>	<b>5,416</b>	<b>1,706</b>	<b>280,609</b>
Of which:								
Certificates of deposit held included in bank and corporate securities, classified as:								
– Held-for-trading	–	535	24	123	6	–	–	688

In HK\$ millions	Repayable on demand	Less than 1 month	3 months or less but over 1 month	Group		After 5 years	Undated	Total
				1 year or less but over 3 months	5 years or less but over 1 year			
2013								
Assets								
– Cash and balances with central banks	995	–	–	–	–	–	–	995
– Government securities and treasury bills, classified as								
– Held-for-trading	–	102	1,228	667	1,371	80	–	3,448
– Available-for-sale	–	2,519	7,055	1,461	723	900	–	12,658
– Due from banks	4,836	22,455	18,334	16,716	–	–	–	62,341
– Bank and corporate securities								
– Debt securities classified as held-for- trading	–	56	17	344	425	12	–	854
– Debt securities classified as available- for-sale	–	751	735	3,970	3,935	231	15	9,637
– Debt securities classified as loans and receivables	–	–	–	–	2,171	–	–	2,171
– Equity securities	–	–	–	–	–	–	70	70
– Loans and advances to customers	8,368	30,044	37,415	47,921	31,299	43,940	1,267	200,254
– Others	43	9,396	2,079	99	79	7	4,528	16,231
<b>Total assets</b>	<b>14,242</b>	<b>65,323</b>	<b>66,863</b>	<b>71,178</b>	<b>40,003</b>	<b>45,170</b>	<b>5,880</b>	<b>308,659</b>
Liabilities								
– Due to banks	875	3,658	71	147	–	–	–	4,751
– Deposits and balances from customers	92,934	62,136	54,589	28,602	130	–	–	238,391
– Certificates of deposit issued	–	180	–	3,193	2,986	1,205	–	7,564
– Subordinated liability	–	–	–	–	–	4,187	–	4,187
– Others	920	14,902	1,741	1,280	882	41	2,733	22,499
<b>Total liabilities</b>	<b>94,729</b>	<b>80,876</b>	<b>56,401</b>	<b>33,222</b>	<b>3,998</b>	<b>5,433</b>	<b>2,733</b>	<b>277,392</b>
Of which:								
Certificates of deposit held included in bank and corporate securities, classified as:								
– Held-for-trading	–	–	–	38	–	–	–	38
– Available-for-sale	–	–	388	1,416	–	–	–	1,804
	–	–	388	1,454	–	–	–	1,842

The contractual undiscounted cash flow projections of the Group's financial liabilities, derivatives, contingent liabilities and commitments analysed by the remaining period as at 31 December to the contractual maturity dates are as follows :

In HK\$ millions	Repayable on demand	3 months or less	Group		After 5 years	Total
			1 year or less but over 3 months	5 years or less but over 1 year		
<b>2014*</b>						
<b>Financial liabilities</b>						
– Due to banks	3,781	488	9	–	–	4,278
– Deposits and balances from customers	114,541	113,396	28,785	346	–	257,068
– Certificates of deposit issued	–	90	991	3,065	1,142	5,288
– Subordinated liability	–	29	95	742	4,821	5,687
– Others	322	8,809	1,807	1,037	177	12,152
	<b>118,644</b>	<b>122,812</b>	<b>31,687</b>	<b>5,190</b>	<b>6,140</b>	<b>284,473</b>
<b>Derivatives settled on a gross basis</b>						
– Foreign exchange contracts						
– inflow	–	119,967	158,770	66,079	–	344,816
– outflow	–	119,992	158,844	65,896	–	344,732
<b>Contingent liabilities and commitments</b>						
– Contingent liabilities	–	10,601	–	–	–	10,601
– Commitments	73,284	73,310	–	–	–	146,594
	<b>73,284</b>	<b>83,911</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>157,195</b>
<b>2013*</b>						
<b>Financial liabilities</b>						
– Due to banks	875	3,730	148	–	–	4,753
– Deposits and balances from customers	92,934	117,138	28,916	161	–	239,149
– Certificates of deposit issued	–	212	3,320	3,324	1,186	8,042
– Subordinated liability	–	29	90	776	5,345	6,240
– Others	920	12,062	1,600	2,024	467	17,073
	<b>94,729</b>	<b>133,171</b>	<b>34,074</b>	<b>6,285</b>	<b>6,998</b>	<b>275,257</b>
<b>Derivatives settled on a gross basis</b>						
– Foreign exchange contracts						
– inflow	–	127,743	131,177	42,907	–	301,827
– outflow	–	127,778	131,148	42,920	–	301,846
<b>Contingent liabilities and commitments</b>						
– Contingent liabilities	–	11,121	–	–	–	11,121
– Commitments	71,954	65,990	–	–	–	137,944
	<b>71,954</b>	<b>77,111</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>149,065</b>

\* The balances in the above table will not agree with the balances in the consolidated balance sheet as the table incorporates all cash flows, on an undiscounted basis, related to both principal as well as future interest payments.

For the purpose of risk management, the Group actively monitors and manages its liquidity profile based on the cashflow maturity mismatch analysis.

In forecasting the cashflows under the analysis, behavioural profiling is necessary in cases where a product has indeterminate maturity or the contractual maturity does not realistically reflect the expected cashflows. An example would be maturity-indeterminate savings and current account deposits which are generally viewed as a source of stable funding for commercial banks and consistently exhibited stability even under historical periods of stress.

A conservative view is therefore adopted in the Group's behavioural profiling of assets, liabilities and off-balance sheet commitments that have exhibited cashflow patterns that differ significantly from the contractual maturity profile shown under Note 41.

The table below shows the Group's behavioural net and cumulative maturity mismatch between assets and liabilities over a 1-year period under a normal scenario without incorporating growth projections. The Group's liquidity is observed to remain adequate under the maturity mismatch analysis, amidst sustained growth in loans supported by stable sources of funds from deposits gathering.

In HK\$ millions <sup>(i)</sup>	Less than 7 days	1 week to 1 month	1 to 3 months	3 to 12 months
<b>2014</b>				
Net liquidity mismatch	<b>18,275</b>	<b>10,173</b>	<b>52,036</b>	<b>23,862</b>
Cumulative mismatch	<b>18,275</b>	<b>28,448</b>	<b>80,484</b>	<b>104,346</b>
<b>2013<sup>(ii)</sup></b>				
Net liquidity mismatch	20,928	7,312	40,573	39,610
Cumulative mismatch	20,928	28,240	68,813	108,423

(i) Positive indicates a position of liquidity surplus. Negative indicates a liquidity shortfall that has to be funded.

(ii) As the behavioural assumptions used to determine the maturity mismatch between assets and liabilities are updated from time to time, the information presented above is not directly comparably past balance sheet dates.

#### (d) Operational risk

Operational Risk is the risk of loss resulting from inadequate or failed internal processes, people or systems, or from external events, including legal risk, but does not include strategic or reputational risk. Operational risk is inherent in most of the Group's businesses and activities.

The Group's objective is to keep operational risk at appropriate levels, taking into account the markets the Bank operates in, the characteristics of the businesses as well as the competitive and regulatory environment the Group is subject to.

#### Operational Risk Management

The Group's framework for operational risk management comprises the following building blocks:

- **Policies**

To govern Operational Risk Management practices in a consistent manner, the Group Operational Risk Management Framework includes a set of Core Operational Risk Standards which provides guidance on the baseline controls to ensure a controlled and sound operating environment. There are also corporate operational risk policies which are owned by the respective corporate oversight functions.

- **Risk Methodologies**

To manage and control operational risk, there are various tools including control self-assessment, operational risk event management and key risk indicators monitoring. Control self-assessment is used by each business or support unit to identify key operational risk and assess the degree of effectiveness of the internal controls. For those control issues identified, the units are responsible to develop action plans and track the timely resolution of these issues. Operational risk events are classified in accordance with Basel standards. Such events, including any significant incidents that may impact the Bank's reputation, are required to be reported based on certain established thresholds. Key risk indicators with pre-defined escalation triggers are employed to facilitate risk monitoring in a forward looking manner.

- **Processes, systems and reports**

Robust internal control process and system are integral to identifying, monitoring, managing and reporting operational risk. The Bank has implemented a web-based system that supports multiple operational risk management processes and tools including operational risk event reporting, control self-assessment, key risk indicators, tracking of issues or action plans and operational risk reporting.

Units are responsible for the day-to-day management of operational risk in their products, processes, systems and activities in accordance with the various frameworks and policies. RMG Operational Risk and other control functions provide oversight and monitor the effectiveness of operational risk management, assess key operational risk issues with units to determine the impact across the Bank, and report and/or escalate key operational risks to relevant senior management and Board-level committees with recommendations on appropriate risk mitigation strategies.

**(e) Capital management**

The Group's capital management policies are to diversify its sources of capital, to allocate capital efficiently, guided by the need to maintain a prudent relationship between available capital and the risks of its underlying businesses and to meet the expectations of key constituencies, including investors and regulators.

The Banking Ordinance and the Banking (Capital) Rules set out the current requirements relating to the minimum capital adequacy ratios for an authorised institution incorporated in Hong Kong and the methodology for calculating these ratios.

The Bank is required to compute its capital adequacy ratios on a combined basis that includes the Bank and its overseas branch.

The Bank complied with the capital requirements imposed by the HKMA throughout 2014 and 2013.

**42 MATERIAL RELATED PARTY TRANSACTIONS****(a) Holding companies and fellow subsidiaries**

The Group's immediate holding company is DHB Limited and the ultimate holding company is DBS Group Holdings Ltd ("DBSH"). DBS Bank Ltd is an intermediate holding company of the Group.

As part of the Bank and the Group's normal course of business, it enters into various transactions with holding companies and fellow subsidiaries on normal commercial terms. These transactions include interbank placements, taking of deposits, financial derivatives, contingent liabilities and commitments.

The Group has policies on credit processing for its affiliates, as well as transactions with its affiliates and related parties. Affiliate-related transactions must be conducted on an arm's length basis using credit standards, terms and conditions that are comparable to similar transactions with non-affiliates.

Information relating to income and expenses from these transactions during the year and balances outstanding as at 31 December are set out below:

**(i) Income and expenses with holding companies and fellow subsidiaries**

In HK\$ millions	DBS Group Holdings Ltd		DBS Bank Ltd		Fellow subsidiaries	
	2014	2013	2014	2013	2014	2013
Interest income	-	-	449	400	4	-
Interest expense	(40)	-	(125)	(229)	(6)	(2)
Net fee and commission income/(expense)	-	-	9	2	(7)	(8)
Net (loss)/income from financial instruments at fair value through profit or loss	-	-	(1,598)	1,130	-	-
Other income	-	-	30	25	6	6
Total expenses (charged)/recovered	-	-	(16)	(57)	73	22

**(ii) Balances with DBS Bank Ltd as at 31 December**

In HK\$ millions	Group		Bank	
	2014	2013	2014	2013
<b>Asset</b>				
Due from banks	66,996	49,841	66,996	49,838
Derivatives	1,258	4,617	1,258	4,617
Other assets	751	243	751	243
	69,005	54,701	69,005	54,698
<b>Liabilities</b>				
Due to banks	1,839	2,352	1,839	2,352
Derivatives	4,206	5,116	4,206	5,116
Subordinated liability	-	4,187	-	4,187
Other liabilities	127	140	127	140
	6,172	11,795	6,172	11,795

**(iii) Contract/notional amounts of financial derivatives with DBS Bank Ltd and fellow subsidiaries as at 31 December**

In HK\$ millions	Group and Bank	
	2014	2013
Foreign exchange contracts	408,560	378,986
Interest rate contracts	22,111	20,149
Equity contracts	515	269
	431,186	399,404

**(iv) Contingent liabilities and commitments with DBS Bank Ltd and fellow subsidiaries**

As at 31 December 2014, total contingent liabilities and commitments with DBS Bank Ltd and fellow subsidiaries amounted to HK\$1,207 million (2013: HK\$587 million).

(v) Balances with immediate holding company and other intermediate holding companies as at 31 December

In HK\$ millions	Group and Bank	
	2014	2013
Deposits and balances from customers	<b>315</b>	315

(vi) Balances with DBS Group Holdings Ltd as at 31 December

In HK\$ millions	Group and Bank	
	2014	2013
Subordinated liability	<b>4,189</b>	–
Other liabilities	<b>6</b>	–
	<b>4,195</b>	–

(vii) Balances with fellow subsidiaries as at 31 December

In HK\$ millions	Group		Bank	
	2014	2013	2014	2013
Due from banks	<b>6</b>	–	<b>6</b>	–
Loans and advances to customers	<b>1,070</b>	–	<b>1,070</b>	–
Other assets	<b>168</b>	95	<b>168</b>	95
	<b>1,244</b>	95	<b>1,244</b>	95
Due to banks	<b>182</b>	139	<b>182</b>	139
Deposits and balances from customers	<b>2,810</b>	934	<b>2,810</b>	934
Other liabilities	<b>83</b>	70	<b>83</b>	70
	<b>3,075</b>	1,143	<b>3,075</b>	1,143

#### (b) Directors and key management personnel

(i) Transactions and balances with directors and key management personnel

For the year ended 31 December 2014 and 2013, the Group has banking and non-banking transactions with directors of the Bank and DBSH Group and key management personnel of the Bank and their close family members. These transactions, including the taking of deposit and extension of credit card and other loan facilities, are made in the ordinary course of business and on commercial terms, and are not material, except for a banking facility of HK\$500 million provided to one of the directors in 2013. This banking facility was cancelled in 2014.

(ii) Compensation of directors and key management personnel

In HK\$ millions	Group and Bank	
	2014	2013
Salaries, other short term employee benefits and directors' fee (Note)	<b>76</b>	78
Pension	<b>3</b>	3
Share-based compensation	<b>20</b>	18
	<b>99</b>	99

Note:

The Directors' fees are payable in 2015 to eligible persons who acted as Directors of DBS Bank (Hong Kong) Limited during the year ended 31 December 2014. Such fees are subject to the approval of the shareholders of DBS Bank (Hong Kong) Limited.

The amount included cash bonus accrued during the year, to be paid in the following year. Such cash bonus is subject to the approval of DBSH Board of Directors.

#### (c) Loans to officers

Pursuant to section 78 of Schedule 11 to the Hong Kong Companies Ordinance (Cap. 622), with reference to section 161B of the predecessor Hong Kong Companies Ordinance (Cap.32), particulars of loans made to officers are as follows:

In HK\$ millions	Balance outstanding as at 31 December		Maximum balance during the year	
	2014	2013	2014	2013
Aggregate amount outstanding in respect of principal and interest	–	450	<b>450</b>	493

#### 43 SHARE BASED COMPENSATION PLANS

The Group participated in various share-based compensation plans operated by the DBSH to reward good performers, support retention of key employees and enable employees to share the success.

Main Scheme/Plan	Note
<b>DBSH Share Plan (Share Plan)</b>	
<ul style="list-style-type: none"> <li>• Share Plan is granted to Group executives as determined by the CMDC appointed to administer the Share Plan from time to time</li> <li>• Participants are awarded DBSH shares, their equivalent cash value or a combination</li> <li>• Awards consists of Main award and Retention award (20% of main awards)</li> <li>• Vesting of main award is staggered between 2 – 4 years after grant i.e. 33% will vest 2 years after grant. Another 33% will vest on the third year and the remainder 34% plus the retention awards will vests 4 year after grant.</li> <li>• The fair value of the shares awarded are computed based on the market price of the ordinary shares at the time of the award</li> </ul>	43(i)
<b>DBSH Employee Share Plan (ESP)</b>	
<ul style="list-style-type: none"> <li>• ESP caters to employees not eligible to participate in the above listed Share Plan. Eligible employees are awarded DBSH ordinary shares, their equivalent cash value or a combination of both (at the discretion of the CMDC), when time-based conditions are met.</li> <li>• The awards structure and vesting conditions are similar to DBSH Share Plan</li> <li>• There are no additional retention awards for shares granted to top performers and key employees.</li> <li>• However, in specific cases where the award form part of an employee's annual performance remuneration, the "retention" award which constitute 20% of the shares given in the main award will be granted. The shares in the retention award will vest four years after the date of grant.</li> </ul>	43(i)
<b>DBSH Share Option Plan (Option Plan)</b>	
<ul style="list-style-type: none"> <li>• The Option Plan expired on 19 June 2009. Its termination does not affect the rights of holders of outstanding existing options</li> <li>• Option Plan is granted to eligible Group executives who holds the rank of Vice President (or equivalent) and above and selected employees below the rank of Vice President (or equivalent)</li> <li>• The exercise price is equal to the average of the last dealt prices for the DBSH shares as determined by reference to the daily official list published by the Singapore Exchange Securities Trading Ltd, for the three consecutive trading days immediately preceding the date of the grant</li> <li>• Vest over a period in accordance to vesting schedule</li> <li>• Exercisable after the first anniversary of the date of the grant up to the date of expiration of the options</li> <li>• The fair value of options granted is determined using the Binomial model</li> </ul>	43(ii)

## (i) DBSH Share Plan and DBSH Employee Share Plan

The following table sets out the outstanding awards at the end of each reporting period and the movement during the year:

Number of shares	2014		2013	
	Share Plan	ESP	Share Plan	ESP
Balance at 1 January	1,085,568	383,637	810,576	341,310
Granted	454,304	177,700	428,373	162,800
Transfer	3,095	3,910	28,764	12,412
Vested	(283,399)	(115,062)	(153,052)	(79,629)
Forfeited	(27,273)	(40,933)	(29,093)	(53,256)
Balance at 31 December	1,232,295	409,252	1,085,568	383,637
Weighted average fair value of the shares granted during the year	SG\$16.66	SG\$16.65	SG\$15.19	SG\$15.07

Since the inception of the Share Plan and ESP, no awards have been cash-settled.

## (ii) DBSH Share Option Plan

The following table sets out the movements of the unissued ordinary shares under outstanding options issued and additional information on these options.

	2014		2013	
	Unissued number of ordinary shares under outstanding options	Weighted average exercise price SG\$	Unissued number of ordinary shares under outstanding options	Weighted average exercise price SG\$
Balance as at 1 January	219,087	12.59	518,949	11.66
Movements during the year:				
– Exercised	(160,506)	12.55	(256,463)	11.00
– Transfer	(2,823)	12.81	(18,934)	12.64
– Forfeited / Expired	(20,147)	12.57	(24,465)	9.52
Balance as at 31 December	35,611	12.81	219,087	12.59

Additional information:

Weighted average remaining contractual life of options outstanding as at 31 December

0.16 years

0.39 years

Range of exercise price of options outstanding as at 31 December

SG\$12.81

SG\$12.53-  
SG\$12.81

In 2014, 160,506 options (2013: 256,463) were exercised at their contractual exercise prices. During the year, the weighted average market price of DBSH shares was SG\$16.53 (2013: SG\$15.53).

DBSH options	Number of unissued ordinary shares		During the year		Number of unissued ordinary shares 31 December 2014	Exercise price per share SGD	Expiry date
	1 January 2014	Transfer	Exercised	Forfeited/ Expired			
March 2004	168,741	–	151,181	17,560	–	12.53	02 Mar 2014
March 2005	50,346	(2,823)	9,325	2,587	35,611	12.81	01 Mar 2015
	219,087	(2,823)	160,506	20,147	35,611		

**44 COMPARATIVES**

Prior period comparatives have been aligned to the current year presentation (Note 2(b)). The table below provides a reconciliation of the current Balance Sheet presentation to the old Balance Sheet presentation for 2013 balances.

In HK\$ millions 2014 Line Item	2013 Line Item	Group		Bank
Cash and balances with central banks		995		995
	Cash and balances with bank		995	995
Government securities and treasury bills		16,106		16,106
	Trading securities		3,448	3,448
	Financial investments		12,658	12,658
Due from banks		62,341		62,338
	Placements with and advances to banks		57,505	57,502
	Cash and balances with bank		4,836	4,836
Bank and corporate securities		12,732		12,732
	Trading securities		854	854
	Financial investments		11,878	11,878
Other assets		4,157		4,157
	Other assets		4,118	4,118
	Deferred tax assets		39	39
Due to banks		4,751		4,751
	Deposit and balances from banks		4,751	4,751
Deposit and balances from customers		238,391		238,391
	Deposit from customers		230,269	230,269
	Financial liabilities designated at fair value through profit or loss		8,122	8,122
Other liabilities		13,408		13,406
	Trading liabilities		3,122	3,122
	Current income tax liabilities		168	168
	Amount due to a joint venture		2,887	2,887
	Other liabilities		7,231	7,229

DBS Bank (Hong Kong) Limited and its Subsidiaries

# UNAUDITED SUPPLEMENTARY INFORMATION

for the year ended 31 December 2014

The following disclosures are prepared in accordance with the Banking (Disclosure) Rules.

## 1 CAPITAL ADEQUACY

The capital adequacy ratios as at 31 December 2014 and 31 December 2013 were compiled in accordance with the Banking (Capital) Rules issued by the Hong Kong Monetary Authority.

	As at 31 December 2014	As at 31 December 2013
Capital Adequacy Ratios		
Common Equity Tier 1	<b>14.6%</b>	13.9%
Tier 1	<b>14.6%</b>	13.9%
Total	<b>16.7%</b>	16.1%

The Bank uses the Internal Ratings-Based ("IRB") approach for the calculation of the risk-weighted assets for the majority of its credit risk exposures and the Standardised approach for those

exempted from the IRB approach. The Bank uses the Standardised approaches for the calculation of risk-weighted assets for market risk and operational risk.

## Additional information

Capital disclosures as required by section 45 of the Banking (Disclosure) Rules are available on our website [www.dbs.com.hk](http://www.dbs.com.hk).

## 2 FINANCIAL STATEMENTS AND REGULATORY SCOPE OF CONSOLIDATION

For regulatory reporting purposes, the Bank is required to compute its capital adequacy ratios on a combined basis that includes the Bank and its overseas branch, while the preparation of its financial statements is based on consolidation basis that also includes its subsidiaries.

The following entities are within the Group's accounting scope of consolidation but are excluded from its regulatory scope of consolidation.

Name of entity	Principal activities	Total Assets HK\$'M	Total Equity HK\$'M
Dao Heng Finance Limited	Inactive	59	58
Hang Lung Bank (Nominee) Limited	Provision of nominee services	–	–
DBS Kwong On (Nominees) Limited	Provision of nominee services	–	–
Overseas Trust Bank Nominees Limited	Provision of nominee services	–	–
Ting Hong Nominees Limited	Provision of nominee, trustee and agency services	–	–
DBS Trustee (Hong Kong) Limited	Provision of trustee and trust administration services	5	5
DBS Trustee H.K.(New Zealand) Limited	Provision of trustee and trust administration services	1	–
DBS COMPASS Limited (formerly known as Hutchison DBS Card Limited)	Provision of credit card services	804	803

### 3 CAPITAL REQUIREMENTS FOR DIFFERENT TYPES OF RISK

The following table indicates the capital requirements for different types of risk on each exposure class as at 31 December:

In HK\$ millions	2014	2013
<b>Credit risk:</b>		
IRB approach		
Retail exposures:		
Residential mortgages	256	330
Qualifying revolving retail exposures	1,429	1,380
Small business retail exposures	–	–
Other retail exposures to individuals	897	692
Wholesale exposures:		
Sovereign exposures	200	217
Bank exposures	2,665	3,126
Corporate exposures	7,617	7,660
Other exposures	382	356
	<b>13,446</b>	13,761
Standardised approach		
On-balance sheet		
Public sector entity exposures	6	8
Bank exposures	3	2
Corporate exposures	680	624
Regulatory retail exposures	59	63
Other exposures which are not past due exposures	527	395
Past due exposures	39	26
Off-balance sheet		
Off-balance sheet exposures other than over-the-counter derivative transactions	47	31
Over-the-counter derivative transactions	16	7
	<b>1,377</b>	1,156
Credit valuation adjustment	367	343
<b>Total capital requirements for credit risk</b>	<b>15,190</b>	15,260
<b>Market risk:</b>		
Standardised approach		
Interest rate exposures	267	272
Foreign exchange exposures	114	102
<b>Total capital requirements for market risk</b>	<b>381</b>	374
<b>Total capital requirements for operational risk</b>	<b>1,069</b>	1,015
<b>Total capital requirements before deductions</b>	<b>16,640</b>	16,649
<b>Deductions</b>	<b>(31)</b>	(21)
<b>Total capital requirements after deductions</b>	<b>16,609</b>	16,628

## 4 CREDIT RISK ASSESSED USING IRB APPROACH

### (a) Internal rating system and process

#### Nature of exposures within IRB approach

Retail exposures comprise residential mortgages, qualifying revolving retail exposures, small business retail exposures and other retail exposures to individuals. These exposures are categorised into asset classes under the Retail IRB approach.

Wholesale exposures comprise sovereign, bank, corporate, corporate small business (which are assessed under Foundation IRB approach) and specialised lending (which is assessed under the supervisory slotting criteria approach).

Other exposures mainly comprise premises, equipment and other fixed assets and notes and coins, which are assessed under specific risk-weight approach.

#### Structure and control mechanisms for internal rating systems

The Bank adopts various rating systems for the different asset classes under Internal Ratings Based Approach ("IRBA"). There is a robust governance process for the development and approval of a credit risk model. Credit risk models developed are validated by an independent risk unit in the Bank to ensure they are fit for purpose. The models are placed through a rigorous review process prior to endorsement by Hong Kong Credit Risk Committee of the Bank and Group Credit Risk Model Committee of DBSH. The models have also been approved by Risk Executive Committee and Board Risk Management Committee of the Bank and Risk Executive Committee and Board Risk Management Committee of DBSH before use.

To ensure the adequacy and robustness of these rating systems on a continual basis, the Bank conducts regular performance monitoring on these rating systems and reports the results to the Hong Kong Credit Risk Committee and the Board Risk Management Committee of the Bank. This process will highlight any material deterioration in the credit systems for management's attention. In addition, an independent risk unit conducts formal validation annually for each of the rating systems. The validation processes are also subject to an independent review by Internal Audit.

#### Use of internal estimates

The internal credit risk ratings produced by credit rating models are used to calculate the IRB approach capital requirements. In addition, the ratings from the credit models are used as the basis to support the underwriting of credit, monitoring the performance of the portfolios, reporting, stress testing, risk rating migration and to facilitate the calculation for risk based pricing.

#### Definitions of variables

The group-wide credit risk rating framework incorporates Probability of Default ("PD") of a counterparty and loss severity

expressed in terms of Exposure-at-Default ("EAD") and Loss Given Default ("LGD").

PD expressed as a percentage, measures the probability that a borrower will default within one year.

LGD expressed as a percentage, is an estimate of the severity of the loss that the Bank will experience per unit of exposure in the event that the borrower defaults.

EAD is the expected amount of the exposure upon the default of the borrower, which is the sum of the on-balance sheet amounts and/or credit equivalent of the off-balance sheet amounts multiplied by a credit conversion factor determined in accordance with the Banking (Capital) Rules.

#### Methods and data for estimation and validation of the PD, LGD and EAD

For retail exposures, facilities / borrowers with homogenous nature of facility utilisation, payment history, delinquency trend and other transaction characteristics are segmented into homogenous risk pools. PD is estimated by each risk pool based on long run average of historical internal default experience with appropriate adjustment to reflect adverse economic condition to ensure conservatism for capital calculation. The LGD is estimated by dividing the loss by EAD. Loss represents the written-off or specific provision amounts plus collection costs at the end of LGD workout period after netting off recoveries. The LGD is calibrated to reflect adverse economic condition to ensure conservatism for capital calculation. For retail non-revolving exposures, EAD estimation is based on the sum of current outstanding. For retail revolving exposures, EAD estimation is referring to projected further draw down prior to defaults based on historical experience.

For wholesale exposures (including corporate, corporate small business, bank and sovereign exposures), PD generated by models and/or rating templates for individual counterparty is reviewed by credit risk managers. An Adjusted Counterparty Risk Rating ("ACRR") is assigned by taking the counterparty's PD and mapping it to the Bank's internal ACRR scale. The Bank applies the LGD determined by reference to the supervisory LGD estimates provided by the HKMA based on the nature of the collateral for its Foundation IRB portfolios and subordination. These supervisory LGD estimates are used in the computation of risk-weights and regulatory capital calculations for the portfolios. EAD estimation is subject to parameters set by the HKMA.

ACRR is estimated using a 11-grade scale expanded into 19 risk ratings to provide greater rating granularity that corresponds more closely to the Standard & Poor's ("S&P") rating scale. 14 of which are non-default ratings representing varying degrees of strength of financial condition, and 5 are default ratings. These scales are used group-wide for all distinct borrowers.

For specialised lending exposure, rating is assigned based on the borrower and transaction characteristics. The Bank uses supervisory slotting criteria approach in rating its regulatory specialised lending exposure by adopting the specialised lending rating templates. For income-producing real estate specialised lending exposure, the Bank adopts a credit scoring framework to enable a granular assessment of credit risk for the real estate financing activities aligning with the context of Hong Kong real estate market and the DBSH's real estate lending policies.

Model validation process enables the Bank to reaffirm the continuing appropriateness of the models. The model validation

process involves quantitative and qualitative assessment of the model that includes assessment of a model's discriminatory power, calibration, ratings stability and model design. To ensure the models are reliable, an independent validation is conducted by Risk Management Group and an independent review on the validation process is carried out by Internal Audit.

The credit risk ratings for the wholesale exposures have been mapped to likely corresponding external rating equivalents. A description of the risk rating is provided in the following table to give a qualitative explanation of the risk benchmarks.

DBS Probability of Default (PD) Grade (ACRR)	Description of Risk Ratings	Internal Classification	Likely Corresponding HKMA Classification	S&P's Likely Ratings
1	Taking into account the impact of relevant economic, social or geopolitical conditions, capacity to meet its financial commitment is exceptional	Exceptional	Pass	AAA
2	Taking into account the impact of the relevant economic, social or geopolitical conditions, capacity to meet its financial commitment is excellent	Excellent	Pass	AA+, AA, AA-
3	More susceptible to adverse economic, social, geopolitical conditions and other circumstances, capacity to meet its financial commitment is strong	Strong	Pass	A+, A, A-
4A/4B	Adequate protection against adverse economic, social or geopolitical conditions or changing circumstances. More likely to lead to a weakened capacity of the obligor to meet its financial commitment	Good	Pass	BBB+/BBB
5	Relatively worse off than an obligor rated "4B" but exhibits adequate protection parameters	Satisfactory	Pass	BBB-
6A/6B	Satisfactory capacity to meet its financial commitment but capacity may become inadequate due to adverse business, financial, economic, social or geopolitical conditions and changing circumstances	Acceptable	Pass	BB+/BB
7A/7B	Marginal capacity to meet its financial commitment but capacity may become inadequate or uncertain due to adverse business, financial, economic, social or geopolitical conditions and changing circumstances	Marginal	Pass	BB-
8A	Sub-marginal capacity to meet its financial commitment. Adverse business, financial, or economic conditions will likely impair the obligor's capacity or willingness to meet its financial commitment	Sub-Marginal	Pass	B+
8B/8C	Low capacity to meet its financial commitment. Adverse business, financial, or economic condition will likely impair the obligor's capacity or willingness to meet its financial commitment	Special Caution	Special Mention	B/B-
9	Vulnerable to non-payment and is dependent upon favourable business, financial, and economic conditions for the obligor to meet its financial commitment. Likely to have little capacity to meet its financial commitment under adverse conditions	Sub-Performing	Sub-Standard (Non-Defaulting)	CCC - C
10 and Above	An obligor rated "10" and above is in default (as defined under Basel Capital Accord)	Default	Sub-Standard and Below (Defaulting)	D

**(b) Summary of credit exposures by IRB calculation approach**

The following table summarises the Bank's credit exposures as at 31 December:

In HK\$ millions	2014	2013
<b>Retail exposures:</b>		
Retail IRB approach		
Residential mortgages	<b>29,968</b>	34,157
Qualifying revolving retail exposures	<b>55,193</b>	53,225
Small business retail exposures	<b>25</b>	30
Other retail exposures to individuals	<b>9,461</b>	8,839
<b>Wholesale exposures:</b>		
Foundation IRB approach		
Sovereign exposures	<b>24,209</b>	17,359
Bank exposures	<b>119,587</b>	129,665
Corporate exposures	<b>84,718</b>	80,195
Supervisory slotting criteria approach		
Specialised lending	<b>10,312</b>	12,773
<b>Other exposures:</b>		
Specific risk-weight approach	<b>5,699</b>	5,060
	<b>339,172</b>	341,303

**(c) Retail exposures**

Retail portfolios are categorised into asset classes under the Retail IRB approach, namely residential mortgages, qualifying revolving retail exposures, small business retail exposures and other retail exposures to individuals.

Within each asset class, exposures are managed on a portfolio basis. Each account is assigned to a risk pool, taking into consideration factors such as borrower characteristics and collateral type. Loss estimates are based on historical default and realised losses within a defined period. Business-specific credit risk policies and procedures including underwriting criteria, scoring models, approving authorities, frequency of asset quality and business strategy reviews; as well as systems, processes and techniques to monitor portfolio performance against benchmarks are in place. Risk models are being used for associated retail exposures to update risk level of each loan on a monthly basis, reflecting the broad usage of risk models in portfolio quality reviews in accordance with Basel Capital Accord principles.

The following tables summarise the Bank's retail credit exposures by expected loss percentage ("EL%") range as at 31 December:

**Residential mortgages**

In HK\$ millions	2014 Exposure amount	2013 Exposure amount
<b>EL% range</b>		
Up to 0.10%	<b>29,422</b>	33,077
> 0.10% to 0.50%	–	–
> 0.50%	<b>531</b>	1,067
Default	<b>15</b>	13
	<b>29,968</b>	34,157

**Qualifying revolving retail exposures**

In HK\$ millions	2014 Exposure amount	2013 Exposure amount
<b>EL% range</b>		
Up to 5%	<b>52,895</b>	51,191
> 5%	<b>2,246</b>	1,983
Default	<b>52</b>	51
	<b>55,193</b>	53,225

**Small business retail exposures**

In HK\$ millions	2014 Exposure amount	2013 Exposure amount
<b>EL% range</b>		
Up to 0.3%	<b>25</b>	25
> 0.3%	–	5
	<b>25</b>	30

**Other retail exposures to individuals**

In HK\$ millions	2014 Exposure amount	2013 Exposure amount
<b>EL% range</b>		
Up to 0.3%	<b>4,573</b>	4,453
> 0.3%	<b>4,844</b>	4,344
Default	<b>44</b>	42
	<b>9,461</b>	8,839

**(d) Wholesale exposures**

Wholesale exposures comprise sovereign, bank, corporate, corporate small business (which are assessed under Foundation IRB approach) and specialised lending (which is assessed under the supervisory slotting criteria approach).

Sovereign exposures are risk rated using internal risk rating models and guidelines in line with Foundation IRB portfolios.

Bank exposures are assessed using a bank rating model covering various credit risk factors such as capital levels and liquidity, asset quality, earnings, management and market sensitivity. The risk ratings derived are benchmarked against external credit risk ratings to ensure that the internal rating systems are well aligned and appropriately calibrated.

Corporate credits are assessed using approved models and reviewed by credit risk managers taking into consideration of relevant credit risk factors. Credit factors considered in the rating process include the obligor's financial standing and non-financial factors such as management quality, industry outlook and market position. The Counterparty Risk Rating assigned to smaller business borrowers is primarily based on the borrower's financial position and strength, which are assessed via the use of validated quantitative tool. This is supplemented by qualitative factors such as facility utilisation.

Credit ratings under the Foundation IRB portfolios are reviewed on an annual basis at a minimum unless credit conditions require more frequent assessment. The Counterparty Risk Rating process is reinforced by the Facility Risk Rating Framework which considers other exposure risk mitigations, such as collateral, third party guarantees and transfer risks.

A default is considered to have occurred with regard to a particular obligor when either or both of the two following events have taken place.

- Subjective default: Obligor is unlikely to pay its credit obligations in full, without recourse by the Bank to actions such as realising security (if held).
- Technical default: Obligor is past due more than 90 days on any credit obligation to the Bank.

The following tables summarise the Bank's wholesale exposures as at 31 December:

#### Sovereign exposures

Credit Risk Rating	PD range (%)	Exposure amount HK\$'M	Exposure-weighted average risk-weight (%)
<b>2014</b>			
1-3	0.00 - 0.10	24,209	10
<b>2013</b>			
1-3	0.00 - 0.10	17,359	16

#### Bank exposures

Credit Risk Rating	PD range (%)	Exposure amount HK\$'M	Exposure-weighted average risk-weight (%)
<b>2014</b>			
1-3	0.03 - 0.10	107,522	23
4A/4B	0.10 - 0.33	8,084	63
5	0.33 - 0.47	2,340	72
6A/6B	0.47 - 1.11	877	98
7A-9	1.11 - 99.99	764	134
Total		119,587	

Credit Risk Rating	PD range (%)	Exposure amount HK\$'M	Exposure-weighted average risk-weight (%)
<b>2013</b>			
1-3	0.03 - 0.10	112,988	23
4A/4B	0.10 - 0.33	9,861	65
5	0.33 - 0.47	2,821	66
6A/6B	0.47 - 1.11	2,810	106
7A-9	1.11 - 99.99	1,185	134
Total		129,665	

#### Corporate exposures

Credit Risk Rating	PD range (%)	Exposure amount HK\$'M	Exposure-weighted average risk-weight (%)
<b>2014</b>			
1-3	0.03 - 0.10	2,982	19
4A/4B	0.10 - 0.33	2,049	52
5	0.33 - 0.47	2,028	61
6A/6B	0.47 - 1.11	13,639	82
7A-9	1.11 - 99.99	62,991	111
10A-11	100	1,029	188
Total		84,718	

Credit Risk Rating	PD range (%)	Exposure amount HK\$'M	Exposure-weighted average risk-weight (%)
<b>2013</b>			
1-3	0.03 - 0.10	2,353	17
4A/4B	0.10 - 0.33	1,542	41
5	0.33 - 0.47	1,256	68
6A/6B	0.47 - 1.11	13,564	84
7A-9	1.11 - 99.99	60,574	115
10A-11	100	906	102
Total		80,195	

### Specialised lending

Specialised lending IRB portfolios represent real estate finance adopting the supervisory slotting criteria specified under the Banking (Capital) Rules. The supervisory slotting criteria guidelines under the supervisory rating categories are used to determine the risk-weights to calculate the credit risk-weighted exposures.

Obligor grade	Exposure amount HK\$'M	Exposure-weighted average risk-weight (%)
<b>2014</b>		
Strong	2,240	68
Good	6,483	87
Satisfactory	1,588	122
Weak	1	265
<b>Total</b>	<b>10,312</b>	

Obligor grade	Exposure amount HK\$'M	Exposure-weighted average risk-weight (%)
<b>2013</b>		
Strong	1,385	72
Good	8,831	90
Satisfactory	2,534	122
Weak	23	265
<b>Total</b>	<b>12,773</b>	

### (e) Policies for establishing provisions

The policies are set out in Note 2(i) to the financial statements, which describe the Group's accounting policies on the assessment of individual and collective impairment allowances on the financial assets.

### (f) Comparison of rating estimates against actual outcome

#### Comparison of actual loss against expected loss

Actual loss refers to impairment allowances made in the Bank's income statement during the year.

In HK\$ millions	Actual loss for the year ended 31 December 2014	Expected loss as at 31 December 2013
Residential mortgages	–	34
Qualifying revolving retail exposures	126	562
Small business retail exposures	–	–
Other retail exposures to individuals	72	432
Sovereign exposures	–	37
Bank exposures	–	53
Corporate exposures	116	911
	<b>314</b>	<b>2,029</b>

In HK\$ millions	Actual loss for the year ended 31 December 2013	Expected loss as at 31 December 2012
Residential mortgages	–	36
Qualifying revolving retail exposures	89	537
Small business retail exposures	–	–
Other retail exposures to individuals	49	349
Sovereign exposures	–	35
Bank exposures	–	59
Corporate exposures	115	971
	<b>253</b>	<b>1,987</b>

### Comparison of actual default rate against estimated probability of default

% Exposure classes	Actual percentage of default for the year ended 31 December 2014	Estimated 1-year probability of default as at 31 December 2013
Residential mortgages	0.08	0.63
Qualifying revolving retail exposures	0.47	1.08
Small business retail exposures	–	0.34
Other retail exposures to individuals	3.21	6.76
Sovereign exposures	–	0.03
Bank exposures	–	0.48
Corporate exposures	1.16	3.13

% Exposure classes	Actual percentage of default for the year ended 31 December 2013	Estimated 1-year probability of default as at 31 December 2012
Residential mortgages	0.03	0.65
Qualifying revolving retail exposures	0.45	1.00
Small business retail exposures	–	0.29
Other retail exposures to individuals	3.04	6.26
Sovereign exposures	–	0.03
Bank exposures	–	0.52
Corporate exposures	0.99	3.44

The actual default rate is measured by using the number of obligors or number of accounts defaulted, depending on the exposure class for the annual reporting period whereas the estimated probability of default is the long run average default rate estimated for 2014 and 2013.

Expected loss is a measure of expected future losses based on IRB models where PDs are more through-the-cycle and LGDs are on a downturn basis, floored by regulatory minimums. Actual loss is an accounting construct which includes impairment allowances and charge-offs for loans originated in prior years which defaulted in 2014 and 2013 respectively. The two measures of losses are therefore not directly comparable.

### 5 CREDIT RISK ASSESSED USING STANDARDISED APPROACH

The following table indicates the exposure amounts and risk-weighted amounts for each class of exposure under the Standardised approach as at 31 December:

In HK\$ millions	Total exposures	Total exposures after credit risk mitigation	Risk-weighted amount after credit risk mitigation
<b>2014</b>			
<b>On-balance sheet</b>			
Sovereign exposures	–	5	–
Public sector entity exposures	–	379	76
Bank exposures	38	38	38
Corporate exposures	11,147	8,502	8,502
Regulatory retail exposures	1,544	984	739
Other exposures which are not past due exposures	10,247	5,683	6,593
Past due exposures	329	329	486
	<b>23,305</b>	<b>15,920</b>	<b>16,434</b>

<b>Off-balance sheet</b>			
Off-balance sheet exposures other than over-the-counter derivative transactions	677	584	584
Over-the-counter derivative transactions	336	197	197
	<b>1,013</b>	<b>781</b>	<b>781</b>

In HK\$ millions	Total exposures	Total exposures after credit risk mitigation	Risk-weighted amount after credit risk mitigation
------------------	--------------------	---	--

<b>2013</b>			
<b>On-balance sheet</b>			
Sovereign exposures	–	16	–
Public sector entity exposures	–	498	100
Bank exposures	22	22	22
Corporate exposures	8,712	7,798	7,798
Regulatory retail exposures	1,391	1,045	784
Other exposures which are not past due exposures	7,158	4,876	4,936
Past due exposures	234	234	332
	<b>17,517</b>	<b>14,489</b>	<b>13,972</b>

<b>Off-balance sheet</b>			
Off-balance sheet exposures other than over-the-counter derivative transactions	582	387	387
Over-the-counter derivative transactions	240	92	91
	<b>822</b>	<b>479</b>	<b>478</b>

Total exposures in the above table refer to principal amounts or credit equivalent amounts, as applicable, net of individual impairment allowances.

The exposure amounts and risk-weighted amounts in the above table do not take into account the credit assessment ratings assigned by the External Credit Assessment Institutions.

## 6 CREDIT RISK MITIGATION

Credit risk mitigation techniques are taken into account when analysing credit risk-weighted asset amounts. Amounts are adjusted for recognised collateral or recognised guarantees allowed under the Banking (Capital) Rules.

Recognised collateral includes both financial and physical assets. Financial collateral consists of mainly cash deposits, debt

securities and shares, while physical collateral includes land and buildings.

Eligible credit protection is also used to abate credit losses in the event that the exposure defaults. The policies and procedures on credit risk mitigation techniques are set out in Note 41 to the financial statements. The Bank adopts the comprehensive approach for credit risk mitigation and the impact on PD or LGD is based on the same guidelines for Foundation IRB portfolios.

As at 31 December 2014 and 2013, the credit and market risks concentrations within the credit risk mitigation used by the Bank are under a minimal level.

Total exposures covered by recognised collateral or guarantees under Foundation IRB approach and Standardised approach as at 31 December are as follows:

In HK\$ millions	Exposure amount covered by recognised collateral	Exposure amount covered by recognised guarantee
<b>2014</b>		
<b>Foundation IRB approach</b>		
Corporate exposures	32,297	14,279
Bank exposures	10	–
	<b>32,307</b>	<b>14,279</b>
<b>Standardised approach</b>		
Corporate exposures	2,640	5
Regulatory retail exposures	559	–
Other exposures which are not past due exposures	4,186	379
Past due exposures	3	4
Off-balance sheet exposures other than over-the-counter derivative transactions	93	–
Over-the-counter derivative transactions	139	–
	<b>7,620</b>	<b>388</b>
<b>Total</b>	<b>39,927</b>	<b>14,667</b>

In HK\$ millions	Exposure amount covered by recognised collateral	Exposure amount covered by recognised guarantee
<b>2013</b>		
<b>Foundation IRB approach</b>		
Corporate exposures	26,441	12,487
Bank exposures	3,566	–
	<b>30,007</b>	<b>12,487</b>
<b>Standardised approach</b>		
Corporate exposures	899	15
Regulatory retail exposures	345	1
Other exposures which are not past due exposures	1,784	498
Past due exposures	19	7
Off-balance sheet exposures other than over-the-counter derivative transactions	195	–
Over-the-counter derivative transactions	148	–
	<b>3,390</b>	<b>521</b>
<b>Total</b>	<b>33,397</b>	<b>13,008</b>

## 7 COUNTERPARTY CREDIT RISK-RELATED EXPOSURES

The analysis of the default risk exposures and risk-weighted amounts after taking into account the recognised collateral and effect of valid bilateral netting agreements for over-the-counter derivative contracts and securities financing transactions as at 31 December is as follows:

In HK\$ millions	2014	2013
<b>Counterparty credit risk exposures under IRB approach</b>		
<b>Default risk exposures</b>		
(a) Derivative contracts		
– Positive fair values	4,995	8,785
– Potential future exposures	10,586	8,705
	15,581	17,490
Of which:		
– Bank exposures	6,019	8,286
– Corporate exposures	9,562	9,204
	15,581	17,490
Less : Effects of netting arrangement	(3,976)	(6,605)
Default risk exposures after netting	11,605	10,885
Less: Collateral amount		
– Recognised financial collateral	(457)	(432)
– Other eligible collateral	(1,382)	(763)
	9,766	9,690
(b) Securities financing transactions		
Default risk exposures		
– Bank exposures	–	5,150
Less: Collateral amount		
– Recognised financial collateral	–	(3,559)
	–	1,591
<b>Risk-weighted amounts</b>		
(a) Derivative contracts		
– Bank exposures	435	368
– Corporate exposures	10,729	10,859
	11,164	11,227
(b) Securities financing transactions		
– Bank exposures	–	121
	–	121

In HK\$ millions	2014	2013
<b>Counterparty credit risk exposures under Standardised approach</b>		
<b>Default risk exposures</b>		
(a) Derivative contracts		
– Positive fair values	211	143
– Potential future exposures	125	97
	336	240
Of which:		
– Corporate exposures	226	239
– Regulatory retail exposures	–	1
– Other exposures which are not past due exposures	110	–
	336	240
Less: Recognised financial collateral	(139)	(148)
	197	92
<b>Risk-weighted amounts</b>		
(a) Derivative contracts		
– Corporate exposures	194	90
– Regulatory retail exposures	–	1
– Other exposures which are not past due exposures	3	–
	197	91

There is no outstanding credit derivative contract which creates exposures to counterparty credit risk as at 31 December 2014 (2013: Nil).

The current exposure method is used for calculating the Bank's default risk exposures and risk-weighted amount of derivative contracts, using the mark-to-market exposures with appropriate add-on factors for potential future exposures.

If there is a 2-notch downgrade in the Bank's credit ratings, the impact on the Bank's collateral obligations under derivative contracts is minimal.

## 8 LIQUIDITY RATIO

The average liquidity ratio for the year, calculated in accordance with the Fourth Schedule of the Banking Ordinance, is as follows:

	2014	2013
Average liquidity ratio	45.1%	38.8%

The average liquidity ratio is the simple average of each calendar month's average liquidity ratio for the twelve months of the financial year of the Hong Kong office of the Bank.

## 9 SEGMENTAL INFORMATION

### (a) Segmental information by class of business

In HK\$ millions 2014	Group			Total
	Commercial and consumer banking	Treasury	Others	
Total income	<b>7,574</b>	<b>345</b>	<b>126</b>	<b>8,045</b>
Profit before allowances for credit losses	<b>3,679</b>	<b>216</b>	<b>107</b>	<b>4,002</b>
Profit before income tax	<b>3,162</b>	<b>216</b>	<b>274</b>	<b>3,652</b>
Operating assets	<b>185,388</b>	<b>120,930</b>	<b>7,122</b>	<b>313,440</b>
2013				
Total income	7,385	400	411	8,196
Profit before allowances for credit and other losses	3,816	263	351	4,430
Profit before income tax	3,724	266	138	4,128
Operating assets	200,169	100,179	8,311	308,659

Commercial and consumer banking business mainly comprises deposit account services, residential mortgage and other consumer lending, credit card services, corporate lending, trade finance and international banking.

Treasury activities are mainly the provision of foreign exchange services and centralized cash management for deposit taking and lending, trading activities and management of investment securities and the overall funding of the Group.

### (b) Segmental information by booking location

Over 90% of the Group's total income, profit before income tax, total assets, total liabilities, contingent liabilities and commitments are booked in Hong Kong.

### (c) Cross-border claims

Analysis of cross-border claims by location and type of counterparty is as follows:

In HK\$ millions	Group			Total
	Banks	Public sector entities	Others	
<b>2014</b>				
Asia Pacific excluding Hong Kong	<b>106,959</b>	<b>3,868</b>	<b>14,228</b>	<b>125,055</b>
North and South America	<b>1,784</b>	<b>6,717</b>	<b>657</b>	<b>9,158</b>
Europe	<b>1,328</b>	<b>48</b>	<b>2,027</b>	<b>3,403</b>
Others	<b>21</b>	<b>–</b>	<b>2,877</b>	<b>2,898</b>
	<b>110,092</b>	<b>10,633</b>	<b>19,789</b>	<b>140,514</b>
<b>2013</b>				
Asia Pacific excluding Hong Kong	113,189	4,009	13,675	130,873
North and South America	1,513	1,241	439	3,193
Europe	1,892	10	2,470	4,372
Others	25	79	1,131	1,235
	116,619	5,339	17,715	139,673

The above analysis by geographical area is based on the location of the counterparty after taking into account the transfer of risk. In general, transfer of risk applies if the claim is guaranteed by a party in a country which is different from that of the counterparty.

## 10 LOANS AND ADVANCES TO CUSTOMERS

### (a) Loans and advances to customers by loan usage

In HK\$ millions	Bank			
	2014 Outstanding balance	Balance covered by collateral	2013 Outstanding balance	Balance covered by collateral
Gross loans and advances for use in Hong Kong				
Industrial, commercial and financial				
– Property development	2,228	2,226	1,521	1,520
– Property investment	24,828	23,846	27,198	26,135
– Financial concerns	3,815	3,518	1,539	1,244
– Stockbrokers	1,144	64	9	9
– Wholesale and retail trade	19,111	15,497	16,882	13,500
– Manufacturing	11,444	8,284	10,712	7,664
– Transport and transport equipment	10,005	9,547	9,995	9,677
– Recreational activities	161	154	21	17
– Information technology	317	110	241	100
– Others	7,263	5,896	8,931	7,552
Individuals				
– Loans for the purchase of flats in the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme or their respective successor schemes	390	390	506	506
– Loans for the purchase of other residential properties	26,489	26,489	29,615	29,615
– Credit card advances	8,549	–	7,846	–
– Others	13,277	6,918	9,171	3,082
	129,021	102,939	124,187	100,621
Trade finance (including trade bills)	50,179	14,064	69,909	12,307
Gross loans and advances for use outside Hong Kong	6,768	2,714	7,664	2,375
	185,968	119,717	201,760	115,303

### (b) Overdue loans and advances to customers

The overdue loans and advances are analysed as follows:

	Bank			
	2014 HK\$'M	% of gross loans and advances to customers	2013 HK\$'M	% of gross loans and advances to customers
Six months or less but over three months	267	0.14	137	0.07
One year or less but over six months	289	0.16	212	0.10
Over one year	696	0.37	881	0.44
	1,252	0.67	1,230	0.61
Individual impairment allowances made in respect of the above overdue loans and advances	534		733	
Current market value of collateral held against the covered portion of the above overdue loans and advances	986		740	
Covered portion of the above overdue loans and advances	594		450	
Uncovered portion of the above overdue loans and advances	658		780	

**(c) Rescheduled loans and advances to customers**

The rescheduled loans and advances (net of those which have been overdue for over three months and reported in item (b) above) are analysed as follows:

	2014		2013	
	HK\$'M	Bank % of gross loans and advances to customers	HK\$'M	% of gross loans and advances to customers
Rescheduled loans and advances	258	0.14	261	0.13

**(d) Repossessed assets**

As at 31 December 2014, repossessed assets of the Bank amounted to HK\$49 million (2013: HK\$63 million).

**(e) Mainland activities**

The table below summarises the non-bank Mainland China exposure of the Bank (excluding its Macau Branch), categorised by types of counterparties:

In HK\$ millions			
Types of Counterparties	On-balance sheet exposure	Off-balance sheet exposure	Total
<b>2014</b>			
(a) Central government, central government-owned entities and their subsidiaries and joint ventures ("JVs")	1,566	26	1,592
(b) Local governments, local government-owned entities and their subsidiaries and JVs	878	46	924
(c) PRC nationals residing in Mainland China or other entities incorporated in Mainland China and their subsidiaries and JVs	4,165	692	4,857
(d) Other entities of central government not reported in part (a) above	532	1	533
(e) Other entities of local governments not reported in part (b) above	466	128	594
(f) PRC nationals residing outside Mainland China or entities incorporated outside Mainland China where the credit is granted for use in Mainland China	6,135	1,875	8,010
(g) Other counterparties where the exposures are considered by the reporting institution to be non-bank Mainland China exposures	1,276	53	1,329
Total	15,018	2,821	17,839
Total assets after provision	311,354		
On-balance sheet exposures as percentage of total assets	4.82%		

In HK\$ millions Types of Counterparties	On-balance sheet exposure	Off-balance sheet exposure	Total
2013			
(a) Central government, central government-owned entities and their subsidiaries and joint ventures ("JVs")	1,001	1	1,002
(b) Local governments, local government-owned entities and their subsidiaries and JVs	1,328	150	1,478
(c) PRC nationals residing in Mainland China or other entities incorporated in Mainland China and their subsidiaries and JVs	2,742	158	2,900
(d) Other entities of central government not reported in part (a) above	941	–	941
(e) Other entities of local governments not reported in part (b) above	266	–	266
(f) PRC nationals residing outside Mainland China or entities incorporated outside Mainland China where the credit is granted for use in Mainland China	4,927	1,109	6,036
(g) Other counterparties where the exposures are considered by the reporting institution to be non-bank Mainland China exposures	685	85	770
<b>Total</b>	<b>11,890</b>	<b>1,503</b>	<b>13,393</b>
 Total assets after provision	 282,764		
 On-balance sheet exposures as percentage of total assets	 4.20%		

## 11 CURRENCY CONCENTRATION

The table below summarises the Group's assets and liabilities at carrying amounts, categorised by currency:

In HK\$ millions	USD	GBP	EUR	CNY	CAD	CHF	AUD	SGD	NZD	Others	Total
<b>2014</b>											
<b>Hong Kong dollar equivalents</b>											
Spot assets	108,171	2,426	1,848	29,193	90	116	5,167	2,266	33	1,863	151,173
Spot liabilities	(78,794)	(1,912)	(2,396)	(27,292)	(1,579)	(204)	(9,740)	(1,098)	(1,810)	(1,765)	(126,590)
Forward purchases	178,331	1,360	1,463	174,790	1,591	145	5,495	73	1,928	1,066	366,242
Forward sales	(208,836)	(1,773)	(867)	(175,493)	(123)	(103)	(858)	(1,220)	(226)	(1,117)	(390,616)
Net options position	(10)	(122)	6	(68)	(14)	–	75	–	102	(2)	(33)
Net (short) / long non-structural position	(1,138)	(21)	54	1,130	(35)	(46)	139	21	27	45	176
Net structural position	–	–	–	29	–	–	–	–	–	(59)	(30)
<b>2013</b>											
<b>Hong Kong dollar equivalents</b>											
Spot assets	80,767	2,634	1,394	44,838	280	153	5,281	2,143	46	1,393	138,929
Spot liabilities	(67,248)	(1,515)	(2,109)	(22,658)	(2,264)	(239)	(11,220)	(1,221)	(1,220)	(1,339)	(111,033)
Forward purchases	174,230	255	1,156	135,916	2,248	110	7,673	296	1,385	5,020	328,289
Forward sales	(188,697)	(1,419)	(501)	(157,197)	(285)	(9)	(1,608)	(1,219)	(85)	(5,076)	(356,096)
Net options position	48	(14)	–	(1)	2	–	(23)	–	(84)	(2)	(74)
Net (short) / long non-structural position	(900)	(59)	(60)	898	(19)	15	103	(1)	42	(4)	15
Net structural position	–	–	–	29	–	–	–	–	–	(32)	(3)

Structural foreign exchange positions arising from capital investments outside Hong Kong, mainly in Chinese Renminbi and Macau Pataca.

The net options position is calculated based on the delta-weighted position as set out in the prudential return "Foreign Currency Position" issued by the Hong Kong Monetary Authority.

*DBS Bank (Hong Kong) Limited and its Subsidiaries*

# CORPORATE GOVERNANCE REPORT

The following information is disclosed as part of the accompanying information to the financial statements and does not form part of the audited financial statements.

## 1 BOARD AND MANAGEMENT COMMITTEES

DBS Bank (Hong Kong) Limited ("the Bank") is fully committed to effective governance to protect the interests of all our stakeholders and to promote the long term sustainability of the Bank. As an Authorized Institution, the Bank is subject to, and during the year has complied, in all material aspects, with the guidelines set out in the Hong Kong Monetary Authority Supervisory Policy Manual CG-1 Corporate Governance of Locally Incorporated Authorized Institutions issued on 3 August 2012 ("CG-1").

Under the corporate governance structure of the Bank, the role of the Board of Directors is to provide high-level guidance and effective oversight over management. To assist the Board of Directors in fulfilling its responsibilities and in accordance with the best corporate governance practice, the Board Audit Committee and Board Risk Management Committee were established and a number of specialised committees were formed to effectively contribute to the strategic and operational development of the Bank.

CG-1 provides that a licensed bank which is a wholly owned subsidiary may rely on the nomination committee of the holding company to act on its behalf, provided that a majority of the nomination committee members are independent non-executive directors of the holding company. The Nominating Committee of DBS Group Holdings Ltd ("DBSH") performs the nomination committee functions on behalf of the Bank as required under CG-1. Please refer to the Corporate Governance Report in the Annual Report of DBSH for details on the functions of the DBSH Nominating Committee.

The roles, functions and composition of the Board and management committees of the Bank are listed below.

### (a) Board Audit Committee

The Board Audit Committee is authorised by the Board of Directors to investigate any activity of the Bank within its terms of reference. Its main duties include, inter alia, review of the Bank's financial statements before submission to the Board of Directors, recommendations to the Board of Directors on the appointment, re-appointment and removal of the external auditor, approval of remuneration and terms of engagement of the external auditor, review of the external auditor's audit plan, audit report and evaluation of internal accounting controls, approval of hiring including appointment, removal, evaluation and remuneration of Head of Audit, review of the scope and results of internal audits, and effectiveness of internal audit procedures, as well as the adequacy of internal financial, operational and compliance controls, accounting policies and systems.

The Board Audit Committee comprises four non-executive directors. A majority, three out of the four directors, including the Board Audit Committee Chairman are independent non-executive directors of the Bank. All members of the Board Audit Committee have adequate accounting or related financial management experience.

### (b) Board Risk Management Committee

The Board Risk Management Committee is authorised by the Board of Directors to provide oversight of the Bank's risk governance and related matters. The principal duties include, inter alia, oversight of the Internal Capital Adequacy Assessment Process ("ICAAP") and review of ICAAP's overall risk appetite statement and size of operating buffer to be maintained above the regulatory minimum, for approval by the Board of Directors, and review and endorsement of the approach to the allocation of internal capital.

In addition, the Board Risk Management Committee reviews and recommends risk strategy and risk appetite to the Board of Directors, and approves the Bank's overall and specific risk governance frameworks. It also oversees the establishment and the operation of an independent risk management system for managing the Bank's overall risks, and the adequacy of the risk management function. The Board Risk Management Committee obtains assurance that risk management activities are effective and that such activities have sufficient independence, status and visibility. It monitors the types of risk exposure and approaches used to measure and manage risks, and reviews risk reporting on significant risks and risk capital adequacy.

The Board Risk Management Committee obtains assurance that the Bank is on track to meet the Basel Capital Accord requirements according to the plans approved by the Board Risk Management Committee. It is also responsible for setting entity level risk-taking authority in relation to credit risk, market risk, liquidity risk, as well as underwriting and investment risks relating to non-strategic investments (including traded equity and private equity). It also determines the quantum of the house credit limit.

The Board of Directors has established an overall risk appetite which is supervised by the Board Risk Management Committee. This risk appetite framework guides Management in the pursuit of the Bank's strategy and business plans. This is encapsulated in a formal risk appetite statement which considers capital adequacy, earnings volatility and the various risk types including but not limited to credit risk, country risk, market risk, liquidity risk, operational risk and reputational risk. Risk appetite takes into account potential impact arising from stressed conditions and concentration risk.

Portfolio risk limits for the quantifiable risk types are established through a top down approach and operationalised through a formal framework. Other significant risk aspects are guided by qualitative expression of principles.

The risk appetite framework is reviewed annually.

The Board Risk Management Committee comprises five directors. A majority, four out of the five directors, including the Board Risk Management Committee Chairman, are non-executive directors. The Board Risk Management Committee members are appropriately qualified to discharge their responsibilities as they have the relevant technical experience in risk disciplines.

**(c) Hong Kong Management Committee**

The Hong Kong Management Committee is responsible for formulating and implementing DBS's strategy for Hong Kong, as well as the financial and non-financial results of DBS's activities in this geographic segment. Key to its mandate is to provide leadership to the various business and support units in Hong Kong, with a view toward ensuring sound and effective governance, and achieving the targeted financial returns.

Toward this end, the Hong Kong Management Committee is responsible for prioritising business development initiatives (as well as the support infrastructure projects necessary to underpin robust growth), and capital allocation, within the context of DBS's strategy. The Hong Kong Management Committee is also responsible for ensuring that policies and practices are in place to maintain high corporate governance, risk management and compliance standards in Hong Kong. Chaired by the Chief Executive Officer of the Bank, members of the Hong Kong Management Committee comprises senior management staff in Hong Kong.

**(d) Hong Kong Risk Executive Committee**

The Hong Kong Risk Executive Committee provides oversight of all risk types (including those not covered by any committee for a specific risk) and their interactions across all business / support units of the Hong Kong entities, and establishes the overall local risk architecture direction and priorities in line with those established by DBSH. It performs risk review on portfolios, business mandates and all matters involving heightened or complex risk impact. The Hong Kong Risk Executive Committee comprises the Chief Executive Officer of the Bank, the Senior Risk Executive of Hong Kong and representatives from key business units and support units.

**(e) Hong Kong Asset and Liability Committee**

The Hong Kong Asset and Liability Committee oversees asset and liability management activities, including strategies to enhance the quality of net interest income, liquidity management and structural FX management for Hong Kong country and including Macau. The Hong Kong Asset and Liability Committee also reviews the Bank's capital position and adequacy; assesses capital deployment, and approves risk capital quantification methodologies. The Hong Kong Asset and Liability Committee comprises the Chief Executive Officer of the Bank and representatives from the relevant business units and support units and others nominated by the Chairman of the Hong Kong Asset and Liability Committee.

**(f) Hong Kong Credit Risk Committee**

The Hong Kong Credit Risk Committee serves as an executive forum for discussion and decisions on all aspects of credit risk and its management. It assesses credit risk taking and risk-return tradeoffs. The Hong Kong Credit Risk Committee identifies and monitors credit risk portfolio, special loan and asset review situations, specific credit concentrations and trends. In respect of continually determining the suitability of DBS Hong Kong's credit risk management strategy and framework as well as Internal Ratings-Based systems in meeting the standards under Basel Capital Accord, the Hong Kong Credit Risk Committee exercises active oversight to ensure the continuing appropriateness of the rating systems, the parameterization process and the stress testing process. The members of the Hong Kong Credit Risk Committee are the Chief Credit Officer, Hong Kong, representatives from relevant business, credit, risk management and other units.

**(g) Hong Kong Market and Liquidity Risk Committee**

The Hong Kong Market and Liquidity Risk Committee provides comprehensive and location-wide oversight, direction and counsel relating to the management of market and liquidity risks. It serves as an executive forum for discussions and decisions on all aspects of market and liquidity risks and their management. It maintains oversight on effectiveness of market and liquidity risk management infrastructure, including framework, policies, people, processes, information, methodologies and systems on market and liquidity risks. It sets standards and provides necessary guidance on the establishment and maintenance of the location-wide liquidity contingency plan. The Hong Kong Market and Liquidity Risk Committee comprises senior management from Risk Management, representatives from relevant business units and support units and others nominated by the Chairman of the Hong Kong Market and Liquidity Risk Committee.

**(h) Hong Kong Operational Risk Committee**

The Hong Kong Operational Risk Committee provides comprehensive location-wide oversight and direction relating to the management of operational risks. It monitors and reviews the effectiveness of operational risk management framework, policies, processes, methodologies and infrastructures. It performs top-down assessment and monitors critical operational risk exposures and provides direction for resolution of critical operational risk issues and monitors issue resolution. The Hong Kong Operational Risk Committee comprises the Head of Risk Management Group - Operational Risk, representatives from key business units, support units and others nominated by the Chairman of the Hong Kong Operational Risk Committee.

## 2 DISCLOSURE ON REMUNERATION PURSUANT TO THE HKMA SUPERVISORY POLICY MANUAL CG-5 "GUIDELINE ON A SOUND REMUNERATION SYSTEM"

### (a) Design and implementation of the remuneration system

DBS Bank (Hong Kong) Limited adopts the remuneration policy and practices formulated by DBS Group Holdings Ltd ("DBSH"). Please refer to the Annual Report of DBSH for details of the Board Compensation and Management Development Committee and major characteristics of the remuneration system.

### (b) Aggregate quantitative information on remuneration for senior management and key personnel for the year ended 31 December 2014 are as follows:

Senior management is defined as those who are responsible for oversight of the Bank's strategy or activities or those of the Bank's material business lines. Key personnel is defined as individual employees whose duties or activities in the course of their employment involve the assumption of material risk or taking on of material exposures on behalf of the Bank.

Breakdown of remuneration awarded	2014	2013
Number of senior management	10	10
Number of key personnel	1	1
<b>In HK\$ millions</b>		
Fixed remuneration		
• Cash based	35	32
• Share based	–	–
• Other	–	–
Variable remuneration (i)		
• Cash based	37	36
• Share based	24	27
• Other	–	–
	<b>96</b>	<b>95</b>

In HK\$ millions Breakdown of deferred remuneration	2014	2013
• Outstanding – vested	–	–
• Outstanding – unvested	87	63
• Awarded during the year	24	27
• Paid out during the year	15	6
• Reductions in current year due to ex-post adjustment – explicit (ii)	–	–
• Reductions in current year due to ex-post adjustment – implicit (iii)	–	–

- (i) Cash and share based variable remuneration are subject to the approval of the DBSH Board of Directors.
- (ii) Examples of explicit ex-post adjustments include malus, clawbacks, or similar reversals or downward revaluation of awards.
- (iii) Examples of implicit ex-post adjustments include fluctuations in the value of shares or performance units.

No senior management or key personnel has been awarded with new guaranteed bonus or severance payments in 2014 (2013: Nil).

No sign-on award being paid to senior management or key personnel (2013: two cases amounting to HK\$1,461,313).

## 3 INTERNAL AUDIT

Internal Audit is a function that is independent of the activities it audits. The objective, scope of authority and responsibility of Internal Audit are defined in the Hong Kong Audit charter, which is approved by the Board Audit Committee. Head of Internal Audit reports functionally to the Head of Group Audit and the Board Audit Committee, as well as administratively to the Chief Executive Officer.

Internal Audit's responsibilities include:

- (i) Evaluating the reliability, adequacy and effectiveness of the Bank's risk management and internal control systems, including whether there is prompt and accurate recording of transactions and proper safeguarding of assets;
- (ii) Providing an independent assessment of the Bank's credit management processes, portfolio strategies and portfolio quality;
- (iii) Reviewing whether the Bank complies with laws and regulations and adheres to established policies; and
- (iv) Reviewing whether management is taking appropriate steps to address control deficiencies.

Internal Audit adopts a risk-based approach in its auditing activities. An annual audit plan is developed using a structured risk and control assessment framework, where Internal Audit assesses the inherent risk and control effectiveness of each auditable entity in the Bank. The assessment also covers risks arising from new lines of business or product. Audit projects are planned based on the results of the assessment, with priority given to auditing higher risk areas. Consideration is also given to conducting audit projects required by regulators. Appropriate resources are deployed to complete the plan, which is reviewed and approved by the Board Audit Committee.

Internal Audit has unfettered access to the Board Audit Committee and senior management, as well as the right to seek information and explanation. Internal Audit has an organisational and strategic alignment to the Bank. The positioning of Internal Audit is such that the Head of Internal Audit has a seat in the Bank's Management Committee attending all the business reviews and strategic planning forums.

Internal Audit staff is required to adhere to the Code of Conduct as well as the Code of Ethics established by the Institute of Internal Auditors (IIA), from which the principles of objectivity, competence, confidentiality and integrity are based.

Audit reports containing identified issues and corrective action plans are reported to the Board Audit Committee and senior management. The progress of the corrective action plans is monitored through a centralised issue management system. Information on outstanding issues is included in regular reports to the Board Audit Committee, senior management and business and support unit heads.

Internal Audit apprises the regulators and external auditors of all relevant audit matters. It works closely with the external auditors to coordinate audit efforts.

In line with leading practices, Group Audit has established a quality assurance and improvement programme that covers all aspects of its audit activity and conforms to the International Standards for the Professional Practice of Internal Auditing. The programme includes periodic internal quality assurance reviews, self-assessments based on standards established by the IIA and internal audit methodologies, stakeholder surveys and industry benchmarking surveys. External quality assessments are also carried out at least once every five years by qualified professionals from an external organisation. The most recent assessment was conducted in 2013 by KPMG. KPMG is also the independent assessor for Group Audit's quarterly internal quality assurance review in 2014.

Group Audit achieved another significant milestone during its participation in the 2014 Securities Investors Association of Singapore (SIAS) Investors' Choice Awards, jointly organised by the SIAS, IIA Singapore and Singapore Management University. Group Audit emerged as the runner-up for the Internal Audit Excellence Award, and top among banks for the fourth year running. These wins are significant for the Group as the SIAS Investors' Choice Awards is one of only few awards in the market that recognises public-listed companies for their exemplary corporate governance and transparency practices.

Group Audit continues to improve on its approach towards the internal audit function. One of its initiatives is the industrialisation of computer assisted audit techniques (CAATs) as well as more complex data analytics, for greater efficiency and effectiveness, as well as to enhance productivity.

Technology will continue to play a central role in driving innovation and process automation to improve quality and efficiency in performing audits and managing internal department processes. As part of its Future of Audit initiative, Group Audit embarked on a collaborative effort with A\*Star-I2R (Agency for Science, Technology and Research – Institute for Infocomm Research) researchers to develop predictive models in anticipating emerging risks. The predictive model will be cascaded to each audit location and shared with respective business and support units for application and usage. Group Audit is continuously looking into ways to connect the dots by sharing insights on issues, and how one issue is connected to another, with all stakeholders. This boundary-spanning sharing also crosses business segments and geographical locations.

Last but not least, Group Audit continues to invest in its people, ensuring that it is adequately staffed to meet the demands of internal audit. Proper training roadmaps and up-skilling programmes are instituted to constantly enhance the knowledge, skills and competencies of its internal auditors.