

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

Annual Report 2013

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

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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 2013.

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 24 to the financial statements.

Results and appropriations

The results of the Group for the year ended 31 December 2013 are set out in the consolidated income statement on page 5.

An interim dividend of HK\$0.171 per share totalling HK\$1,200 million was paid on 9 April 2013 for the year ended 31 December 2013 (2012: Nil).

The directors do not recommend the payment of a final dividend for the year ended 31 December 2013 (2012: Nil).

Reserves

Details of the movements in the reserves of the Bank and the Group during the year are set out in Note 34 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 25 to the financial statements.

Donations

Donations made by the Group during the year amounted to HK\$3,363,000 (2012: HK\$775,000).

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

(appointed on 8 April 2013)

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

REPORT OF THE DIRECTORS (CONTINUED)

Directors (continued)

In accordance with Article 98 of the Bank's Articles of Association, Mr Alexander Reid Hamilton will retire from office at the forthcoming Annual General Meeting and, being eligible, offer himself for re-election.

Directors' interests in contracts

During the year, 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 is 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.

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

Under the DBSH Share Plan, DBSH's ordinary shares may be granted to DBSH Group executives who hold such rank as may be determined by the Compensation and Management Development Committee ("CMDC") of DBSH appointed to administer the DBSH Share Plan from time to time. The awards could be performance-based and/or time-based.

Where time-based awards are granted, they will only vest after the satisfactory completion of time-based service conditions. Participants are awarded shares of DBSH, their equivalent cash value or a combination of both as part of their deferred bonus (at the discretion of the CMDC).

A time-based award comprises two elements, namely, the main award and the "retention" award (previously known as "kicker" award). The shares comprised in the "retention" award constitute twenty percent of the shares comprised in the main award. Effective 2010, the deferral period for unvested shares was extended from a 3-year period to a 4-year period showing a more prudent risk management arrangement. Under the new vesting schedule, thirty-three percent of the shares comprised in the main award will vest two years after the date of grant. A further thirty-three percent of the shares comprised in the main award will vest three years after the date of grant. The remainder thirty-four percent of the shares comprised in the main award, together with the shares comprised in the "retention" award, will vest four years after the date of grant. For time-based awards, the fair value of the shares awarded are computed based on the market price of the ordinary shares at the time of the award and is amortized through the income statement over the vesting period.

During the year, a total of 16,299 DBSH share awards were granted to Mr. Seah Lim Huat, Peter pursuant to the DBSH Share Plan and 21,338 shares were vested in him under the Share Plan during the year.

During the year, Mr. Piyush Gupta was eligible to receive awards under the Share Plan. A total of 367,488 DBSH share awards were granted to him and a total of 99,564 DBSH shares were vested in him under the Share Plan during the year.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

REPORT OF THE DIRECTORS (CONTINUED)

Arrangements to acquire shares (continued)

During the year, Mr. J. E. Sebastian Paredes Muirragui was eligible to receive awards under the Share Plan. A total of 73,511 DBSH share awards were granted to him and no shares were vested in him under the Share Plan during the year.

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, 24 January 2014

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 91, which comprise the consolidated and company balance sheets as at 31 December 2013, 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 141 of the Hong Kong Companies Ordinance and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of 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 2013, 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, 24 January 2014

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

CONSOLIDATED INCOME STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2013

(Expressed in millions of Hong Kong dollars)

| | Note | 2013 HK\$'M | 2012 HK\$'M |
|---|------|----------------|----------------|
| Interest income | 4 | 6,310 | 6,355 |
| Interest expense | 5 | (1,884) | (2,173) |
| Net interest income | | 4,426 | 4,182 |
| Net fee and commission income | 6 | 1,610 | 1,430 |
| Net income from financial instruments at fair value through profit or loss | 7 | 1,694 | 1,140 |
| Net income from financial investments | 8 | 79 | 103 |
| Other income | 9 | 353 | 493 |
| Total income | | 8,162 | 7,348 |
| Total expenses | 10 | (3,766) | (3,591) |
| Profit before allowances for credit and other losses | | 4,396 | 3,757 |
| Allowances for credit and other losses | 11 | (302) | (59) |
| Profit after allowances for credit and other losses | | 4,094 | 3,698 |
| Share of profit of a joint venture | | 34 | 37 |
| Profit before income tax | | 4,128 | 3,735 |
| Income tax expense | 13 | (604) | (508) |
| Profit attributable to shareholders | 14 | 3,524 | 3,227 |
| Dividend | 15 | 1,200 | – |

The notes on pages 12 to 91 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 2013

(Expressed in millions of Hong Kong dollars)

| | 2013 HK\$'M | 2012 HK\$'M |
|--|---------------------|---------------------|
| Profit attributable to shareholders | <u>3,524</u> | <u>3,227</u> |
| Other comprehensive income | | |
| Available-for-sale financial investments | | |
| – Net valuation taken to equity | (36) | 69 |
| – Amortisation of reserve to income statement arising from reclassification of available-for-sale financial investments to loans and receivables | 1 | 2 |
| – Transferred to income statement | (50) | (86) |
| – Deferred income tax credited / (charged) to equity | <u>13</u> | <u>(7)</u> |
| Other comprehensive income attributable to shareholders, net of tax | <u>(72)</u> | <u>(22)</u> |
| Total comprehensive income attributable to shareholders | <u><u>3,452</u></u> | <u><u>3,205</u></u> |

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 12 to 91 form part of these financial statements.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

CONSOLIDATED BALANCE SHEET

AS AT 31 DECEMBER 2013

(Expressed in millions of Hong Kong dollars)

| | Note | 2013 HK\$'M | 2012 HK\$'M |
|---|-------|----------------|----------------|
| Assets | | | |
| Cash and balances with banks | 16 | 5,831 | 7,318 |
| Placements with and advances to banks | 17 | 57,505 | 57,951 |
| Trading securities | 18 | 4,302 | 7,577 |
| Derivatives | | 9,084 | 5,215 |
| Financial investments | 19 | 24,536 | 24,637 |
| Loans and advances to customers | 20 | 200,254 | 175,651 |
| Other assets | 22 | 4,118 | 4,154 |
| Interest in a joint venture | 23 | 364 | 330 |
| Deferred tax assets | 31(b) | 39 | 11 |
| Properties and other fixed assets | 25 | 2,626 | 2,668 |
| Total assets | | <u>308,659</u> | <u>285,512</u> |
| Liabilities | | | |
| Deposits and balances from banks | | 4,751 | 9,356 |
| Trading liabilities | 26 | 3,122 | 6,450 |
| Derivatives | | 9,091 | 5,109 |
| Financial liabilities designated at fair value through profit or loss | 27 | 8,122 | 1,779 |
| Deposits from customers | 28 | 230,269 | 212,333 |
| Certificates of deposit issued | 29 | 7,564 | 7,283 |
| Other liabilities | 30 | 7,231 | 7,217 |
| Current income tax liabilities | 31(a) | 168 | 143 |
| Amount due to a joint venture | 23 | 2,887 | 2,641 |
| Subordinated liability | 32 | 4,187 | 4,186 |
| Total liabilities | | <u>277,392</u> | <u>256,497</u> |
| Equity | | | |
| Share capital | 33 | 7,000 | 7,000 |
| Reserves | 34 | 24,267 | 22,015 |
| Total equity | | <u>31,267</u> | <u>29,015</u> |
| Total liabilities and equity | | <u>308,659</u> | <u>285,512</u> |

The notes on pages 12 to 91 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

BANK LEVEL BALANCE SHEET

AS AT 31 DECEMBER 2013

(Expressed in millions of Hong Kong dollars)

| | Note | 2013 HK\$'M | 2012 HK\$'M |
|---|-------|----------------|----------------|
| Assets | | | |
| Cash and balances with banks | 16 | 5,831 | 7,318 |
| Placements with and advances to banks | 17 | 57,502 | 57,948 |
| Trading securities | 18 | 4,302 | 7,577 |
| Derivatives | | 9,084 | 5,215 |
| Financial investments | 19 | 24,536 | 24,637 |
| Loans and advances to customers | 20 | 200,254 | 175,651 |
| Other assets | 22 | 4,118 | 4,154 |
| Interest in a joint venture | 23 | 1 | 1 |
| Deferred tax assets | 31(b) | 39 | 11 |
| Subsidiaries | 24 | 48 | 152 |
| Properties and other fixed assets | 25 | 2,626 | 2,668 |
| Total assets | | <u>308,341</u> | <u>285,332</u> |
| Liabilities | | | |
| Deposits and balances from banks | | 4,751 | 9,356 |
| Trading liabilities | 26 | 3,122 | 6,450 |
| Derivatives | | 9,091 | 5,109 |
| Financial liabilities designated at fair value through profit or loss | 27 | 8,122 | 1,779 |
| Deposits from customers | 28 | 230,269 | 212,333 |
| Certificates of deposit issued | 29 | 7,564 | 7,283 |
| Other liabilities | 30 | 7,229 | 7,215 |
| Current income tax liabilities | 31(a) | 168 | 143 |
| Amount due to a joint venture | 23 | 2,887 | 2,641 |
| Amounts due to subsidiaries | 24 | 83 | 234 |
| Subordinated liability | 32 | 4,187 | 4,186 |
| Total liabilities | | <u>277,473</u> | <u>256,729</u> |
| Equity | | | |
| Share capital | 33 | 7,000 | 7,000 |
| Reserves | 34 | 23,868 | 21,603 |
| Total equity | | <u>30,868</u> | <u>28,603</u> |
| Total liabilities and equity | | <u>308,341</u> | <u>285,332</u> |

The notes on pages 12 to 91 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 2013

(Expressed in millions of Hong Kong dollars)

| | Share capital HK\$'M | Share premium HK\$'M | Other reserves HK\$'M | Retained earnings HK\$'M | Total equity HK\$'M |
|--------------------------------|----------------------------|----------------------------|-----------------------------|--------------------------------|---------------------------|
| Balance as at 1 January 2012 | 7,000 | 595 | 2,657 | 15,558 | 25,810 |
| Total comprehensive income | — | — | (22) | 3,227 | 3,205 |
| Balance as at 31 December 2012 | <u>7,000</u> | <u>595</u> | <u>2,635</u> | <u>18,785</u> | <u>29,015</u> |
| 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 | <u>7,000</u> | <u>595</u> | <u>2,563</u> | <u>21,109</u> | <u>31,267</u> |

The notes on pages 12 to 91 form part of these financial statements.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

CONSOLIDATED CASH FLOW STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2013

(Expressed in millions of Hong Kong dollars)

| | Note | 2013 HK\$'M | 2012 HK\$'M |
|--|------|----------------|----------------|
| Cash flows from operating activities | | | |
| Profit before income tax | | 4,128 | 3,735 |
| Adjustments for non-cash items: | | | |
| Net gain on disposal of properties and other fixed assets | | (275) | (343) |
| Fair value adjustment on investment properties | | (34) | (69) |
| Allowances for credit and other losses | | 302 | 59 |
| Write-off of properties and other fixed assets | | 5 | 1 |
| Depreciation | | 220 | 200 |
| Advances written off net of recoveries | | (357) | (392) |
| Revaluation for certificates of deposit issued | | (179) | 62 |
| Amortisation of discount on certificates of deposit issued | | 4 | 36 |
| Interest expense for certificates of deposit issued | | 163 | 269 |
| Interest expense for subordinated liability | | 118 | 59 |
| Share of profit of a joint venture | | (34) | (37) |
| | | <hr/> | <hr/> |
| Profit before changes in operating assets and liabilities | | 4,061 | 3,580 |
| Increase / (decrease) in: | | | |
| Deposits and balances from banks | | (4,605) | (12,589) |
| Trading liabilities | | (3,328) | (124) |
| Deposits from customers | | 24,287 | 28,329 |
| Amount due to a joint venture | | 246 | 153 |
| Other liabilities and derivatives | | 4,020 | (3,544) |
| (Increase) / decrease in: | | | |
| Placements with and advances to banks | | 18,121 | (27,463) |
| Trading securities | | 1,340 | 3,281 |
| Advances to customers | | (24,548) | 18,767 |
| Financial investments | | (410) | (964) |
| Other assets and derivatives | | (3,833) | 2,084 |
| | | <hr/> | <hr/> |
| Net cash generated from operating activities before income tax | | 15,351 | 11,510 |
| Hong Kong profits tax paid | | (588) | (590) |
| Overseas tax paid | | (6) | (8) |
| | | <hr/> | <hr/> |
| Net cash generated from operating activities | | 14,757 | 10,912 |

The notes on pages 12 to 91 form part of these financial statements.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

CONSOLIDATED CASH FLOW STATEMENT (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2013

(Expressed in millions of Hong Kong dollars)

| | Note | 2013 HK\$'M | 2012 HK\$'M |
|---|-------|----------------------|-----------------|
| Cash flows from investing activities | | | |
| Purchase of fixed assets | | (194) | (184) |
| Proceeds from disposal of properties and other fixed assets | | <u>320</u> | <u>378</u> |
| Net cash generated from investing activities | | <u>126</u> | <u>194</u> |
| Cash flows from financing activities | | | |
| Dividend paid | | (1,200) | – |
| Interest paid for certificates of deposits issued | | (187) | (259) |
| Interest paid for subordinated liability | | (118) | (56) |
| Issuance of certificates of deposit | 36(a) | 2,230 | 11,105 |
| Redemption of certificates of deposit issued | 36(a) | <u>(1,784)</u> | <u>(20,493)</u> |
| Net cash used in financing activities | | <u>(1,059)</u> | <u>(9,703)</u> |
| Exchange differences and other adjustments | | <u>3</u> | <u>28</u> |
| Net change in cash and cash equivalents | | 13,827 | 1,431 |
| Cash and cash equivalents as at 1 January | | <u>27,330</u> | <u>25,899</u> |
| Cash and cash equivalents as at 31 December | 36(b) | <u>41,157</u> | <u>27,330</u> |

The notes on pages 12 to 91 form part of these financial statements.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Hong Kong dollars)

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 24 January 2014.

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”) and the requirements of the Hong Kong Companies Ordinance.

The consolidated financial statements are presented in Hong Kong dollars and rounded to the nearest million, unless otherwise stated. They are prepared on the historical cost convention, except for derivative financial instruments, available-for-sale financial assets, financial assets and financial liabilities held at fair value through profit or loss and investment properties, which have been measured at fair value. In addition, the carrying amounts of assets and liabilities that are designated as hedged items in a fair value hedge are adjusted for fair value changes attributable to the hedged risks.

The preparation of financial statements in conformity with HKFRSs requires management to exercise judgement, use estimates and make assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. 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) Adoption of new and revised accounting standards

On 1 January 2013, the Group adopted the following new or revised HKFRSs that are issued by HKICPA and relevant for the Group:

Amendments to HKAS 1 Presentation of Financial Statements

The amendments require entities to group items presented in other comprehensive income on the basis of whether they are potentially recycled to the income statement (reclassification adjustments). Where an entity presents its comprehensive income into two separate statements, the amendments specifically require these statements to be presented consecutively.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

(b) Adoption of new and revised accounting standards (continued)

Amendments to HKFRS 7 Financial Instruments: Disclosures – Offsetting financial assets and liabilities

The amendments introduce more extensive disclosures which focus on quantitative information about recognised financial instruments that are offset on the balance sheet as well as those that are subject to master netting or similar arrangements irrespective of whether they are offset on the balance sheet. Please see note 41 for additional disclosures.

HKFRS 10 Consolidated Financial Statements

HKFRS 10 establishes control as the basis for determining which entities are consolidated. It provides a single model to be applied in the control analysis for all investees, including special purpose entities that are previously within the scope of HK(SIC) INT 12 Consolidation – Special Purpose Entities. Control exists under HKFRS 10 when the investor has power, exposure to variable returns and the ability to use that power to affect its returns from the investee.

HKFRS 12 Disclosure of Interests in Other Entities

HKFRS 12 combines the disclosure requirements in a single disclosure standard. It requires the disclosure of summarised financial information about each subsidiary that has material non-controlling interests as well as material associates and joint ventures. It also sets out new disclosure requirements such as financial or other support provided to consolidated and unconsolidated structure entities, and financial information about unconsolidated structure entities that the reporting entity had sponsored.

HKFRS 13 Fair Value Measurement

HKFRS 13 unifies the definition for fair value and establishes a single framework for measuring fair value. It replaces and expands the disclosure requirements about fair value measurements in other HKFRSs, including HKFRS 7. Please see Note 25 and 35 for additional disclosures in this regard.

HKFRS 11 Joint Arrangements

HKFRS 11 applies to all parties to a joint arrangement including those who participate in, but do not have joint control of, a joint arrangement. The standard prescribes the accounting for joint operations and joint ventures in both consolidated and separate financial statements. Previously, the Group recognises its interest in jointly controlled entity using the proportionate consolidation method under HKAS 31 Interests in Joint Ventures. With the adoption of HKFRS 11, the interest in joint venture is accounted for under the equity method. The equity method has been applied retrospectively and the comparative figures have been restated, as summarised below. The retrospective application of HKFRS 11 has no impact to the Group's retained earnings.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

(b) Adoption of new and revised accounting standards (continued)

| | As previously reported HK\$'M | Adjustment HK\$'M | As restated HK\$'M |
|--|-------------------------------------|----------------------|-----------------------|
| Consolidated income statement for the year ended 31 December 2012 | | | |
| Interest income | 6,493 | (138) | 6,355 |
| Interest expense | 2,229 | (56) | 2,173 |
| Net interest income | 4,264 | (82) | 4,182 |
| Net fee and commission income | 1,458 | (28) | 1,430 |
| Total income | 7,458 | (110) | 7,348 |
| Total expenses | 3,639 | (48) | 3,591 |
| Allowances for credit and other losses | 77 | (18) | 59 |
| Share of profit of a joint venture | – | 37 | 37 |
| Profit before income tax | 3,742 | (7) | 3,735 |
| Income tax expense | 515 | (7) | 508 |
| Consolidated balance sheet as at 31 December 2012 | | | |
| Advances to customers | 175,625 | 26 | 175,651 |
| Other assets | 4,157 | (3) | 4,154 |
| Interest in a joint venture | – | 330 | 330 |
| Deferred tax assets | 14 | (3) | 11 |
| Properties and other fixed assts | 2,669 | (1) | 2,668 |
| Other liabilities | 8,188 | (971) | 7,217 |
| Amount due to a joint venture | 1,321 | 1,320 | 2,641 |

Except for the above restatements and additional disclosures, there is no significant impact on the Group's financial statements from the adoption of the new or revised HKFRSs.

General Accounting Policies

(c) **Group accounting**

The consolidated financial statements incorporate the financial statements of the Bank, its subsidiaries and its interest in a joint venture.

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

Subsidiaries

Subsidiaries are entities controlled by the Group. 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. When assessing whether the Group has power, only substantive rights (held by the group and other parties) are considered. Subsidiaries are consolidated from the date control is transferred to the Group to the date control ceases.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

(c) Group accounting (continued)

Investment in a joint venture

A joint venture is an arrangement whereby the Group and other parties contractually agree to share control of the arrangement, and have rights to the net assets of the arrangement. The Group recognises its interest in joint venture 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.

(d) Foreign currency translation

(i) Functional and presentation currency

Items 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.

(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 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 foreign currency are translated using the exchange rate at the date of the transaction.

(iii) Foreign operations

The results and financial positions of the Group's operations whose functional currency is not Hong Kong dollars are translated into Hong Kong dollars in the following manner:

- Assets and liabilities are translated at the exchange rate ruling at the balance sheet date;
- Income and expenses in the income statement are translated at an average exchange rate approximating the exchange rates at the dates of the transactions; and
- All resulting exchange differences are taken to the translation reserve grouped under "Other reserves".

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

Income Statement

(e) Revenue recognition

(i) Interest income and interest expense

Interest income and interest expense as presented in Note 4 and 5 respectively represent the interest on all assets and liabilities regardless of the classification and measurement of the asset and liabilities on accrual 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 which the related service is provided or credit risk is undertaken. Specifically

- Card related fee and commission income is recognised net of interchange fees paid.
- Income from issued financial guarantees are generally amortised over the duration of the instrument. For loan commitments, revenue is recognised over the period covered by the commitment. Please see Note 2(k) for the accounting policy on such commitments. Loan syndication fee received as payment for arranging a loan is recognised as revenue when the act has been completed, i.e. when the syndication has been finalised and the Group retained no part of the loan package for itself, or retained a part at the same effective interest rate as for the other participants.
- Management and advisory fees are recognised over the period for which the services are provided.

Expenses that are required, directly related and incremental to the revenue generation are offset in the net fee and commission income. These typically include brokerage fees paid, card-related expenses, sales commissions but do not include expenses for services delivered over a period (service contracts) and other expenses that are not directly related to any specific transaction.

(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", while that arising from available-for-sale financial assets is recognised in "Net income from financial investments".

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

(e) Revenue recognition (continued)

(iv) Rental income

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

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

Balance Sheet

(f) Financial assets

Initial recognition

Purchases and sales of all financial assets regardless of the subsequent classification and measurement are recognised on the date that the Group enters into the contractual provisions of the arrangements with counterparties. When the Group acts in a capacity as trustee or other fiduciary capacity without the direct control or direct benefit from the assets, these assets and the corresponding income belonging to a customer are excluded from the financial statements.

Financial assets are initially recognised at fair value plus transaction costs except for financial assets at fair value through profit or loss, for which transaction costs are expensed off immediately. The fair value of a financial asset on initial recognition is usually 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 segments 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 payment, 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 in which they arise.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

(f) Financial assets (continued)

Classification and subsequent measurement (continued)

- Derivatives (including embedded derivatives that are required to be separated from their host contracts under HKAS 39) are also categorised as “held for trading” unless they are designated as hedges in accordance with Note 2(n). 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. Please see Note 2(n) for details on hedging and hedge accounting.

Reclassification of financial assets

When the purpose for holding a financial asset change, or when HKFRS otherwise require 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 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 to sell the asset in an orderly transaction between market participants at the measurement date.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

(f) *Financial assets (continued)*

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 have been transferred and the Group has transferred 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. If all or substantially all risks and rewards are retained, the transferred financial assets are not derecognised from the balance sheet. Transactions where transfers of financial assets result in the Group retaining all or substantially all risks and rewards include repurchase transactions. They also include certain transactions where control over the financial asset is retained, for example by a simultaneous transaction with the same counterparty to which the asset is transferred such as options. In such cases the Group continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

Please refer to Note 40 for disclosures on transfers of financial assets.

(g) *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 trading securities and available-for-sale financial investments which are readily convertible into cash.

(h) *Impairment of financial assets*

Financial assets carried at amortised cost

The Group assesses at each balance sheet date whether there is objective 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

(h) Impairment of financial assets (continued)

Financial assets carried at amortised cost (continued)

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.

Available-for-sale financial investments

The Group assesses at each balance sheet date whether there is objective evidence that an available-for-sale financial investment is impaired. In the case of an equity investment, a significant or prolonged decline in the fair value of security below its cost is considered in determining whether the asset is impaired. When there is objective evidence of an impairment of an available-for-sale financial investment, the cumulative loss – measured as the difference between the amortised 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. Impairment losses recognised in the income statement on the equity investments are not reversed, until the equity investments are disposed of. A subsequent recovery in the value of an available-for-sale debt instrument whose value has been impaired is reversed through the income statement if there has been an identifiable event that led to the recovery.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

(i) 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

Properties 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 properties. 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 |

(iii) Furniture, fixtures and equipment

Furniture, fixtures and equipment are stated at cost less depreciation and impairment losses. Depreciation on furniture, fixtures and equipment is calculated using the straight-line method over the estimated useful lives of between 3 and 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 25 for the details of properties and other fixed assets and their movements during the year.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

(j) Financial liabilities

Initial recognition

Financial liabilities are initially recognised at fair value, net of transaction costs incurred, except for financial liabilities at fair value through profit or loss, for which transaction costs are expensed off immediately.

Classification and subsequent measurement

The Group 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) or designated by management on initial recognition (designated under the fair value option). These often pertain to short positions in securities for the purpose of ongoing market making, hedging or trading.

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 classified as held for trading unless they are designated as hedging instruments and are carried at fair value through profit or loss. Please refer to Note 2(f) 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 from customers” and those under “Other liabilities”.

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. The 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.

Please refer also to Note 35 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

(k) *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 Provisions, Contingent Liabilities and Contingent Assets. They form part of the disclosures in Note 38. Upon a loan draw-down by the counterparty, the amount of the loan is generally accounted for under “loans and receivables” as described in Note 2(f).

Letters of Credit

Letters of credit are recorded off-balance sheet as contingent liabilities upon issuance, and the corresponding payables / receivables to / from the beneficiary / applicant 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 was given. Subsequent to initial recognition, the Group’s liability under each guarantee is measured at the higher of the initial measurement less amortisation and the best estimate of the expenditure required to settle any financial obligation arising at the balance sheet date.

The exposure to potential losses associated with a financial guarantee is monitored periodically. When there is objective evidence indicating probability of losses occurring, a provision is recognised for the financial guarantee.

(l) *Provisions and other liabilities*

Provisions 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.

(m) *Share capital*

Ordinary shares are classified as equity. Incremental external costs directly attributable to the issuance of new ordinary shares are deducted against 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

Other Specific Topics

(n) Hedging and hedge accounting

The Group mainly uses derivative contracts 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 derivative (measured at fair value through profit or loss) and the hedged item (measured at amortised cost) exist.

For a qualifying fair value hedge, the changes in the fair value of the 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, options) that the Group transacted 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 37 for disclosures on hedging derivatives.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

(o) *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 leave as a result of services rendered by employees up to the balance sheet date.

(p) *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.

(q) *Current and deferred taxes*

Current income tax for current and prior periods is recognised at 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.

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

Deferred tax related to fair value re-measurement of available-for-sale financial 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

2 Summary of significant accounting policies (continued)

(r) 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.

(s) ***New and revised HKFRSs (which are relevant to the Group's operations) issued but effective for compliance after 2013***

The Group is in the process of making an assessment on the impact of the new/revised HKFRS and has not early adopted the following new/revised standards although early adoption in 2013 is permitted by the standard:

| | |
|---------------------|---|
| HKFRS 9 | Financial Instruments |
| HKAS 32 (Amendment) | Financial Instruments: Presentation – Offsetting financial assets and financial liabilities |

3 Critical accounting estimates and judgements in applying accounting policies

The Group makes certain assumptions and estimates in the process of applying the Group's accounting policies. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

3 Critical accounting estimates and judgements in applying accounting policies (continued)

(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, such as interest rate yield curves, option volatilities and foreign exchange rates. Valuation reserves or pricing adjustments where applicable will be used to converge to fair value.

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.

The determination of fair value is subject to the Valuation Framework approved by the Board Risk Management Committee ("BRMC") and the oversight of senior management committees. The Valuation Framework is implemented by the Group through policies and procedures approved by the committees. These policies and procedures 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. Judgement may also be applied in adjusting prices for less readily observable external parameters such as through the use of valuation reserves. Other factors such as model assumptions and market dislocations leading to market anomalies can also materially affect these estimates. Please refer to Note 35 for details about the fair value hierarchy of the Group's financial instruments measured at fair value.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

3 Critical accounting estimates and judgements in applying accounting policies (continued)

(c) 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.

(d) 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 Interest income

| | 2013 HK\$'M | 2012 HK\$'M |
|---|----------------|----------------|
| Interest income on listed investments | 357 | 423 |
| Interest income on unlisted investments | 121 | 214 |
| Other interest income | 5,832 | 5,718 |
| | <u>6,310</u> | <u>6,355</u> |

Interest income recognised on financial assets that are not at fair value through profit or loss amounted to HK\$6,257 million (2012: HK\$6,280 million).

5 Interest expense

| | 2013 HK\$'M | 2012 HK\$'M |
|--|----------------|----------------|
| Interest expense on subordinated liability (Note 32) | 118 | 59 |
| Other interest expense | 1,766 | 2,114 |
| | <u>1,884</u> | <u>2,173</u> |

Interest expense recognised on financial liabilities that are not at fair value through profit or loss amounted to HK\$1,860 million (2012: HK\$2,146 million).

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

6 Net fee and commission income

| | 2013 HK\$'M | 2012 HK\$'M |
|--|----------------|----------------|
| Fee and commission income | 1,868 | 1,658 |
| Less: Fee and commission expense | (258) | (228) |
| Net fee and commission income | <u>1,610</u> | <u>1,430</u> |
| Comprising: | | |
| – Wealth management | 567 | 458 |
| – Trade and transaction services | 464 | 412 |
| – Loan-related | 246 | 237 |
| – Cards | 224 | 208 |
| – Stock broking | 40 | 36 |
| – Investment banking | 10 | 9 |
| – Others | 59 | 70 |
| | <u>1,610</u> | <u>1,430</u> |
| Of which: | | |
| Fee and commission income arising from: | | |
| – Financial assets or financial liabilities not at fair value through profit or loss | 704 | 648 |
| – Trust or other fiduciary activities | 23 | 22 |
| Fee and commission expense arising from: | | |
| – Financial assets or financial liabilities not at fair value through profit or loss | 199 | 181 |
| Note: | | |
| (i) Trade and transaction services includes trade & remittances, guarantees and deposit-related fees | | |
| (ii) Gross cards fees are net of interchange fees paid | | |

7 Net income from financial instruments at fair value through profit or loss

| | 2013 HK\$'M | 2012 HK\$'M |
|---|----------------|----------------|
| Net trading income | | |
| – Foreign exchange | 1,483 | 965 |
| – Interest rates, credit and equities | 343 | 217 |
| | <u>1,826</u> | <u>1,182</u> |
| Net loss from financial instruments designated at fair value through profit or loss | <u>(132)</u> | <u>(42)</u> |
| | <u>1,694</u> | <u>1,140</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

8 Net income from financial investments

| | 2013 HK\$'M | 2012 HK\$'M |
|--------------------------------|----------------|----------------|
| Debt securities | | |
| – Available-for-sale | 14 | 86 |
| Equity securities | 65 | 17 |
| | <u>79</u> | <u>103</u> |
| Of which dividend income from: | | |
| – Listed investments | 2 | 1 |
| – Unlisted investments | 17 | 16 |
| | <u>19</u> | <u>17</u> |

9 Other income

| | 2013 HK\$'M | 2012 HK\$'M |
|---|----------------|----------------|
| Fair value adjustment on investment properties (Note 25(a)) | 34 | 69 |
| Net gain on disposal of properties and other fixed assets | 275 | 343 |
| Others | 44 | 81 |
| | <u>353</u> | <u>493</u> |

10 Total expenses

| | 2013 HK\$'M | 2012 HK\$'M |
|--|----------------|----------------|
| Employee benefits | | |
| – Salaries and other short term employee benefits | 1,969 | 1,897 |
| – Pensions | 112 | 113 |
| – Share-based compensation | 34 | 31 |
| Premises and equipment expenses excluding depreciation | | |
| – Rental of premises | 214 | 201 |
| – Others | 253 | 259 |
| Depreciation (Note 25(a)) | 220 | 200 |
| Auditor's remuneration | 10 | 7 |
| Computerisation expenses | 356 | 323 |
| Other operating expenses | 598 | 560 |
| | <u>3,766</u> | <u>3,591</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

11 Allowances for credit and other losses

| | 2013 HK\$'M | 2012 HK\$'M |
|---|----------------|----------------|
| Individual impairment allowances on loans and advances to customers (Note 21) | 112 | 9 |
| Collective impairment allowances on loans and advances to customers (Note 21) | 190 | 54 |
| Allowances for other credit related losses | – | (4) |
| | <u>302</u> | <u>59</u> |
| Individual impairment allowances on loans and advances to customers | | |
| – New allowances | 247 | 189 |
| – Releases | (120) | (171) |
| – Recoveries | (15) | (9) |
| | <u>112</u> | <u>9</u> |
| Collective impairment allowances on loans and advances to customers | | |
| – New allowances | 272 | 211 |
| – Releases | (60) | (136) |
| – Recoveries | (22) | (21) |
| | <u>190</u> | <u>54</u> |
| Allowances for other credit related losses | | |
| – Releases | – | (4) |
| | <u>–</u> | <u>(4)</u> |

12 Directors' emoluments

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

| | 2013 HK\$'M | 2012 HK\$'M |
|--|----------------|----------------|
| Fees (Note a) | 3 | 2 |
| Salaries, housing and other allowances and benefits (Note b) | 18 | 14 |
| Pensions | 1 | 1 |
| | <u>22</u> | <u>17</u> |

Note:

- (a) The Directors' fees are payable in 2014 to eligible persons who acted as Directors of DBS Bank (Hong Kong) Limited during the year ended 31 December 2013. Such fees are subject to the approval of the shareholders of DBS Bank (Hong Kong) Limited.
- (b) The amount included bonus accrued during the year, to be paid in the following year. Such cash bonus is subject to the approval of DBS Bank Board of Directors.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

13 Income tax expense

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

| | 2013 HK\$'M | 2012 HK\$'M |
|----------------------------------|----------------|----------------|
| Hong Kong profits tax | | |
| – Current year | 632 | 534 |
| – Overprovision in prior years | (27) | (51) |
| Overseas tax | | |
| – Current year | 6 | 8 |
| | <u>611</u> | <u>491</u> |
| Current income tax | (7) | 17 |
| Deferred income tax (Note 31(b)) | <u>604</u> | <u>508</u> |

Hong Kong profits tax has been provided at 16.5% (2012: 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 (credited) / charged to the consolidated income statement comprises the following temporary differences:*

| | 2013 HK\$'M | 2012 HK\$'M |
|-------------------------------------|----------------|----------------|
| Accelerated depreciation allowances | 7 | 3 |
| Impairment allowances | (6) | 14 |
| Share-based compensation | – | (8) |
| Accrued expenses | (8) | 8 |
| | <u>(7)</u> | <u>17</u> |

(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% (2012: 16.5%) is as follows:*

| | 2013 HK\$'M | 2012 HK\$'M |
|---|----------------|----------------|
| Profit before income tax | <u>4,128</u> | <u>3,735</u> |
| Tax calculated at tax rate of 16.5% (2012: 16.5%) | 681 | 616 |
| Effect of different tax rates in other countries | (2) | (2) |
| Income not subject to tax | (53) | (59) |
| Expenses not deductible for tax purposes | 19 | 9 |
| Overprovision in prior years | (27) | (51) |
| Others | (14) | (5) |
| | <u>604</u> | <u>508</u> |
| Income tax expense | <u>604</u> | <u>508</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

14 Profit attributable to shareholders

The profit attributable to shareholders is dealt with in the financial statements of the Bank to the extent of HK\$3,537 million (2012: HK\$3,186 million).

15 Dividend

| | 2013 HK\$'M | 2012 HK\$'M |
|--|----------------|----------------|
| Interim dividend paid of HK\$0.171 per share (2012: Nil) | <u>1,200</u> | <u>–</u> |

16 Cash and balances with banks

| | Group and Bank | |
|-----------------------------|----------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M |
| Cash in hand | 503 | 381 |
| Balances with central banks | 492 | 3,712 |
| Balances with banks | <u>4,836</u> | <u>3,225</u> |
| | <u>5,831</u> | <u>7,318</u> |

17 Placements with and advances to banks

| | Group | | Bank | |
|---------------------------------------|----------------|----------------|----------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M | 2013 HK\$'M | 2012 HK\$'M |
| Remaining maturity | | | | |
| – Within one month | 22,455 | 22,277 | 22,452 | 22,274 |
| – One year or less but over one month | 35,050 | 35,515 | 35,050 | 35,515 |
| – Over one year | – | 159 | – | 159 |
| | <u>57,505</u> | <u>57,951</u> | <u>57,502</u> | <u>57,948</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

18 Trading securities

| | Group and Bank | |
|---|-----------------------|--------------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Treasury bills | 1,652 | 4,570 |
| Certificate of deposit held | 38 | – |
| Other debt securities | 2,612 | 3,007 |
| | 4,302 | 7,577 |
| Of which: | | |
| – Listed in Hong Kong, at fair value | 1,899 | 2,016 |
| – Listed outside Hong Kong, at fair value | 371 | 469 |
| – Unlisted, at fair value | 2,032 | 5,092 |
| | 4,302 | 7,577 |
| Analysed by issuer as follows: | | |
| – Sovereigns | 3,448 | 6,911 |
| – Public sector entities | – | 3 |
| – Banks | 270 | 57 |
| – Corporates | 584 | 606 |
| | 4,302 | 7,577 |
| Analysed by rating agency designation as follows: | | |
| – AA- to AA+ | 3,641 | 6,831 |
| – A- to A+ | 186 | 155 |
| – BBB to BBB+ | 119 | 217 |
| – Unrated | 356 | 374 |
| | 4,302 | 7,577 |

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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

19 Financial investments

| | Group and Bank | |
|-----------------------|-----------------------|--------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Available-for-sale | 22,365 | 24,068 |
| Loans and receivables | 2,171 | 569 |
| | 24,536 | 24,637 |

(a) Available-for-sale

| | Group and Bank | |
|---|-----------------------|--------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Treasury bills | 9,264 | 11,377 |
| Certificate of deposit held | 1,804 | 250 |
| Other debt securities | 11,227 | 12,360 |
| Debt securities | 22,295 | 23,987 |
| Equity securities | 70 | 81 |
| | 22,365 | 24,068 |
| Debt securities | | |
| – Listed in Hong Kong, at fair value | 1,167 | 959 |
| – Listed outside Hong Kong, at fair value | 6,142 | 8,145 |
| – Unlisted, at fair value | 14,971 | 14,869 |
| – Unlisted, at cost | 15 | 14 |
| | 22,295 | 23,987 |
| Equity securities | | |
| – Listed in Hong Kong, at fair value | 40 | 49 |
| – Unlisted, at cost | 30 | 32 |
| | 70 | 81 |
| | 22,365 | 24,068 |
| Analysed by issuer as follows: | | |
| – Sovereigns | 12,658 | 15,824 |
| – Public sector entities | 650 | 856 |
| – Banks | 7,017 | 5,050 |
| – Corporates | 2,025 | 2,324 |
| – Others | 15 | 14 |
| | 22,365 | 24,068 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

19 Financial investments (continued)

(a) Available-for-sale (continued)

| | Group and Bank | |
|---|-----------------------|---------------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Analysed by rating agency designation as follows: | | |
| – AAA | 5,449 | 7,853 |
| – AA- to AA+ | 12,495 | 13,172 |
| – A- to A+ | 3,721 | 2,061 |
| – BBB to BBB+ | 60 | 479 |
| – Unrated | 570 | 422 |
| | 22,295 | 23,987 |

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 2013 and 2012, there were no impaired, overdue or rescheduled available-for-sale financial investments.

(b) Loans and receivables

| | Group and Bank | |
|---|-----------------------|------------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Debt securities | | |
| – Listed outside Hong Kong | 1,968 | 125 |
| – Unlisted | 203 | 444 |
| | 2,171 | 569 |
| Analysed by issuer as follows: | | |
| – Public sector entities | 1,847 | – |
| – Corporates | 324 | 569 |
| | 2,171 | 569 |
| Analysed by rating agency designation as follows: | | |
| – A- to A+ | – | 234 |
| – BBB to BBB+ | 324 | 335 |
| – Unrated | 1,847 | – |
| | 2,171 | 569 |

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 2013, the fair value of the above debt securities is HK\$2,218 million (2012: HK\$582 million).

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

19 Financial investments (continued)

(b) Loans and receivables (continued)

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 2013 were HK\$22 million (2012: HK\$38 million) and HK\$102,000 (2012: exchange loss of HK\$1 million) 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\$7 million (2012: HK\$28 million).

The above debt securities are neither past due nor impaired.

20 Loans and advances to customers

| | Group and Bank | |
|---------------------------------------|-----------------------|---------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Gross loans and advances to customers | 201,760 | 177,152 |
| Less: Impairment allowances | | |
| – Individually assessed (Note 21) | (793) | (899) |
| – Collectively assessed (Note 21) | (713) | (602) |
| | 200,254 | 175,651 |
| Comprising: | | |
| – Trade bills | 48,701 | 28,250 |
| – Loans | 151,553 | 147,401 |
| | 200,254 | 175,651 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

20 Loans and advances to customers (continued)

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

| | Group and Bank | |
|--|-----------------------|--------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Gross investments in finance leases and hire purchase contracts receivables: | | |
| – Not later than one year | 1,077 | 1,264 |
| – Later than one year and not later than five years | 2,411 | 2,597 |
| – Later than five years | 6,839 | 7,503 |
| | 10,327 | 11,364 |
| Unearned future finance income | (24) | (23) |
| Net investments in finance leases and hire purchase contracts receivables | 10,303 | 11,341 |
| The net investments in finance leases and hire purchase contracts receivables are analysed as follows: | | |
| – Not later than one year | 1,064 | 1,251 |
| – Later than one year and not later than five years | 2,400 | 2,587 |
| – Later than five years | 6,839 | 7,503 |
| | 10,303 | 11,341 |

The unguaranteed residual values included in the gross investments in finance leases and hire purchase contracts receivables as at 31 December 2013 and 2012 are considered not material for disclosure purposes.

The individual impairment allowances for finance leases and hire purchase contracts receivables amounted to HK\$62 million as at 31 December 2013 (2012: HK\$117 million).

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

21 Impairment allowances on loans and advances to customers

| | Group and Bank | | |
|---|------------------------------------|------------------------------------|-----------------|
| | Individually assessed HK\$'M | Collectively assessed HK\$'M | Total HK\$'M |
| 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 11) | 112 | 190 | 302 |
| Others | (6) | 66 | 60 |
| As at 31 December 2013 | <u>793</u> | <u>713</u> | <u>1,506</u> |
| As at 1 January 2012 | 1,142 | 688 | 1,830 |
| Amounts written off | (261) | (161) | (422) |
| Recoveries of loans and advances written off in previous years | 9 | 21 | 30 |
| Net charge to consolidated income statement (Note 11) | 9 | 54 | 63 |
| As at 31 December 2012 | <u>899</u> | <u>602</u> | <u>1,501</u> |

22 Other assets

| | Group and Bank | |
|------------------------------|----------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M |
| Accrued interest receivables | 457 | 478 |
| Acceptances | 2,024 | 2,242 |
| Other accounts | 1,637 | 1,434 |
| | <u>4,118</u> | <u>4,154</u> |

23 Interest in a joint venture

| | Group | | Bank | |
|-------------------------------|----------------|----------------|----------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M | 2013 HK\$'M | 2012 HK\$'M |
| Unlisted shares, at cost | | | <u>1</u> | <u>1</u> |
| Share of net assets | <u>364</u> | <u>330</u> | | |
| Amount due to a joint venture | <u>2,887</u> | <u>2,641</u> | <u>2,887</u> | <u>2,641</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

23 Interest in a joint venture (continued)

Details of the joint venture are as follows:

| <u>Name of company</u> | <u>Country of incorporation</u> | <u>Place of operation</u> | <u>Particulars of issued shares</u> | <u>Interest held</u> | <u>Principal activities</u> |
|----------------------------|---------------------------------|---------------------------|--|----------------------|-----------------------------------|
| Hutchison DBS Card Limited | British Virgin Islands | Hong Kong | 500,000 class A shares of HK\$1 each 500,000 class B shares of HK\$1 each | 50% | Provision of credit card services |

Hutchison DBS Card Limited is the only joint venture in which the Group participates, which is an unlisted corporate entity, whose quoted market price is not available.

There are no contingent liabilities relating to the Group's interest in the joint venture.

Summarised financial information of Hutchison DBS Card Limited, and reconciliation to the carrying amount, in the consolidated financial statements, are disclosed below:

| | 2013 | 2012 |
|--|----------------|---------|
| | HK\$'M | HK\$'M |
| <u>Gross amounts of Hutchison DBS Card Limited's</u> | | |
| Current assets | 2,891 | 2,646 |
| Non-current assets | 5 | 7 |
| Current liabilities | (2,160) | (1,938) |
| Non-current liabilities | (8) | (55) |
| Net assets | 728 | 660 |
| Included in the above assets and liabilities: | | |
| Cash and cash equivalents | 2,048 | 1,814 |
| Current financial liabilities | (2,160) | (1,938) |
| Non-current financial liabilities | (8) | (55) |
| Revenue | | |
| Profit from continuing operations | 68 | 74 |
| Post-tax profit or loss from discontinued operations | – | – |
| Other comprehensive income | – | – |
| Total comprehensive income | 68 | 74 |
| Dividend received from Hutchison DBS Card Limited | – | – |
| Included in the above profit: | | |
| Interest income | 63 | 57 |
| Interest expense | (63) | (57) |
| Depreciation and amortisation | (1) | (2) |
| Income tax expense | (14) | (14) |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

23 Interest in a joint venture (continued)

| | 2013 HK\$'M | 2012 HK\$'M |
|---|----------------|----------------|
| Reconciled to the Group's interest in the joint venture | | |
| Gross amounts of Hutchison DBS Card Limited's net assets | 728 | 660 |
| Group's effective interest | 50% | 50% |
| Group's share of Hutchison DBS Card Limited's net assets and carrying amount in the consolidated financial statements | <u>364</u> | <u>330</u> |

24 Subsidiaries

| | Bank | |
|---|----------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M |
| Unlisted shares, at cost after impairment loss of HK\$2 million (2012: HK\$2 million) | 39 | 145 |
| Amounts due from subsidiaries | <u>9</u> | <u>7</u> |
| | <u>48</u> | <u>152</u> |
| Amounts due to subsidiaries | <u>83</u> | <u>234</u> |

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 are listed below:

| Name of company | Place of operation and incorporation | Particulars of issued share capital | Principal activities |
|--|--------------------------------------|-------------------------------------|--|
| DBS Corporate Services (Hong Kong) Limited | Hong Kong | 500,000 shares of HK\$1 each | Provision of corporate services |
| Ting Hong Nominees Limited | Hong Kong | 10,000 shares of HK\$1 each | Provision of nominee, trustee and agency services |
| Overseas Trust Bank Nominees Limited | Hong Kong | 50,000 shares of HK\$1 each | Provision of nominee services |
| DBS Trustee H.K. (Jersey) Limited | Jersey | 100,000 shares of £1 each | Provision of trustee and trust administration services |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

25 Properties and other fixed assets

(a) Properties and other fixed assets movements

Group

| | Freehold land and building HK\$'M | Land and buildings HK\$'M | Furniture, fixtures and equipment HK\$'M | Subtotal HK\$'M | Investment properties HK\$'M | Total HK\$'M |
|---|--|---------------------------------|---|--------------------|------------------------------------|-----------------|
| 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 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

25 Properties and other fixed assets (continued)

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

Group

| | Freehold land and building HK\$'M | Land and buildings HK\$'M | Furniture, fixtures and equipment HK\$'M | Subtotal HK\$'M | Investment properties HK\$'M | Total HK\$'M |
|---|--|---------------------------------|---|--------------------|------------------------------------|-----------------|
| Cost or valuation | | | | | | |
| As at 1 January 2012 | | | | | | |
| – as previously reported | 23 | 2,707 | 1,030 | 3,760 | 407 | 4,167 |
| – on adoption of HKFRS 11 | – | – | (36) | (36) | – | (36) |
| – as restated | 23 | 2,707 | 994 | 3,724 | 407 | 4,131 |
| Additions | – | 10 | 174 | 184 | – | 184 |
| Disposals | – | (81) | (20) | (101) | – | (101) |
| Fair value adjustment | – | – | – | – | 69 | 69 |
| As at 31 December 2012 | 23 | 2,636 | 1,148 | 3,807 | 476 | 4,283 |
| Accumulated depreciation and impairment | | | | | | |
| As at 1 January 2012 | | | | | | |
| – as previously reported | 17 | 788 | 709 | 1,514 | – | 1,514 |
| – on adoption of HKFRS 11 | – | – | (34) | (34) | – | (34) |
| – as restated | 17 | 788 | 675 | 1,480 | – | 1,480 |
| Charge for the year | | | | | | |
| – as previously reported | – | 55 | 146 | 201 | – | 201 |
| – on adoption of HKFRS 11 | – | – | (1) | (1) | – | (1) |
| – as restated | – | 55 | 145 | 200 | – | 200 |
| Disposals | – | (46) | (19) | (65) | – | (65) |
| As at 31 December 2012 | 17 | 797 | 801 | 1,615 | – | 1,615 |
| Net book value | | | | | | |
| As at 31 December 2012 | 6 | 1,839 | 347 | 2,192 | 476 | 2,668 |
| The analysis of cost or valuation of the above assets as at 31 December 2012 is as follows: | | | | | | |
| At cost | 23 | 2,636 | 1,148 | 3,807 | – | 3,807 |
| At valuation | – | – | – | – | 476 | 476 |
| | 23 | 2,636 | 1,148 | 3,807 | 476 | 4,283 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

25 Properties and other fixed assets (continued)

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

Bank

| | Freehold land and building HK\$'M | Land and buildings HK\$'M | Furniture, fixtures and equipment HK\$'M | Subtotal HK\$'M | Investment properties HK\$'M | Total HK\$'M |
|---|--|---------------------------------|---|--------------------|------------------------------------|-----------------|
| 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 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

25 Properties and other fixed assets (continued)

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

Bank

| | Freehold land and building HK\$'M | Land and buildings HK\$'M | Furniture, fixtures and equipment HK\$'M | Subtotal HK\$'M | Investment properties HK\$'M | Total HK\$'M |
|---|--|---------------------------------|---|--------------------|------------------------------------|-----------------|
| Cost or valuation | | | | | | |
| As at 1 January 2012 | 23 | 2,707 | 994 | 3,724 | 407 | 4,131 |
| Additions | – | 10 | 174 | 184 | – | 184 |
| Disposals | – | (81) | (20) | (101) | – | (101) |
| Fair value adjustment | – | – | – | – | 69 | 69 |
| As at 31 December 2012 | 23 | 2,636 | 1,148 | 3,807 | 476 | 4,283 |
| Accumulated depreciation and impairment | | | | | | |
| As at 1 January 2012 | 17 | 788 | 675 | 1,480 | – | 1,480 |
| Charge for the year | – | 55 | 145 | 200 | – | 200 |
| Disposals | – | (46) | (19) | (65) | – | (65) |
| As at 31 December 2012 | 17 | 797 | 801 | 1,615 | – | 1,615 |
| Net book value | | | | | | |
| As at 31 December 2012 | 6 | 1,839 | 347 | 2,192 | 476 | 2,668 |
| The analysis of cost or valuation of the above assets as at 31 December 2012 is as follows: | | | | | | |
| At cost | 23 | 2,636 | 1,148 | 3,807 | – | 3,807 |
| At valuation | – | – | – | – | 476 | 476 |
| | 23 | 2,636 | 1,148 | 3,807 | 476 | 4,283 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

25 Properties and other fixed assets (continued)

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

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

| | Group and Bank | | | |
|------------------------------------|------------------------------|---------------------------------|------------------------------|---------------------------------|
| | 2013 | | 2012 | |
| | Land and buildings HK\$'M | Investment properties HK\$'M | Land and buildings HK\$'M | Investment properties HK\$'M |
| Freeholds | | | | |
| Held outside Hong Kong | <u>6</u> | <u>–</u> | <u>6</u> | <u>–</u> |
| Leaseholds | | | | |
| Held in Hong Kong | | | | |
| – Leases of over 50 years | 187 | 434 | 200 | 402 |
| – Leases of between 10 to 50 years | 1,559 | 76 | 1,637 | 74 |
| Held outside Hong Kong | | | | |
| – Leases of between 10 to 50 years | <u>2</u> | <u>–</u> | <u>2</u> | <u>–</u> |
| | <u>1,748</u> | <u>510</u> | <u>1,839</u> | <u>476</u> |

(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

| | Group and Bank | | |
|-----------------------|-------------------|-------------------|-------------------|
| | Level 1 HK\$'M | Level 2 HK\$'M | Level 3 HK\$'M |
| Investment properties | <u>–</u> | <u>100</u> | <u>410</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

25 Properties and other fixed assets (continued)

(b) Fair value of investment properties (continued)

(i) Fair value hierarchy (continued)

During the year ended 31 December 2013, 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 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. The fair value represents the estimated amount at which the asset should exchange on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein 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 inputs used for valuation are market yields. The movement in fair value arising from reasonably possible changes to the market yields is assessed as not significant.

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

| | Group and Bank |
|-----------------------|-----------------------|
| | HK\$'M |
| At 1 January 2013 | 381 |
| Fair value adjustment | 29 |
| At 31 December 2013 | <u>410</u> |

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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

25 Properties and other fixed assets (continued)

(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\$11 million (2012: HK\$10 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:

| | Group and Bank | |
|---|----------------|-----------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Not later than one year | 14 | 8 |
| Later than one year and not later than five years | 21 | 5 |
| | <u>35</u> | <u>13</u> |

26 Trading liabilities

| | Group and Bank | |
|-------------------------------|----------------|--------------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Short positions in securities | <u>3,122</u> | <u>6,450</u> |

27 Financial liabilities designated at fair value through profit or loss

| | Group and Bank | |
|--|----------------|--------------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Structured investment deposits (Note 28) | 8,122 | 1,771 |
| Certificates of deposit issued (Note 29) | – | 8 |
| | <u>8,122</u> | <u>1,779</u> |

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\$159 million as at 31 December 2013 (2012: HK\$9 million).

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

28 Deposits from customers

| | Group and Bank | |
|--|-----------------------|---------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Deposits from customers | | |
| – As stated in the balance sheets | 230,269 | 212,333 |
| – Structured investment deposits reported as financial liabilities designated at fair value through profit or loss (Note 27) | 8,122 | 1,771 |
| | 238,391 | 214,104 |
| Analysed by: | | |
| – Demand deposits and current accounts | 23,097 | 20,912 |
| – Savings deposits | 69,739 | 69,485 |
| – Time, call and notice deposits | 145,555 | 123,707 |
| | 238,391 | 214,104 |

29 Certificates of deposit issued

| | Group and Bank | |
|---|-----------------------|--------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Certificates of deposit issued | | |
| – As stated in the balance sheets (at amortised cost) | 7,564 | 7,283 |
| – Reported as financial liabilities designated at fair value through profit or loss (Note 27) | – | 8 |
| | 7,564 | 7,291 |

30 Other liabilities

| | Group | | Bank | |
|----------------------------------|---------------|--------|---------------|--------|
| | 2013 | 2012 | 2013 | 2012 |
| | HK\$'M | HK\$'M | HK\$'M | HK\$'M |
| Accrued interest payable | 388 | 442 | 388 | 442 |
| Acceptances | 2,024 | 2,242 | 2,024 | 2,242 |
| Other liabilities and provisions | 4,819 | 4,533 | 4,817 | 4,531 |
| | 7,231 | 7,217 | 7,229 | 7,215 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

31 Taxation

(a) Current income tax liabilities

| | Group | | Bank | |
|-------------------------------|------------------------------|----------------|------------------------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M | 2013 HK\$'M | 2012 HK\$'M |
| Hong Kong profits tax payable | 162 | 137 | 162 | 137 |
| Overseas tax payable | 6 | 6 | 6 | 6 |
| | 168 | 143 | 168 | 143 |

(b) Deferred income tax

The movements on the net deferred income tax (liabilities) / assets are as follows:

| | Group | | Bank | |
|---|------------------------------|----------------|------------------------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M | 2013 HK\$'M | 2012 HK\$'M |
| As at 1 January | | | | |
| – as previously reported | 14 | 37 | 11 | 35 |
| – adjustments due to change in accounting standard | (3) | (2) | – | – |
| As restated at 1 January | 11 | 35 | 11 | 35 |
| Deferred income tax credited / (charged) to income statement (Note 13(a)) | 7 | (17) | 7 | (17) |
| Deferred income tax credited / (charged) to equity (Note 34(b)(ii)) | 13 | (7) | 13 | (7) |
| Reversal of previously recognised deferred tax liability | 8 | – | 8 | – |
| As at 31 December | 39 | 11 | 39 | 11 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

31 Taxation (continued)

(b) Deferred income tax (continued)

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

| | Group | | Bank | |
|--------------------------------------|----------------|----------------|----------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M | 2013 HK\$'M | 2012 HK\$'M |
| Deferred tax assets | | | | |
| Impairment allowances | 93 | 87 | 93 | 87 |
| Share-based compensation | 8 | 8 | 8 | 8 |
| Accrued expenses | 8 | – | 8 | – |
| | <u>109</u> | <u>95</u> | <u>109</u> | <u>95</u> |
| Deferred tax liabilities | | | | |
| Accelerated depreciation allowances | 59 | 52 | 59 | 52 |
| Accrued expenses | – | 8 | – | 8 |
| Revaluation of financial investments | 11 | 24 | 11 | 24 |
| | <u>70</u> | <u>84</u> | <u>70</u> | <u>84</u> |

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:

| | Group | | Bank | |
|--------------------------|----------------|----------------|----------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M | 2013 HK\$'M | 2012 HK\$'M |
| Deferred tax assets | 109 | 95 | 109 | 95 |
| Deferred tax liabilities | (70) | (84) | (70) | (84) |
| | <u>39</u> | <u>11</u> | <u>39</u> | <u>11</u> |

32 Subordinated liability

The subordinated loan with principal amount of US\$540,000,000 was obtained from its intermediate holding company, DBS Bank Ltd. on 12 December 2012. The subordinated loan is Basel III-compliant and qualifies as Tier 2 capital for the purpose of computing the Bank's capital adequacy ratios.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

33 Share capital

| | Group and Bank | |
|--|------------------------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M |
| Authorised 12,000,000,000 ordinary shares of HK\$1 each | 12,000 | 12,000 |
| Issued and fully paid 7,000,000,000 ordinary shares of HK\$1 each | 7,000 | 7,000 |

34 Reserves

| | Group | | Bank | |
|---|------------------------------|----------------|------------------------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M | 2013 HK\$'M | 2012 HK\$'M |
| (a) Share premium | | | | |
| As at 1 January and 31 December | 595 | 595 | 595 | 595 |
| (b) Other reserves | | | | |
| (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 | 126 | 148 | 126 | 148 |
| Net valuation taken to equity | (36) | 69 | (36) | 69 |
| Amortisation of reserve to income statement arising from reclassification of available-for- sale financial investments to loans and receivables | 1 | 2 | 1 | 2 |
| Transferred to income statement | (50) | (86) | (50) | (86) |
| Deferred income tax credited/ (charged) to equity | 13 | (7) | 13 | (7) |
| As at 31 December | 54 | 126 | 54 | 126 |
| (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 |
| Total other reserves | 2,563 | 2,635 | 2,437 | 2,509 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

34 Reserves (continued)

| | Group | | Bank | |
|-------------------------------------|----------------|----------------|----------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M | 2013 HK\$'M | 2012 HK\$'M |
| (c) Retained earnings | | | | |
| As at 1 January | 18,785 | 15,558 | 18,499 | 15,313 |
| Profit attributable to shareholders | 3,524 | 3,227 | 3,537 | 3,186 |
| Dividend (Note 15) | (1,200) | – | (1,200) | – |
| As at 31 December | 21,109 | 18,785 | 20,836 | 18,499 |
| Total reserves | 24,267 | 22,015 | 23,868 | 21,603 |

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 2013, HK\$1,304 million (2012: HK\$1,295 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.

35 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

35 Fair value of financial instruments (continued)

(a) Valuation process (continued)

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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

35 Fair value of financial instruments (continued)

(a) Valuation process (continued)

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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

35 Fair value of financial instruments (continued)

(b) Fair value hierarchy (continued)

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

| 2013 | Group and Bank | | | |
|---|-------------------|-------------------|-------------------|-----------------|
| | Level 1 HK\$'M | Level 2 HK\$'M | Level 3 HK\$'M | Total HK\$'M |
| Assets | | | | |
| Trading securities | 4,290 | 12 | – | 4,302 |
| Derivatives | – | 9,084 | – | 9,084 |
| Available-for-sale financial investments: | | | | |
| – Debt securities | 21,541 | 739 | – | 22,280 |
| – Equity securities | 40 | – | – | 40 |
| Liabilities | | | | |
| Trading liabilities | 3,122 | – | – | 3,122 |
| Financial liabilities designated at fair value through profit or loss | – | 8,122 | – | 8,122 |
| Derivatives | – | 9,091 | – | 9,091 |
| | | | | |
| 2012 | Group and Bank | | | |
| | Level 1 HK\$'M | Level 2 HK\$'M | Level 3 HK\$'M | Total HK\$'M |
| Assets | | | | |
| Trading securities | 7,563 | 14 | – | 7,577 |
| Derivatives | – | 5,215 | – | 5,215 |
| Available-for-sale financial investments: | | | | |
| – Debt securities | 22,819 | 1,082 | 72 | 23,973 |
| – Equity securities | 49 | – | – | 49 |
| Liabilities | | | | |
| Trading liabilities | 6,450 | – | – | 6,450 |
| Financial liabilities designated at fair value through profit or loss | – | 1,771 | 8 | 1,779 |
| Derivatives | – | 5,109 | – | 5,109 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

35 Fair value of financial instruments (continued)

(b) Fair value hierarchy (continued)

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.

The following table presents the changes in Level 3 instruments for the financial year ended 31 December:

| 2013 | Group and bank | | | | | |
|--|------------------------------|-----------------------------|--|----------------------|---|------------------------------|
| | Fair value gains or losses | | | Settlement HK\$'M | Transfer out of Level 3 HK\$'M | Closing balance HK\$'M |
| | Opening balance HK\$'M | Profit or loss HK\$'M | Other comprehensive income HK\$'M | | | |
| Assets | | | | | | |
| Available-for-sale financial investments | | | | | | |
| – Debt securities | 72 | – | (2) | (70) | – | – |
| Liabilities | | | | | | |
| Financial liabilities designated at fair value through profit or loss | 8 | – | – | (8) | – | – |
| | | | | | | |
| 2012 | Group and bank | | | | | |
| | Fair value gains or losses | | | Settlement HK\$'M | Transfer out of Level 3 HK\$'M | Closing balance HK\$'M |
| | Opening balance HK\$'M | Profit or loss HK\$'M | Other comprehensive income HK\$'M | | | |
| Assets | | | | | | |
| Available-for-sale financial investments | | | | | | |
| – Debt securities | 1,251 | – | (13) | (1,045) | (121) | 72 |
| Liabilities | | | | | | |
| Financial liabilities designated at fair value through profit or loss | 160 | (2) | – | (150) | – | 8 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

35 Fair value of financial instruments (continued)

(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) Placements with and advances to 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) Financial investments – 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(b).

(iv) Deposits from banks and 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

36 Notes to consolidated cash flow statement

(a) Analysis of changes in financing activities during the year

| | Certificates of deposit issued HK\$'M | Subordinated liability HK\$'M |
|--|--|-------------------------------------|
| Balance as at 1 January 2012 | 16,543 | 4,196 |
| Cash inflow from financing activities | 11,105 | – |
| Cash outflow from financing activities | (20,493) | – |
| Revaluation | 62 | – |
| Amortisation of discount | 36 | – |
| Exchange differences and other adjustments | 38 | (10) |
| | <hr/> | <hr/> |
| Balance as at 31 December 2012 | 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 |
| | <hr/> | <hr/> |
| Balance as at 31 December 2013 | <u>7,564</u> | <u>4,187</u> |

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

| | 2013 HK\$'M | 2012 HK\$'M |
|--|----------------------|----------------------|
| Cash and balances with banks | 5,831 | 7,318 |
| Placements with and advances to banks repayable with original maturity within three months | 33,835 | 16,160 |
| Bills and notes repayable with original maturity within three months | 1,491 | 3,852 |
| | <hr/> | <hr/> |
| | <u>41,157</u> | <u>27,330</u> |

37 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

37 Derivative financial instruments and hedging activities (continued)

(a) Derivatives (continued)

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

| 2013 | Group and Bank | | | |
|--|---|--|-----------------------------------|-----------------------------------|
| | Contract/ notional amount HK\$'M | Credit risk- weighted amount HK\$'M | Positive fair values HK\$'M | Negative fair values HK\$'M |
| 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 |
| | <u>665,116</u> | <u>10,931</u> | <u>8,543</u> | <u>8,674</u> |
| Interest rate derivatives | | | | |
| – Futures | 55 | 1 | – | 1 |
| – Swaps | 28,552 | 325 | 395 | 418 |
| – Options purchased | 17 | – | 1 | – |
| – Options written | 17 | – | – | 1 |
| | <u>28,641</u> | <u>326</u> | <u>396</u> | <u>420</u> |
| Equity derivatives | <u>583</u> | <u>6</u> | <u>4</u> | <u>4</u> |
| Total derivatives held for trading | <u>694,340</u> | <u>11,263</u> | <u>8,943</u> | <u>9,098</u> |
| Derivatives designated and qualified as fair value hedges | | | | |
| Interest rate derivatives | | | | |
| – Swaps | <u>6,648</u> | <u>55</u> | <u>195</u> | <u>147</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

37 Derivative financial instruments and hedging activities (continued)

(a) Derivatives (continued)

| 2012 | Group and Bank | | | |
|--|---|--|-----------------------------------|-----------------------------------|
| | Contract/ notional amount HK\$'M | Credit risk- weighted amount HK\$'M | Positive fair values HK\$'M | Negative fair values HK\$'M |
| Derivatives held for trading | | | | |
| Foreign exchange derivatives | | | | |
| – Forwards | 204,548 | 3,102 | 2,003 | 1,999 |
| – Swaps | 122,321 | 328 | 711 | 721 |
| – Options purchased | 115,851 | 3,737 | 1,416 | – |
| – Options written | 114,678 | – | – | 1,413 |
| | <u>557,398</u> | <u>7,167</u> | <u>4,130</u> | <u>4,133</u> |
| Interest rate derivatives | | | | |
| – Futures | 54 | – | 1 | 1 |
| – Swaps | 33,815 | 521 | 706 | 735 |
| – Options purchased | 1,412 | – | 6 | – |
| – Options written | 1,412 | – | – | 6 |
| | <u>36,693</u> | <u>521</u> | <u>713</u> | <u>742</u> |
| Equity derivatives | <u>489</u> | <u>7</u> | <u>3</u> | <u>3</u> |
| Total derivatives held for trading | <u>594,580</u> | <u>7,695</u> | <u>4,846</u> | <u>4,878</u> |
| Derivatives designated and qualified as fair value hedges | | | | |
| Interest rate derivatives | | | | |
| – Swaps | <u>5,788</u> | <u>74</u> | <u>378</u> | <u>252</u> |

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\$54 million and HK\$154 million respectively (2012: HK\$9 million and HK\$21 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 2013 and 2012 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

37 Derivative financial instruments and hedging activities (continued)

(b) Hedging activities

As at 31 December 2013, the Group has interest rate swap agreements in place with a notional amount of HK\$6,648 million (2012: HK\$5,788 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 losses on the hedging instruments are HK\$93 million (2012: gains of HK\$96 million). The gains on the hedged items attributable to the hedged risk are HK\$93 million (2012: losses of HK\$95 million).

38 Contingent liabilities and commitments

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

| | Group and Bank | |
|---|----------------|----------------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Direct credit substitutes | 1,046 | 1,046 |
| Transaction-related contingencies | 1,459 | 978 |
| Trade-related contingencies | 8,616 | 9,604 |
| Other commitments with an original maturity of not more than one year | 2,082 | 4,003 |
| Other commitments with an original maturity of more than one year | 498 | 405 |
| Other commitments which are unconditionally cancellable | 135,364 | 127,892 |
| | 149,065 | 143,928 |
| Credit risk-weighted amount | 15,430 | 13,141 |

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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

39 Capital and lease commitments

(a) Capital commitments

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

| | Group and Bank | |
|---|----------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M |
| Expenditure contracted but not provided for | 84 | 73 |
| Expenditure authorised but not contracted for | 33 | 28 |
| | <u>117</u> | <u>101</u> |

(b) Lease commitments

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

| | Group and Bank | | | |
|--|----------------------|------------------|----------------------|------------------|
| | 2013 | | 2012 | |
| | Properties HK\$'M | Others HK\$'M | Properties HK\$'M | Others HK\$'M |
| Not later than one year | 211 | 12 | 190 | 8 |
| Later than one year and not later than five years | 418 | 3 | 311 | – |
| Later than five years | 43 | – | 83 | – |
| | <u>672</u> | <u>15</u> | <u>584</u> | <u>8</u> |

40 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

40 Securities pledged and transfers of financial assets (continued)

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

| | Group and Bank | |
|--|----------------|--------------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Secured liabilities – short positions in securities (Notes 26) | <u>3,122</u> | <u>6,450</u> |
| Assets pledged as security | | |
| – Treasury bills | 1,983 | 4,683 |
| – Other securities | <u>1,128</u> | <u>1,756</u> |
| | <u>3,111</u> | <u>6,439</u> |

The assets pledged as security included financial assets at fair value through profit or loss of HK\$2,391 million (2012: HK\$5,532 million).

As at 31 December 2013, the Group has HK\$5,150 million (2012: HK\$6,652 million) of transferred financial assets under securities lending transactions on the balance sheet, which are mostly classified as available-for-sale financial investments.

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

41 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 realize the asset and settle the liability simultaneously. As at 31 December 2013, no financial assets and liabilities were offset on the balance sheet (2012: 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 42 for additional disclosures. Furthermore, the Group's short position in securities was secured by the deposit of assets under sale and repurchase agreements.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

41 Offsetting financial assets and financial liabilities (continued)

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 42.

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.

2013

| Types of financial assets/liabilities | Carrying amounts on balance sheet | Financial instruments (including non-cash collateral) ^(a) | Cash collateral received / pledged | Net amounts ^(b) |
|--|-----------------------------------|--|------------------------------------|----------------------------|
| | (A) HK\$'M | (B) HK\$'M | (C) HK\$'M | (D)=(A)-(B)-(C) HK\$'M |
| Financial assets | | | | |
| Positive fair values for financial derivatives | 9,084 | 7,616 | 36 | 1,432 |
| Financial liabilities | | | | |
| Negative fair values for financial derivatives | 9,091 | 7,616 | – | 1,475 |
| Trading liabilities | 3,122 | 3,111 | – | 11 |
| Total | 12,213 | 10,727 | – | 1,486 |

2012

| Types of financial assets / liabilities | Carrying amounts on balance sheet | Financial instruments (including non-cash collateral) ^(a) | Cash collateral received / pledged | Net amounts ^(b) |
|--|-----------------------------------|--|------------------------------------|----------------------------|
| | (A) HK\$'M | (B) HK\$'M | (C) HK\$'M | (D)=(A)-(B)-(C) HK\$'M |
| Financial assets | | | | |
| Positive fair values for financial derivatives | 5,215 | 3,897 | 62 | 1,256 |
| Financial liabilities | | | | |
| Negative fair values for financial derivatives | 5,109 | 3,895 | – | 1,214 |
| Trading liabilities | 6,450 | 6,439 | – | 11 |
| Total | 11,559 | 10,334 | – | 1,225 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

41 Offsetting Financial Assets and Financial Liabilities (continued)

Notes:

- (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.

42 Financial risk management

Risk governance

Under the risk governance framework, the Board of Directors, through the Board Risk Management Committee, oversees the establishment of robust enterprise-wide risk management policies and processes. Risk appetite limits are established to guide risk-taking.

Management is accountable to the Board for ensuring the effectiveness of risk management and adherence to the risk appetite limits. To provide risk oversight, risk committees are mandated to focus on specific risk areas. These oversight committees are the Hong Kong Risk Executive Committee, the Hong Kong Credit Risk Committee, the Hong Kong Market & Liquidity Risk Committee and the Hong Kong Operational Risk Committee.

On a day-to-day basis, business units have primary responsibility for risk management. In partnership with the business units, independent control functions provide senior management with a timely assessment of key risk exposures and the associated management responses. These units also recommend risk appetite and control limits for approval in line with the risk governance framework.

(a) Credit risk

Credit risk is the potential earnings volatility caused by obligors’ inability to fulfill their contractual debt obligations. Senior management sets the overall direction and policy for managing credit risk at the Group level. In so doing, it directs the risk appetite and underwriting activities for various countries, industries and counterparties taking into account factors such as prevailing business and economic conditions. The Core Credit Risk Policy and other credit policies of DBS Bank Ltd. set forth the principles by which the Bank conducts its credit risk underwriting activities. Please refer to the Credit Risk section in the Financial Statements of DBS Bank Ltd. for more details. The Hong Kong Credit Risk Committee serves as the executive forum for overseeing various aspects of credit risk taking including framework, limits management, policies, processes, methodologies and systems.

Exposure to credit risk arises from lending, sales and trading as well as derivative activities. 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 of contingent nature. Documentary and commercial letters of credit, which are undertakings by the Group on behalf of customers, are usually collateralised by the underlying shipments of goods to which they relate and therefore exhibit different risk characteristics from direct borrowing. Commitments to extend credit include unused portions of loan commitments, guarantees or letters of credit. The majority of unused commitments are contingent upon customers observing or meeting certain credit terms and conditions.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(a) Credit risk (continued)

The credit exposure of a derivative transaction is based on the positive mark-to-market value to the Group, which in general is only a fraction of the derivative contract or notional amount used to express the volume of instruments. This credit exposure, together with potential exposures from market movements, is managed as part of the overall lending limits to the counterparties. Credit exposures on these instruments are usually unsecured, except where the Group enters into collateralised margin transactions with counterparties. The Group currently uses the current exposure method for the purpose of providing capital for such counterparty exposures. Internally, the Bank measures counterparty credit exposure using the mark-to-market exposure with an appropriate add-on for future potential exposures.

The risk management of the exposures is conducted through the credit application process which includes the assessment of repayment likelihood and the establishment of appropriate credit limits. The Group uses various internal and external risk rating systems (credit scorecards, customer risk grading and credit bureau scores) to assess the level of credit risk accepted by the Group. Business units and credit risk managers have the responsibility to ensure that credits are properly assessed and classified. Business units also assume the responsibility to ensure all crucial information is included in the application process for the purpose of assessment and approval.

The Group adopts a multi-level credit approval process requiring loan approval at successively higher levels and / or committees (as delegated) depending on, amongst other things, the size, nature of the proposed transactions and credit quality. Exposures are monitored against credit limits and other control limits (such as large exposures and concentration limits) by credit management units at the transaction and the portfolio levels, as appropriate.

In addition to the consideration of the primary recourse to the obligor for the credit risk underwritten, the employment of various credit risk mitigation techniques such as appropriate credit structuring, and posting of collateral and / or third party support as well as the use of credit derivatives to hedge or transfer risk to other third parties form an integral part of the credit risk management process. Some specific mitigation measures are outlined below:

(i) Collateral

Where possible, the Group takes collateral as a secondary recourse to the borrower. The collateral includes cash, marketable securities, properties, trade receivables, inventory, equipment and other physical and financial collateral. The Group may also take fixed and floating charges on assets of borrowers. It has put in place policies which govern the determination of eligibility of various collateral to be considered for credit risk mitigation which includes the minimum operational requirements that are required for the specific collateral to be considered as effective risk mitigations. For collateral taken in the global financial market operations, the collateral is marked to market on a mutually agreed period with the respective counterparties. For collateral taken for commercial banking, the collateral is revalued periodically ranging from daily to annually, depending on the type of collateral. In general, the Group considers the collateral it has taken as well diversified.

(ii) Master netting arrangements

The Group further manages its credit exposure by entering into master netting arrangements with counterparties where it is appropriate and feasible to do so. Master netting arrangements do not generally result in an offset of balance sheet assets and liabilities as transactions are usually accounted for individually on a gross basis. However, 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(a) Credit risk (continued)

(iii) Other risk mitigating factors

In addition, the Group may use guarantees, credit derivatives and credit insurance as credit risk mitigating factors. Whilst the Group may accept guarantees from any counterparty, it sets a threshold internally for considering guarantors to be eligible for credit risk mitigation. Credit derivatives are used as credit risk mitigating factors mainly in structured transactions and for global financial market operations.

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 38 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 shown in the disclosures required under the Banking (Disclosure) Rules.

Analysis of collateral

Whilst the Group's maximum exposure to credit risk is the carrying value of the assets or, in the case of off-balance sheet instruments, the amount guaranteed, committed, accepted or endorsed, the likely exposure may be lower due to offsetting collateral, credit guarantees and other actions taken to mitigate the Group's exposure.

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

Balances with banks, placements with and advances to banks, trading securities and financial investments
Collateral is generally not sought for these assets.

Derivative financial instruments

The Group maintains collateral agreements and enters into master netting agreements with some 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 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 typically 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 amounts shown is a sub-set of the actual collateral arrangements entered into 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(a) Credit risk (continued)

Loans and advances to customers by credit quality

| | Group and Bank | |
|-------------------------------|----------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M |
| Neither past due nor impaired | 198,265 | 173,219 |
| Past due but not impaired | 2,277 | 2,554 |
| Impaired | 1,218 | 1,379 |
| | <u>201,760</u> | <u>177,152</u> |

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

| 2013 | Group and Bank | | |
|---|----------------|------------------------------|-----------------|
| | Pass HK\$'M | Special mention HK\$'M | Total HK\$'M |
| 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 |
| | <u>190,524</u> | <u>7,741</u> | <u>198,265</u> |

| 2012 | Group and Bank | | |
|---|----------------|------------------------------|-----------------|
| | Pass HK\$'M | Special mention HK\$'M | Total HK\$'M |
| Manufacturing | 8,744 | 1,733 | 10,477 |
| Building and construction | 27,655 | 740 | 28,395 |
| Housing loans | 37,345 | 30 | 37,375 |
| General commerce | 58,081 | 5,053 | 63,134 |
| Transportation, storage and communication | 11,388 | 616 | 12,004 |
| Financial institutions, investments and holding companies | 1,444 | 13 | 1,457 |
| Professionals and private individuals (except housing loans) | 14,551 | 19 | 14,570 |
| Others | 5,574 | 233 | 5,807 |
| | <u>164,782</u> | <u>8,437</u> | <u>173,219</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(a) Credit risk (continued)

Loans and advances to customers by credit quality (continued)

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

| 2013 | Past due | | | | Total HK\$'M |
|--|--------------------------------|-------------------------|-------------------------|---------------------------------|-----------------|
| | Less than 1 month HK\$'M | 1-2 months HK\$'M | 2-3 months HK\$'M | More than 3 months HK\$'M | |
| Group and Bank | | | | | |
| 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 |

| 2012 | Past due | | | | Total HK\$'M |
|--|--------------------------------|-------------------------|-------------------------|---------------------------------|-----------------|
| | Less than 1 month HK\$'M | 1-2 months HK\$'M | 2-3 months HK\$'M | More than 3 months HK\$'M | |
| Group and Bank | | | | | |
| Manufacturing | 71 | 8 | 2 | – | 81 |
| Building and construction | 358 | 1 | 6 | – | 365 |
| Housing loans | 885 | 33 | 3 | – | 921 |
| General commerce | 481 | 49 | 9 | – | 539 |
| Transportation, storage and communication | 14 | 1 | – | – | 15 |
| Financial institutions, investments and holding companies | – | – | – | – | – |
| Professionals and private individuals (except housing loans) | 311 | 6 | – | 304 | 621 |
| Others | 11 | 1 | – | – | 12 |
| | 2,131 | 99 | 20 | 304 | 2,554 |

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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(a) Credit risk (continued)

Loans and advances to customers by credit quality (continued)

(iii) Impaired loans and advances to customers

| | Group and Bank | |
|--|-----------------------|--------------|
| | 2013 | 2012 |
| | HK\$'M | HK\$'M |
| Manufacturing | 335 | 447 |
| Building and construction | 45 | 110 |
| Housing loans | 40 | 62 |
| General commerce | 619 | 600 |
| Transportation, storage and communication | 8 | 24 |
| Financial institutions, investments and holding companies | 146 | 121 |
| Professionals and private individuals (except housing loans) | 4 | 15 |
| Others | 21 | – |
| | <u>1,218</u> | <u>1,379</u> |

| | Group and Bank | | | |
|---|-----------------------|---|------------|---|
| | 2013 | | 2012 | |
| | HK\$'M | % of gross Loans and advances to customers | HK\$'M | % of gross Loans and advances to customers |
| Gross impaired advances | 1,218 | 0.60 | 1,379 | 0.78 |
| Individual impairment allowances | (793) | | (899) | |
| | <u>425</u> | | <u>480</u> | |
| Impaired advances covered by collateral | <u>425</u> | | <u>472</u> | |

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

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(a) Credit risk (continued)

Analysis of individual impairment allowances

| | Group and Bank | | | | | As at 31 December 2013 HK\$'M |
|--|--------------------------------|-------------------------------|--|--|------------------|----------------------------------|
| | As at 1 January 2013 HK\$'M | Amounts written off HK\$'M | Recoveries of advances written off in previous years HK\$'M | Net charge to income statement HK\$'M | Others HK\$'M | |
| 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 |
| | 899 | (227) | 15 | 112 | (6) | 793 |

| | Group and Bank | | | | | As at 31 December 2012 HK\$'M |
|--|--------------------------------|-------------------------------|--|--|------------------|----------------------------------|
| | As at 1 January 2012 HK\$'M | Amounts written off HK\$'M | Recoveries of advances written off in previous years HK\$'M | Net charge to income statement HK\$'M | Others HK\$'M | |
| Manufacturing | 394 | (45) | 1 | (2) | – | 348 |
| Building and construction | 49 | (13) | – | 3 | – | 39 |
| Housing loans | – | – | 3 | (3) | – | – |
| General commerce | 427 | (66) | 2 | 2 | – | 365 |
| Transportation, storage and communication | 7 | – | – | (3) | – | 4 |
| Financial institutions, investments and holding companies | – | – | – | 102 | – | 102 |
| Professionals and private individuals (except housing loans) | 131 | (109) | – | 9 | – | 31 |
| Others | 134 | (28) | 3 | (99) | – | 10 |
| | 1,142 | (261) | 9 | 9 | – | 899 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(a) Credit risk (continued)

Analysis of individual impairment allowances

| | Group and Bank | | |
|--|--|---|--|
| | As at 1 January 2013 HK\$'M | Additions/ (Releases) HK\$'M | As at 31 December 2013 HK\$'M |
| 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 |
| | 602 | 111 | 713 |

| | Group and Bank | | |
|--|--|---|--|
| | As at 1 January 2012 HK\$'M | Additions/ (Releases) HK\$'M | As at 31 December 2012 HK\$'M |
| Manufacturing | 77 | (28) | 49 |
| Building and construction | 117 | (32) | 85 |
| Housing loans | 9 | (4) | 5 |
| General commerce | 254 | (35) | 219 |
| Transportation, storage and communication | 29 | 8 | 37 |
| Financial institutions, investments and holding companies | 7 | (3) | 4 |
| Professionals and private individuals (except housing loans) | 170 | 14 | 184 |
| Others | 25 | (6) | 19 |
| | 688 | (86) | 602 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(a) Credit risk (continued)

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.

| | Loans HK\$'M | Trade Finance (including trade bills) HK\$'M | Total HK\$'M |
|-------------------------------|-----------------|--|-----------------|
| As at 31 December 2013 | | | |
| Hong Kong | 118,996 | 19,861 | 138,857 |
| Mainland China | 7,271 | 47,870 | 55,141 |
| Others | 5,584 | 2,178 | 7,762 |
| | <u>131,851</u> | <u>69,909</u> | <u>201,760</u> |
| As at 31 December 2012 | | | |
| Hong Kong | 119,871 | 17,123 | 136,994 |
| Mainland China | 6,679 | 27,044 | 33,723 |
| Others | 4,276 | 2,159 | 6,435 |
| | <u>130,826</u> | <u>46,326</u> | <u>177,152</u> |

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:

| | Impaired advances to customers HK\$'M | Individual impairment allowances HK\$'M | Collective impairment allowances HK\$'M |
|-------------------------------|--|--|--|
| As at 31 December 2013 | | | |
| Hong Kong | 1,036 | 609 | 578 |
| Mainland China | 130 | 142 | 32 |
| As at 31 December 2012 | | | |
| Hong Kong | 1,145 | 710 | 553 |
| Mainland China | 144 | 137 | 30 |

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(b) Market risk

Market risk affects the economic values of financial instruments held by the Group, and arises from changes in interest rate yields, foreign exchange rates, equity prices, credit spreads and changes in the correlations and volatilities of these risk factors.

The Group manages market risk in the course of market-making, structuring and packaging products for investors and clients, as well as to benefit from market opportunities. The Board Risk Management Committee establishes the Group's risk appetite for market risk. The Market and Liquidity Risk Committee, which reports to the Risk Executive Committee, oversees the Group's market risk management infrastructure, sets market risk control limits and provides enterprise-wide oversight of all market risks and their management.

The independent market risk management function, which is supported by DBS Bank Ltd. in terms of model analytics, risk architecture and report production, reports to the Senior Risk Executive and is responsible for day-to-day market risk monitoring and analysis.

The Group's market risk framework sets out the overall approach towards market risk management and this is supplemented with policies which articulate the standards relating to limit setting, independent valuation model validation, risk measuring, risk monitoring and valuation.

The Group's market risk methodology uses a historical simulation approach to forecast the Group's potential loss distribution arising from market risk in the trading and banking books. The principal market risk appetite measures for market risk used by the Group are Tail Value-at-Risk (TVaR) and stress loss. The Group also calculates Value-at-Risk (VaR) at 99% confidence level using the same potential loss distribution and holding period used for TVaR.

TVaR capture losses beyond the chosen confidence interval from the potential loss distribution and hence provides additional information to VaR. TVaR is calculated using a one-day time horizon and a 95% confidence interval. The risk factor scenarios are aligned to parameters and market data that are used for valuation. The scenarios are maintained in the risk system and are used to compute TVaR (in Singaporean Dollars "SG\$") daily at Group level and for each business unit. The TVaR is supplemented by risk control measures, such as sensitivities to risk factors as well as loss triggers for management action.

VaR on the other hand facilitates backtesting and comparability at the industry level. Regular backtesting of daily profit and loss against the VaR forecast is carried out for the trading book as a whole.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(b) Market risk (continued)

(i) Daily TVaR for trading book market risk

Average TVaR for trading book market risk for 2013 was S\$0.6 million compared with S\$1.0 million for 2012. The decrease in the average TVaR for trading book market risk was driven by a decrease in interest rate exposures. The Group's interest rates trading business was the major contributor of the trading book's TVaR and its significant exposures were in CNY and USD in 2013.

The following table shows the period-end, average, high and low daily TVaR (at a 95% confidence level over a one-day holding period) for the trading book market risk.

| Group SG\$'million | As at 31 December 2013 | 1 January 2013 to 31 December 2013 * | | |
|-----------------------|---------------------------|--------------------------------------|------------|------------|
| | | Average | High | Low |
| Total | <u>0.7</u> | <u>0.6</u> | <u>1.1</u> | <u>0.3</u> |

| Group SG\$'million | As at 31 December 2012 | 1 January 2012 to 31 December 2012 * | | |
|-----------------------|---------------------------|--------------------------------------|------------|------------|
| | | Average | High | Low |
| Total | <u>0.4</u> | <u>1.0</u> | <u>1.8</u> | <u>0.4</u> |

* Using a 1-year historical observation period

Although both VaR and TVaR provide valuable insights, no statistical measure can capture all aspects of market risk. Historical simulation VaR and TVaR are based on the assumption that historical rate and price movements are good predictors of the future. To supplement VaR and TVaR, regular stress testing is carried out using a combination of historical and hypothetical scenarios, to monitor the Group's vulnerability to unexpected and extreme shocks.

The trading book definition is based on the firm's investment intent. Issuer risk in trading book is governed by credit spread sensitivity of one basis point shift (CSPV01) and Jump-to-Default measurements.

The Group also manages 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. To optimise its income and balance sheet management, the Group deploys funds in approved debt securities or in the interbank money market.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(b) Market risk (continued)

(ii) Monthly total TVaR for market risk

The Group has a comprehensive risk framework for the identification, measuring, monitoring and reporting of all types of market risk, including interest rate risk in the banking book (except immaterial equity risk in the banking book), in line with its internal capital adequacy assessment process. The Group level monthly total TVaR associated with this framework is tabulated below, showing the period-end, average, high and low TVaR (at a 95% confidence level over a one-day holding period).

| Group SG\$'million | As at 31 December 2013 | 1 January 2013 to 31 December 2013 | | |
|-----------------------|---------------------------|------------------------------------|------------|------------|
| | | Average | High | Low |
| Total | <u>5.5</u> | <u>3.3</u> | <u>5.5</u> | <u>2.1</u> |
| | As at 31 December 2012 | 1 January 2012 to 31 December 2012 | | |
| | | Average | High | Low |
| Total | <u>2.2</u> | <u>4.2</u> | <u>6.9</u> | <u>2.2</u> |

Main risk drivers for the banking book are HKD and USD interest rate positions. The economic value impact of changes in interest rates is simulated under various assumptions for the banking book. The simulated economic value changes are negative HK\$422 million and HK\$838 million (2012: negative \$341 million and \$683 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 risk in the banking book

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 2013 and 2012 were not material and were held for long term investment purpose. They were reported as financial investments in Note 19 to the financial statements and are subject to the accounting and valuation policies set out in Notes 2(f) and 2(h) to the financial statements.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(c) Liquidity risk

Funding liquidity risk (or liquidity risk) is the risk arising from an inability to meet obligations when they come due. The Group's liquidity obligations arise from 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 honored under normal as well as adverse circumstances.

The Board Risk Management Committee is responsible for approving the principles and standards under the Group's liquidity risk management framework, as well as defining the Group's tolerance towards liquidity risk. The Risk Executive Committee, which reports to the Board Risk Management Committee and is supported by the Market & Liquidity Risk Committee, provides liquidity risk control across the Group and its management. On a business and tactical level, the Asset and Liability Committee is the primary committee responsible for ensuring the group-wide management of liquidity is in accordance with the liquidity risk management framework and policies.

In practice, the Group employs a range of strategies 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, maintaining diversified sources of liquidity, and having robust internal control processes. 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.

The primary measure used to manage liquidity within the appetite defined by the Board Risk Management Committee is the 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 appetite statement, core parameters underpinning the performance of the analysis, such as the types of scenarios, the survival period and the minimum level of liquidity reserves, 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 internal risk committees for deliberation and actions.

To complement the maturity mismatch analysis in its objective to manage liquidity within the risk appetite statement, liquidity risk control measures, such as liquidity-related ratios and balance sheet analysis, are performed for more granular monitoring and control over the liquidity profile of the Group and across locations.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(c) Liquidity risk (continued)

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:

| 2013 | Group | | | | | | | Total HK\$'M |
|---|----------------------------------|--------------------------------|--|---|--|----------------------------|-------------------|-----------------|
| | Repayable on demand HK\$'M | Less than 1 month HK\$'M | 3 months or less but over 1 month HK\$'M | 1 year or less but over 3 months HK\$'M | 5 years or less but over 1 year HK\$'M | After 5 years HK\$'M | Undated HK\$'M | |
| Assets | | | | | | | | |
| - Cash and balances with banks | 5,831 | - | - | - | - | - | - | 5,831 |
| - Placements with and advances to banks | - | 22,455 | 18,334 | 16,716 | - | - | - | 57,505 |
| - Trading securities | - | 158 | 1,245 | 1,011 | 1,796 | 92 | - | 4,302 |
| - Financial investments | | | | | | | | |
| - Debt securities classified as available-for-sale | - | 3,270 | 7,790 | 5,431 | 4,658 | 1,131 | 15 | 22,295 |
| - 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 |
| Total assets | 14,242 | 65,323 | 66,863 | 71,178 | 40,003 | 45,170 | 5,880 | 308,659 |
| Liabilities | | | | | | | | |
| - Deposits and balances from banks | 875 | 3,658 | 71 | 147 | - | - | - | 4,751 |
| - Trading liabilities | - | 686 | 1,350 | 377 | 688 | 21 | - | 3,122 |
| - Financial liabilities designated at fair value through profit or loss | - | 1,160 | 1,419 | 5,540 | 3 | - | - | 8,122 |
| - Deposits from customers | 92,934 | 60,976 | 53,170 | 23,062 | 127 | - | - | 230,269 |
| - Certificates of deposit issued | - | 180 | - | 3,193 | 2,986 | 1,205 | - | 7,564 |
| - Subordinated liability | - | - | - | - | - | 4,187 | - | 4,187 |
| - Others | 920 | 14,216 | 391 | 903 | 194 | 20 | 2,733 | 19,377 |
| Total liabilities | 94,729 | 80,876 | 56,401 | 33,222 | 3,998 | 5,433 | 2,733 | 277,392 |
| Of which: | | | | | | | | |
| Certificates of deposit held included in: | | | | | | | | |
| - Trading securities | - | - | - | 38 | - | - | - | 38 |
| - Financial investments as available-for-sale | - | - | 388 | 1,416 | - | - | - | 1,804 |
| | - | - | 388 | 1,454 | - | - | - | 1,842 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(c) Liquidity risk (continued)

| 2012 | Group | | | | | | | Total HK\$'M |
|--|----------------------------------|--------------------------------|--|---|--|----------------------------|-------------------|-----------------|
| | Repayable on demand HK\$'M | Less than 1 month HK\$'M | 3 months or less but over 1 month HK\$'M | 1 year or less but over 3 months HK\$'M | 5 years or less but over 1 year HK\$'M | After 5 years HK\$'M | Undated HK\$'M | |
| Assets | | | | | | | | |
| – Cash and balances with banks | 7,318 | – | – | – | – | – | – | 7,318 |
| – Placements with and advances to banks | – | 22,277 | 29,361 | 6,154 | 159 | – | – | 57,951 |
| – Trading securities | – | 2,693 | 1,328 | 1,309 | 2,217 | 30 | – | 7,577 |
| – Financial investments | | | | | | | | |
| – Debt securities classified as available-for-sale | – | 2,945 | 7,213 | 8,294 | 4,841 | 680 | 14 | 23,987 |
| – Debt securities classified as loans and receivables | – | – | 234 | – | 335 | – | – | 569 |
| – Equity securities | – | – | – | – | – | – | 81 | 81 |
| – Loans and advances to customers | 7,553 | 20,471 | 23,882 | 40,965 | 33,597 | 48,024 | 1,159 | 175,651 |
| – Others | 119 | 5,317 | 2,307 | 135 | 66 | 9 | 4,425 | 12,378 |
| Total assets | 14,990 | 53,703 | 64,325 | 56,857 | 41,215 | 48,743 | 5,679 | 285,512 |
| Liabilities | | | | | | | | |
| – Deposits and balances from banks | 1,122 | 3,269 | 1,751 | 3,055 | 159 | – | – | 9,356 |
| – Trading liabilities | – | 2,156 | 1,602 | 1,547 | 1,126 | 19 | – | 6,450 |
| – Financial liabilities designated at fair value through profit or loss | – | 193 | 774 | 809 | 3 | – | – | 1,779 |
| – Deposits from customers | 90,466 | 58,016 | 42,617 | 21,233 | 1 | – | – | 212,333 |
| – Certificates of deposit issued | – | 1,007 | – | 574 | 3,244 | 2,458 | – | 7,283 |
| – Subordinated liability | – | – | – | – | – | 4,186 | – | 4,186 |
| – Others | 684 | 10,114 | 569 | 857 | 197 | 28 | 2,661 | 15,110 |
| Total liabilities | 92,272 | 74,755 | 47,313 | 28,075 | 4,730 | 6,691 | 2,661 | 256,497 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(c) Liquidity risk (continued)

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:

| 2013* | Group | | | | | Total HK\$'M |
|--|----------------------------------|-------------------------------|---|--|----------------------------|-----------------|
| | Repayable on demand HK\$'M | 3 months or less HK\$'M | 1 year or less but over 3 months HK\$'M | 5 years or less but over 1 year HK\$'M | After 5 years HK\$'M | |
| Financial liabilities | | | | | | |
| – Deposits and balances from banks | 875 | 3,730 | 148 | – | – | 4,753 |
| – Trading liabilities | – | 2,037 | 393 | 682 | 22 | 3,134 |
| – Financial liabilities designated at fair value through profit or loss | – | 2,562 | 5,526 | 20 | – | 8,108 |
| – Deposits from customers | 92,934 | 114,576 | 23,390 | 141 | – | 231,041 |
| – Certificates of deposit issued | – | 212 | 3,320 | 3,324 | 1,186 | 8,042 |
| – Subordinated liability | – | 29 | 90 | 776 | 5,345 | 6,240 |
| – Others | 920 | 10,025 | 1,207 | 1,342 | 445 | 13,939 |
| | <u>94,729</u> | <u>133,171</u> | <u>34,074</u> | <u>6,285</u> | <u>6,998</u> | <u>275,257</u> |
| Derivatives settled on a gross basis | | | | | | |
| – Foreign exchange contracts | | | | | | |
| – inflow | – | 127,743 | 131,177 | 42,907 | – | 301,827 |
| – outflow | – | 127,778 | 131,148 | 42,920 | – | 301,846 |
| Contingent liabilities and commitments | | | | | | |
| – Contingent liabilities | – | 11,121 | – | – | – | 11,121 |
| – Commitments | 71,954 | 65,990 | – | – | – | 137,944 |
| | <u>71,954</u> | <u>77,111</u> | <u>–</u> | <u>–</u> | <u>–</u> | <u>149,065</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(c) Liquidity risk (continued)

| 2012* | Group | | | | | |
|--|----------------------------------|-------------------------------|---|--|----------------------------|-----------------|
| | Repayable on demand HK\$'M | 3 months or less HK\$'M | 1 year or less but over 3 months HK\$'M | 5 years or less but over 1 year HK\$'M | After 5 years HK\$'M | Total HK\$'M |
| Financial liabilities | | | | | | |
| – Deposits and balances from banks | 1,122 | 5,059 | 3,117 | 160 | – | 9,458 |
| – Trading liabilities | – | 3,764 | 1,570 | 1,108 | 18 | 6,460 |
| – Financial liabilities designated at fair value through profit or loss | – | 966 | 805 | 3 | – | 1,774 |
| – Deposits from customers | 90,468 | 100,958 | 21,467 | 1 | – | 212,894 |
| – Certificates of deposit issued | – | 1,062 | 696 | 3,676 | 2,312 | 7,746 |
| – Subordinated liability | – | 29 | 91 | 584 | 5,300 | 6,004 |
| – Others | 682 | 8,458 | 1,261 | 1,170 | 328 | 11,899 |
| | <u>92,272</u> | <u>120,296</u> | <u>29,007</u> | <u>6,702</u> | <u>7,958</u> | <u>256,235</u> |
| Derivatives settled on a gross basis | | | | | | |
| – Foreign exchange contracts | | | | | | |
| – inflow | – | 107,753 | 54,544 | 30,699 | – | 192,996 |
| – outflow | – | 107,639 | 54,489 | 30,719 | – | 192,847 |
| Contingent liabilities and commitments | | | | | | |
| – Contingent liabilities | – | 11,628 | – | – | – | 11,628 |
| – Commitments | 75,104 | 57,196 | – | – | – | 132,300 |
| | <u>75,104</u> | <u>68,824</u> | <u>–</u> | <u>–</u> | <u>–</u> | <u>143,928</u> |

* 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.

Customer assets and liabilities (including non-maturing savings / current deposits) on the table above are represented on a contractual basis or in a period when they can legally be withdrawn. On a behavioural basis for liquidity risk analysis, the assets and liabilities cash flows may differ from contractual basis.

For the purpose of liquidity risk management, the Group actively monitors and manages its liquidity positions within a 1-year period. A conservative view is adopted in the behavioural profiling of assets, liabilities and off-balance sheet commitments that have exhibited cash flow patterns that differ significantly from the actual contractual maturity profile. Examples where behavioural profiling is applied include the profiling of run-offs on deposits and the rate of draw downs on committed facilities. Assumptions made in behavioural profiling are subject to the governance of the Group internal risk committees.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(c) Liquidity risk (continued)

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:

| HK\$'M* | Less than 7 days | 7 days to 1 month | 1 to 3 months | 3 to 12 months |
|------------------------|---------------------|----------------------|------------------|-------------------|
| 2013 | | | | |
| Net liquidity mismatch | 20,928 | 7,312 | 40,573 | 39,610 |
| Cumulative mismatch | 20,928 | 28,240 | 68,813 | 108,423 |
| 2012 | | | | |
| Net liquidity mismatch | 17,331 | 9,401 | 38,163 | 13,328 |
| Cumulative mismatch | 17,331 | 26,732 | 64,895 | 78,223 |

* Positive indicates a position of liquidity surplus. Negative indicates a liquidity shortfall that has to be funded.

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 comparable across 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. An Operational Risk Management Framework, approved by the Board Risk Management Committee, has been developed with the objective to ensure that operational risks are properly identified, monitored, managed and reported in a structured, systematic and consistent manner.

To manage and control operational risk, the Framework encompasses various tools including, control self-assessment, risk event management and key risk indicator monitoring. Risk events, including any significant incidents that may impact the Group's reputation, are required to be reported based on certain thresholds established. Key risk indicators with pre-defined escalation triggers are employed to facilitate risk monitoring in a forward looking manner.

A key component of the Framework is a set of Core Operational Risk Standards which provides guidance on the baseline controls to ensure a controlled and sound operating environment. Each new product or service introduced or outsourcing initiative is subject to a risk review and sign-off process where relevant risks are identified and assessed by departments independent of the risk-taking unit proposing the product or service. Variations of existing products or services and outsourcing initiatives, are also subject to a similar process. Major operational risk mitigation programmes include Business Continuity Management and Global Insurance Programme. On an annual basis, the Chief Executive Officer provides an attestation to the Board of Directors on the state of business continuity management, including any residual risks.

The Hong Kong Operational Risk Committee oversees the operational risk management infrastructure, including the Framework, policies, processes, information, methodologies and systems. The Committee also performs regular review of the operational risk profiles and approves corporate operational risk policies.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

42 Financial risk management (continued)

(e) Capital management

The Bank'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 Hong Kong Monetary Authority throughout 2013 and 2012.

43 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

| | DBS Bank Ltd. | | Fellow subsidiaries | |
|---|----------------|----------------|---------------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M | 2013 HK\$'M | 2012 HK\$'M |
| Interest income | 400 | 347 | – | – |
| Interest expense | (229) | (333) | (2) | (2) |
| Net fee and commission income / (expense) | 2 | 13 | (8) | (7) |
| Net income from financial instruments at fair value through profit or loss | 1,130 | 967 | – | – |
| Other income | 25 | 24 | 6 | 6 |
| Total expenses (charged) / recovered | (57) | (55) | 22 | 22 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

43 Material related party transactions (continued)

(a) Holding companies and fellow subsidiaries (continued)

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

| | Group | | Bank | |
|---------------------------------------|----------------|----------------|----------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M | 2013 HK\$'M | 2012 HK\$'M |
| Asset | | | | |
| Cash and balances with banks | 71 | 46 | 71 | 46 |
| Placements with and advances to banks | 49,770 | 45,730 | 49,767 | 45,727 |
| Derivatives | 4,617 | 2,398 | 4,617 | 2,398 |
| Other assets | 243 | 222 | 243 | 222 |
| | <u>54,701</u> | <u>48,396</u> | <u>54,698</u> | <u>48,393</u> |
| Liabilities | | | | |
| Deposits and balances from banks | 2,352 | 5,053 | 2,352 | 5,053 |
| Derivatives | 5,116 | 3,144 | 5,116 | 3,144 |
| Subordinated liability | 4,187 | 4,186 | 4,187 | 4,186 |
| Other liabilities | 140 | 123 | 140 | 123 |
| | <u>11,795</u> | <u>12,506</u> | <u>11,795</u> | <u>12,506</u> |

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

| | Group and Bank | |
|-------------------------|----------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M |
| Exchange rate contracts | 378,986 | 310,067 |
| Interest rate contracts | 20,149 | 25,211 |
| Equity contracts | 269 | 214 |
| | <u>399,404</u> | <u>335,492</u> |

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

As at 31 December 2013, total contingent liabilities and commitments with DBS Bank Ltd. and fellow subsidiaries amounted to HK\$587 million (2012: HK\$3,485 million).

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

43 Material related party transactions (continued)

(a) Holding companies and fellow subsidiaries (continued)

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

| | Group and Bank | |
|-------------------------|------------------------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M |
| Deposits from customers | 315 | 316 |

- (vi) Balances with fellow subsidiaries as at 31 December

| | Group | | Bank | |
|----------------------------------|------------------------------|----------------|------------------------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M | 2013 HK\$'M | 2012 HK\$'M |
| Other assets | 95 | 186 | 95 | 186 |
| Deposits and balances from banks | 139 | 219 | 139 | 219 |
| Deposits from customers | 934 | 868 | 934 | 868 |
| Other liabilities | 70 | 93 | 70 | 93 |
| | 1,143 | 1,180 | 1,143 | 1,180 |

(b) Joint venture

Under the Joint Venture Agreement (the "Agreement") between the Bank, Whampoa Limited and Hutchison DBS Card Limited ("HDCL"), the Bank issues and services credit cards under the Compass brand. The Compass credit card receivables are included under "Loans and advances to customers" in the Bank's balance sheet. Under the Agreement, all the income, expenses and loan impairment allowances on the Compass cards are recorded in the books of HDCL.

As at 31 December 2013, the amount due from the Bank to the joint venture is HK\$2,887 million (2012: HK\$2,641 million), of which HK\$1,930 million (2012: HK\$1,720 million) is interest-bearing time deposit and the remaining balance is interest free and repayable on demand. Interest expense on the time deposit for the year ended 31 December 2013 paid and payable to HDCL is HK\$63 million (2012: HK\$57 million). Gross service fee income from HDCL to the Bank for the year ended 31 December 2013 is HK\$95 million (2012: HK\$95 million).

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

43 Material related party transactions (continued)

(c) Directors and key management personnel

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

During the year, the Group has 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 (2012: Nil) provided to one of the directors.

- (ii) Compensation of directors and key management personnel

| | Group and Bank | |
|--|----------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M |
| Salaries, other short term employee benefits and directors' fee (Note) | 78 | 72 |
| Pension | 3 | 3 |
| Share-based compensation | 18 | 16 |
| | 99 | 91 |

Note: 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

43 Material related party transactions (continued)

(d) 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 |
|---|-------------|
| DBSH Share Plan (Share Plan) <ul style="list-style-type: none">• Share Plan is granted to Group executives as determined by the CMDC appointed to administer the Share Plan from time to time• Participants are awarded DBSH shares, their equivalent cash value or a combination• Awards consists of Main award and Retention award (20% of main awards)• 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.• The fair value of the shares awarded are computed based on the market price of the ordinary shares at the time of the award | 43(d)(i) |
| DBSH Employee Share Plan (ESP) <ul style="list-style-type: none">• 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.• The awards structure and vesting conditions are similar to DBSH Share Plan• There are no additional retention awards for shares granted to top performers and key employees.• 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. | 43(d)(i) |
| DBSH Share Option Plan (Option Plan) <ul style="list-style-type: none">• The Option Plan expired on 19 June 2009. Its termination does not affect the rights of holders of outstanding existing options• 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)• 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• Vest over a period in accordance to vesting schedule• Exercisable after the first anniversary of the date of the grant up to the date of expiration of the options• The fair value of options granted is determined using the Binomial model | 43(d)(ii) |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

43 Material related party transactions (continued)

(d) Share based compensation plans (continued)

(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 | 2013 | | 2012 | |
|---|-------------------|------------------|------------|-----------|
| | Share Plan | ESP | Share Plan | ESP |
| Balance at 1 January | 810,576 | 341,310 | 750,225 | 278,600 |
| Granted | 428,373 | 162,800 | 446,079 | 147,062 |
| Transfer | 28,764 | 12,412 | – | – |
| Vested | (153,052) | (79,629) | (278,717) | (65,850) |
| Forfeited | (29,093) | (53,256) | (107,011) | (18,502) |
| Balance at 31 December | 1,085,568 | 383,637 | 810,576 | 341,310 |
| Weighted average fair value of the shares granted during the year | SG\$15.19 | SG\$15.07 | SG\$14.10 | SG\$14.10 |

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

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

43 Material related party transactions (continued)

(d) Share based compensation plans (continued)

(ii) DBSH Share Option Plan

The following table sets out the fair value of the outstanding time-based awards and the movement during the year.

| | 2013 | | 2012 | |
|--|--|--------------------------------------|--|--------------------------------------|
| | 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 | 518,949 | 13.71 | 809,895 | 13.44 |
| Movements during the year: | | | | |
| – Exercised | (256,463) | 12.93 | (480,644) | 12.81 |
| – Transfer | (18,934) | 14.87 | 198,447 | 12.66 |
| – Forfeited / Expired | (24,465) | 11.20 | (8,749) | 14.90 |
| Balance as at 31 December | <u>219,087</u> | <u>14.81</u> | <u>518,949</u> | <u>13.71</u> |
| Additional information: | | | | |
| Weighted average remaining contractual life of options outstanding as at 31 December | 0.39 years | | 1.1 years | |
| Range of exercise price of options outstanding as at 31 December | SG\$10.40- SG\$15.07 | | SG\$10.40- SG\$15.07 | |

In 2013, 256,463 options (2012: 480,644) were exercised at their contractual exercise prices. During the year, the weighted average market price of DBSH shares was SG\$15.53 (2012: SG\$14.14).

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(Expressed in millions of Hong Kong dollars)

43 Material related party transactions (continued)

(d) Share based compensation plans (continued)

(ii) DBSH Share Option Plan (continued)

| DBSH options | Number of | During the year | | | Number of | Exercise price per share | Expiry date |
|--------------|--------------------------|-----------------|------------------|--------------------------|------------------|--------------------------|-------------|
| | unissued ordinary shares | | | unissued ordinary shares | | | |
| | 1 January 2013 | Transfer | Exercised | Forfeited/ Expired | 31 December 2013 | SGD | |
| Feb 2003 | 129,038 | - | (109,041) | (19,997) | - | 10.40 | 24 Feb 2013 |
| Mar 2004 | 299,601 | (11,407) | (115,572) | (3,881) | 168,741 | 14.73 | 02 Mar 2014 |
| Mar 2005 | 90,310 | (7,527) | (31,850) | (587) | 50,346 | 15.07 | 01 Mar 2015 |
| | <u>518,949</u> | <u>(18,934)</u> | <u>(256,463)</u> | <u>(24,465)</u> | <u>219,087</u> | | |

44 Loans to officers

Particulars of loans made to officers and disclosed pursuant to Section 161B of the Hong Kong Companies Ordinance are as follows:

| | Balance outstanding as at 31 December | | Maximum balance during the year | |
|---|---------------------------------------|----------------|---------------------------------|----------------|
| | 2013 HK\$'M | 2012 HK\$'M | 2013 HK\$'M | 2012 HK\$'M |
| Aggregate amount outstanding in respect of principal and interest | <u>450</u> | <u>-</u> | <u>493</u> | <u>-</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION

(Expressed in millions of Hong Kong dollars)

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

1 Capital adequacy

The capital adequacy ratios as at 31 December 2013 and 31 December 2012 were compiled in accordance with the Banking (Capital) Rules issued by the Hong Kong Monetary Authority.

| | As at 31 December 2013 | As at 31 December 2012 |
|-------------------------|---------------------------------------|------------------------------|
| Capital Adequacy Ratios | | |
| Common Equity Tier 1 | 13.9% | NA |
| Tier 1 | 13.9% | 14.3% |
| Total | 16.1% | 16.7% |

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.

HKMA implemented Basel III capital adequacy requirements in the Banking (Capital) Rules with effect from 1 January 2013. Capital adequacy disclosures related to dates prior to 1 January 2013 were calculated in accordance with the then prevailing capital adequacy requirements and are thus not directly comparable to those pertaining to dates from 1 January 2013.

Additional information

Capital disclosures as required by section 45 of the Banking (Disclosure) Rules as amended by the Banking (Disclosure) (Amendment) Rules 2013 is available on our website www.dbs.com.hk.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

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 are 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.(Jersey) Limited | Provision of trustee and trust administration services | 7 | 6 |
| DBS Trustee H.K.(New Zealand) Limited | Provision of trustee and trust administration services | 1 | – |
| Hutchison DBS Card Limited | Provision of credit card services | 2,896 | 728 |
| DBS Corporate Services (Hong Kong) Limited | Provision of corporate services | 6 | 5 |
| DHJ Management Limited | Provision of corporate services | – | – |
| DNZ Limited | Provision of corporate services | – | – |
| Kingly Management Limited | Provision of corporate services | – | – |
| JT Administration Limited | Provision of corporate services | – | – |
| Kenson Asia Limited | Provision of corporate services | – | – |
| Market Success Limited | Provision of corporate services | – | – |
| Worldson Services Limited | Provision of corporate services | – | – |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

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:

| | 2013 HK\$'M | 2012 HK\$'M |
|---|----------------|----------------|
| Credit risk: | | |
| IRB approach | | |
| Retail exposures: | | |
| Residential mortgages | 330 | 364 |
| Qualifying revolving retail exposures | 1,380 | 1,297 |
| Small business retail exposures | – | – |
| Other retail exposures to individuals | 692 | 610 |
| Wholesale exposures: | | |
| Sovereign exposures | 217 | 285 |
| Bank exposures | 3,126 | 2,419 |
| Corporate exposures | 7,660 | 7,136 |
| Other exposures | 356 | 354 |
| | <u>13,761</u> | <u>12,465</u> |
| Standardised approach | | |
| On-balance sheet | | |
| Public sector entity exposures | 8 | 11 |
| Bank exposures | 2 | 4 |
| Corporate exposures | 624 | 572 |
| Regulatory retail exposures | 63 | 73 |
| Other exposures which are not past due exposures | 395 | 352 |
| Past due exposures | 26 | 28 |
| Off-balance sheet | | |
| Off-balance sheet exposures other than over-the-counter derivative transactions | 31 | 29 |
| Over-the-counter derivative transactions | 7 | 6 |
| | <u>1,156</u> | <u>1,075</u> |
| Credit valuation adjustment | 343 | – |
| Total capital requirements for credit risk | <u>15,260</u> | <u>13,540</u> |
| Market risk: | | |
| Standardised approach | | |
| Interest rate exposures | 272 | 161 |
| Foreign exchange exposures | 102 | 132 |
| Total capital requirements for market risk | <u>374</u> | <u>293</u> |
| Total capital requirements for operational risk | <u>1,015</u> | <u>928</u> |
| Total capital requirements before deductions | <u>16,649</u> | <u>14,761</u> |
| Deductions | <u>(21)</u> | <u>–</u> |
| Total capital requirements after deductions | <u>16,628</u> | <u>14,761</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

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 the Hong Kong Credit Risk Committee of the Bank and the Group Credit Risk Committee of DBSH. The models have also been approved by the Board Risk Management Committee of the Bank and the 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

4 Credit risk assessed using IRB approach (continued)

(a) Internal rating system and process (continued)

Definitions of variables (continued)

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, 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 Hong Kong Monetary Authority ("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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

4 Credit risk assessed using IRB approach (continued)

(a) Internal rating system and process (continued)

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 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

4 Credit risk assessed using IRB approach (continued)

(b) Summary of credit exposures by IRB calculation approach

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

| | 2013 HK\$'M | 2012 HK\$'M |
|--|----------------|----------------|
| Retail exposures: | | |
| Retail IRB approach | | |
| Residential mortgages | 34,157 | 38,578 |
| Qualifying revolving retail exposures | 53,225 | 54,782 |
| Small business retail exposures | 30 | 33 |
| Other retail exposures to individuals | 8,839 | 9,121 |
| Wholesale exposures: | | |
| Foundation IRB approach | | |
| Sovereign exposures | 17,359 | 23,232 |
| Bank exposures | 129,665 | 100,133 |
| Corporate exposures | 80,195 | 67,801 |
| Supervisory slotting criteria approach | | |
| Specialised lending | 12,773 | 17,849 |
| Other exposures: | | |
| Specific risk-weight approach | 5,060 | 5,076 |
| | <u>341,303</u> | <u>316,605</u> |

(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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

4 Credit risk assessed using IRB approach (continued)

(c) Retail exposures (continued)

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

Residential mortgages

| EL% range | 2013 Exposure amount HK\$'M | 2012 Exposure amount HK\$'M |
|------------------|-----------------------------------|-----------------------------------|
| Up to 0.10% | 33,077 | 37,552 |
| > 0.10% to 0.50% | – | – |
| > 0.50% | 1,067 | 994 |
| Default | 13 | 32 |
| | <u>34,157</u> | <u>38,578</u> |

Qualifying revolving retail exposures

| EL% range | 2013 Exposure amount HK\$'M | 2012 Exposure amount HK\$'M |
|-----------|-----------------------------------|-----------------------------------|
| Up to 5% | 51,191 | 52,359 |
| > 5% | 1,983 | 2,363 |
| Default | 51 | 60 |
| | <u>53,225</u> | <u>54,782</u> |

Small business retail exposures

| EL% range | 2013 Exposure amount HK\$'M | 2012 Exposure amount HK\$'M |
|------------|-----------------------------------|-----------------------------------|
| Up to 0.3% | 25 | 33 |
| > 0.3% | 5 | – |
| | <u>30</u> | <u>33</u> |

Other retail exposures to individuals

| EL% range | 2013 Exposure amount HK\$'M | 2012 Exposure amount HK\$'M |
|------------|-----------------------------------|-----------------------------------|
| Up to 0.3% | 4,453 | 5,266 |
| > 0.3% | 4,344 | 3,804 |
| Default | 42 | 51 |
| | <u>8,839</u> | <u>9,121</u> |

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UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

4 Credit risk assessed using IRB approach (continued)

(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 a validated quantitative tool. This is supplemented by expert judgement of qualitative factors such as management strength by credit officers.

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

2013

| Credit Risk Rating | PD range (%) | Exposure amount HK\$'M | Exposure-weighted average risk-weight (%) |
|--------------------|-----------------|---------------------------|---|
| 1-3 | 0.00 – 0.10 | <u>17,359</u> | 16 |

2012

| Credit Risk Rating | PD range (%) | Exposure amount HK\$'M | Exposure-weighted average risk-weight (%) |
|--------------------|-----------------|---------------------------|---|
| 1-3 | 0.00 – 0.10 | <u>23,232</u> | 15 |

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UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

4 Credit risk assessed using IRB approach (continued)

(d) Wholesale exposures (continued)

Bank exposures

2013

| Credit Risk Rating | PD range (%) | Exposure amount HK\$'M | Exposure-weighted average risk-weight (%) |
|--------------------|-----------------|---------------------------|---|
| 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 | | <u>129,665</u> | |

2012

| Credit Risk Rating | PD range (%) | Exposure amount HK\$'M | Exposure-weighted average risk-weight (%) |
|--------------------|-----------------|---------------------------|---|
| 1-3 | 0.03 – 0.10 | 63,873 | 16 |
| 4A/4B | 0.10 – 0.33 | 28,482 | 49 |
| 5 | 0.33 – 0.47 | 5,566 | 66 |
| 6A/6B | 0.47 – 1.11 | 1,361 | 87 |
| 7A-9 | 1.11 – 99.99 | 851 | 116 |
| Total | | <u>100,133</u> | |

Corporate exposures

2013

| Credit Risk Rating | PD range (%) | Exposure amount HK\$'M | Exposure-weighted average risk-weight (%) |
|--------------------|-----------------|---------------------------|---|
| 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 | | <u>80,195</u> | |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

4 Credit risk assessed using IRB approach (continued)

(d) Wholesale exposures (continued)

Corporate exposures (continued)

2012

| Credit Risk Rating | PD range | Exposure amount | Exposure-weighted average risk-weight |
|--------------------|--------------|-----------------|---------------------------------------|
| | (%) | HK\$'M | (%) |
| 1-3 | 0.03 – 0.10 | 2,097 | 17 |
| 4A/4B | 0.10 – 0.33 | 989 | 53 |
| 5 | 0.33 – 0.47 | 2,335 | 68 |
| 6A/6B | 0.47 – 1.11 | 7,850 | 87 |
| 7A-9 | 1.11 – 99.99 | 53,515 | 116 |
| 10A-11 | 100 | 1,015 | 106 |
| Total | | <u>67,801</u> | |

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.

2013

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

2012

| Obligor grade | Exposure amount | Exposure-weighted average risk-weight |
|---------------|-----------------|---------------------------------------|
| | HK\$'M | (%) |
| Strong | 3,179 | 60 |
| Good | 8,862 | 89 |
| Satisfactory | 5,740 | 122 |
| Weak | 68 | 265 |
| Total | <u>17,849</u> | |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

4 Credit risk assessed using IRB approach (continued)

(e) Policies for establishing provisions

The policies are set out in Note 2(h) 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.

| Exposure classes | Actual loss | Expected loss as at |
|---------------------------------------|--|----------------------------|
| | for the year ended 31 December 2013 HK\$'M | 31 December 2012 HK\$'M |
| 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 |
| | 253 | 1,987 |

| Exposure classes | Actual loss | Expected loss as at |
|---------------------------------------|--|----------------------------|
| | for the year ended 31 December 2012 HK\$'M | 31 December 2011 HK\$'M |
| Residential mortgages | – | 34 |
| Qualifying revolving retail exposures | 80 | 478 |
| Small business retail exposures | – | – |
| Other retail exposures to individuals | 60 | 284 |
| Sovereign exposures | – | 37 |
| Bank exposures | – | 92 |
| Corporate exposures | 38 | 1,109 |
| | 178 | 2,034 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

4 Credit risk assessed using IRB approach (continued)

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

Comparison of actual default rate against estimated probability of default

| 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 |

| Exposure classes | Actual percentage of default for the year ended 31 December 2012 % | Estimated 1-year probability of default as at 31 December 2011 % |
|---------------------------------------|--|--|
| Residential mortgages | 0.05 | 0.55 |
| Qualifying revolving retail exposures | 0.55 | 1.01 |
| Small business retail exposures | – | 0.29 |
| Other retail exposures to individuals | 3.69 | 5.54 |
| Sovereign exposures | – | 0.02 |
| Bank exposures | – | 0.63 |
| Corporate exposures | 0.89 | 3.41 |

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 2013 and 2012.

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 2013 and 2012 respectively. The two measures of losses are therefore not directly comparable.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

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:

2013

| | Total exposures | Total exposures after credit risk mitigation | Risk-weighted amount after credit risk mitigation |
|---|--------------------|--|--|
| | HK\$'M | HK\$'M | HK\$'M |
| On-balance sheet | | | |
| 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 |
| | <u>17,517</u> | <u>14,489</u> | <u>13,972</u> |
| Off-balance sheet | | | |
| Off-balance sheet exposures other than over-the-counter derivative transactions | 582 | 387 | 387 |
| Over-the-counter derivative transactions | 240 | 92 | 91 |
| | <u>822</u> | <u>479</u> | <u>478</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

5 Credit risk assessed using Standardised approach (continued)

2012

| | Total exposures | Total exposures after credit risk mitigation | Risk-weighted amount after credit risk mitigation |
|---|-----------------|--|---|
| | HK\$'M | HK\$'M | HK\$'M |
| On-balance sheet | | | |
| Sovereign exposures | – | 33 | – |
| Public sector entity exposures | – | 652 | 130 |
| Bank exposures | 50 | 50 | 50 |
| Corporate exposures | 7,695 | 7,151 | 7,151 |
| Regulatory retail exposures | 1,615 | 1,213 | 910 |
| Other exposures which are not past due exposures | 5,760 | 4,400 | 4,400 |
| Past due exposures | 253 | 253 | 354 |
| | <u>15,373</u> | <u>13,752</u> | <u>12,995</u> |
| Off-balance sheet | | | |
| Off-balance sheet exposures other than over-the-counter derivative transactions | 563 | 366 | 365 |
| Over-the-counter derivative transactions | 154 | 73 | 72 |
| | <u>717</u> | <u>439</u> | <u>437</u> |

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 42(a) 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 2013 and 2012, the credit and market risks concentrations within the credit risk mitigation used by the Bank are under a minimal level.

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UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

6 Credit risk mitigation (continued)

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

2013

| | Exposure amount covered by recognised collateral | Exposure amount covered by recognised guarantee |
|---|--|---|
| | HK\$'M | HK\$'M |
| Foundation IRB approach | | |
| Corporate exposures | 26,441 | 12,487 |
| Bank exposures | 3,566 | – |
| | <u>30,007</u> | <u>12,487</u> |
| Standardised approach | | |
| 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 | – |
| | <u>3,390</u> | <u>521</u> |
| Total | <u><u>33,397</u></u> | <u><u>13,008</u></u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

6 Credit risk mitigation (continued)

2012

| | Exposure amount covered by recognised collateral | Exposure amount covered by recognised guarantee |
|--|--|---|
| | HK\$'M | HK\$'M |
| Foundation IRB approach | | |
| Corporate exposures | 23,209 | 5,455 |
| Bank exposures | 11 | – |
| | <u>23,220</u> | <u>5,455</u> |
| Standardised approach | | |
| Corporate exposures | 514 | 30 |
| Regulatory retail exposures | 399 | 3 |
| Other exposures which are not past due exposures | 708 | 652 |
| Past due exposures | 20 | 11 |
| Off-balance sheet exposures other than over-the-counter derivative transactions | 198 | – |
| Over-the-counter derivative transactions | 81 | – |
| | <u>1,920</u> | <u>696</u> |
| Total | <u><u>25,140</u></u> | <u><u>6,151</u></u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

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:

| | 2013 HK\$'M | 2012 HK\$'M |
|--|----------------|----------------|
| Counterparty credit risk exposures under IRB approach | | |
| Default risk exposures | | |
| (a) Derivative contracts | | |
| – Positive fair values | 8,785 | 4,992 |
| – Potential future exposures | 8,705 | 7,788 |
| | <u>17,490</u> | <u>12,780</u> |
| Of which: | | |
| – Bank exposures | 8,286 | 6,645 |
| – Corporate exposures | 9,204 | 6,135 |
| | <u>17,490</u> | <u>12,780</u> |
| Less : Effects of netting arrangement | <u>(6,605)</u> | <u>(4,453)</u> |
| Default risk exposures after netting | 10,885 | 8,327 |
| Less: Collateral amount | | |
| – Recognised financial collateral | (432) | (322) |
| – Other eligible collateral | (763) | (489) |
| | <u>9,690</u> | <u>7,516</u> |
| (b) Securities financing transactions | | |
| Default risk exposures | | |
| – Bank exposures | 5,150 | – |
| Less: Collateral amount | | |
| – Recognised financial collateral | (3,559) | – |
| | <u>1,591</u> | <u>–</u> |
| Risk-weighted amounts | | |
| (a) Derivative contracts | | |
| – Bank exposures | 368 | 380 |
| – Corporate exposures | 10,859 | 7,317 |
| | <u>11,227</u> | <u>7,697</u> |
| (b) Securities financing transactions | | |
| – Bank exposures | 121 | – |
| | <u>121</u> | <u>–</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

7 Counterparty credit risk-related exposures (continued)

| | 2013 HK\$'M | 2012 HK\$'M |
|---|----------------|----------------|
| Counterparty credit risk exposures under Standardised approach | | |
| Default risk exposures | | |
| (a) Derivative contracts | | |
| – Positive fair values | 143 | 47 |
| – Potential future exposures | 97 | 107 |
| | <u>240</u> | <u>154</u> |
| Of which: | | |
| – Corporate exposures | 239 | 149 |
| – Regulatory retail exposures | 1 | 3 |
| – Other exposures which are not past due exposures | – | 2 |
| | <u>240</u> | <u>154</u> |
| Less: Recognised financial collateral | <u>(148)</u> | <u>(81)</u> |
| | <u>92</u> | <u>73</u> |
| Risk-weighted amounts | | |
| (a) Derivative contracts | | |
| – Corporate exposures | 90 | 68 |
| – Regulatory retail exposures | 1 | 2 |
| – Other exposures which are not past due exposures | – | 2 |
| | <u>91</u> | <u>72</u> |

There are no outstanding credit derivative contracts which create exposures to counterparty credit risk as at 31 December 2013 (2012: 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.

8 Liquidity ratio

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

| | 2013 | 2012 |
|-------------------------|--------------|--------------|
| Average liquidity ratio | <u>38.8%</u> | <u>40.3%</u> |

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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

9 Segmental information

(a) Segmental information by class of business

| | Group | | | Total HK\$'M |
|--|--|--------------------|------------------|-----------------|
| | Commercial and consumer banking HK\$'M | Treasury HK\$'M | Others HK\$'M | |
| 2013 | | | | |
| Total income | <u>7,351</u> | <u>400</u> | <u>411</u> | <u>8,162</u> |
| Profit before allowances for credit and other losses | <u>3,782</u> | <u>263</u> | <u>351</u> | <u>4,396</u> |
| Profit before income tax | <u>3,724</u> | <u>266</u> | <u>138</u> | <u>4,128</u> |
| Operating assets | <u>200,169</u> | <u>100,179</u> | <u>8,311</u> | <u>308,659</u> |
| 2012 | | | | |
| Total income | <u>6,574</u> | <u>223</u> | <u>551</u> | <u>7,348</u> |
| Profit before allowances for credit and other losses | <u>3,191</u> | <u>64</u> | <u>502</u> | <u>3,757</u> |
| Profit before income tax | <u>3,096</u> | <u>64</u> | <u>575</u> | <u>3,735</u> |
| Operating assets | <u>175,713</u> | <u>101,887</u> | <u>7,912</u> | <u>285,512</u> |

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 centralised cash management for deposit taking and lending, trading activities and management of investment securities and the overall funding of the Banking Group.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

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(Expressed in millions of Hong Kong dollars)

9 Segmental information (continued)

(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:

| | Group | | | |
|----------------------------------|-----------------|--|------------------|-----------------|
| | Banks HK\$'M | Public sector entities HK\$'M | Others HK\$'M | Total HK\$'M |
| 2013 | | | | |
| 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 |
| | <u>116,619</u> | <u>5,339</u> | <u>17,715</u> | <u>139,673</u> |
| 2012 | | | | |
| Asia Pacific excluding Hong Kong | 89,810 | 3,908 | 11,651 | 105,369 |
| North and South America | 2,201 | 2,894 | 352 | 5,447 |
| Europe | 1,906 | 10 | 1,398 | 3,314 |
| Others | 92 | 155 | 1,101 | 1,348 |
| | <u>94,009</u> | <u>6,967</u> | <u>14,502</u> | <u>115,478</u> |

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.

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10 Loans and advances to customers

(a) Loans and advances to customers by loan usage

| | Bank | | | |
|---|----------------------------------|---|----------------------------------|---|
| | 2013 | | 2012 | |
| | Outstanding balance HK\$'M | Balance covered by collateral HK\$'M | Outstanding balance HK\$'M | Balance covered by collateral HK\$'M |
| Gross loans and advances for use in Hong Kong | | | | |
| Industrial, commercial and financial | | | | |
| – Property development | 1,521 | 1,520 | 2,296 | 2,296 |
| – Property investment | 27,198 | 26,135 | 28,758 | 27,988 |
| – Financial concerns | 1,539 | 1,244 | 1,343 | 1,048 |
| – Stockbrokers | 9 | 9 | 13 | 13 |
| – Wholesale and retail trade | 16,882 | 13,500 | 17,090 | 11,852 |
| – Manufacturing | 10,712 | 7,664 | 10,100 | 7,550 |
| – Transport and transport equipment | 9,995 | 9,677 | 10,896 | 10,564 |
| – Recreational activities | 21 | 17 | 35 | 33 |
| – Information technology | 241 | 100 | 290 | 86 |
| – Others | 8,931 | 7,552 | 5,871 | 4,653 |
| 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 | 506 | 506 | 663 | 663 |
| – Loans for the purchase of other residential properties | 29,615 | 29,615 | 33,647 | 33,647 |
| – Credit card advances | 7,846 | – | 7,022 | – |
| – Others | 9,171 | 3,082 | 7,733 | 2,460 |
| | 124,187 | 100,621 | 125,757 | 102,853 |
| Trade finance (including trade bills) | 69,909 | 12,307 | 46,326 | 10,548 |
| Gross loans and advances for use outside Hong Kong | 7,664 | 2,375 | 5,069 | 2,139 |
| | 201,760 | 115,303 | 177,152 | 115,540 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

10 Loans and advances to customers (continued)

(b) Overdue loans and advances to customers

The overdue loans and advances are analysed as follows:

| | Bank | | | |
|---|---------------|---|---------------|---|
| | 2013 | | 2012 | |
| | HK\$'M | % of gross loans and advances to customers | HK\$'M | % of gross loans and advances to customers |
| Six months or less but over three months | 137 | 0.07 | 130 | 0.07 |
| One year or less but over six months | 212 | 0.10 | 192 | 0.11 |
| Over one year | 881 | 0.44 | 1,021 | 0.58 |
| | <u>1,230</u> | <u>0.61</u> | <u>1,343</u> | <u>0.76</u> |
| Individual impairment allowances made in respect of the above overdue loans and advances | <u>733</u> | | <u>855</u> | |
| Current market value of collateral held against the covered portion of the above overdue loans and advances | <u>740</u> | | <u>1,037</u> | |
| Covered portion of the above overdue loans and advances | <u>450</u> | | <u>560</u> | |
| Uncovered portion of the above overdue loans and advances | <u>780</u> | | <u>783</u> | |

(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:

| | Bank | | | |
|--------------------------------|---------------|---|---------------|---|
| | 2013 | | 2012 | |
| | HK\$'M | % of gross loans and advances to customers | HK\$'M | % of gross loans and advances to customers |
| Rescheduled loans and advances | <u>261</u> | 0.13 | <u>261</u> | 0.15 |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

10 Loans and advances to customers (continued)

(d) Repossessed assets

As at 31 December 2013, repossessed assets of the Bank amounted to HK\$63 million (2012: HK\$29 million).

(e) Non-bank Mainland exposures

| Bank | On-balance sheet exposures HK\$'M | Off-balance sheet exposures HK\$'M | Total HK\$'M | Individual impairment allowances HK\$'M |
|--|--|---|-------------------------|--|
| 2013 | | | | |
| Mainland entities | 6,046 | 312 | 6,358 | 21 |
| Companies and individuals outside Mainland where the credit is granted for use in Mainland | 5,922 | 1,300 | 7,222 | 192 |
| Other counterparties where the exposures are considered to be non-bank Mainland exposures | 1,137 | 101 | 1,238 | – |
| | <u>13,105</u> | <u>1,713</u> | <u>14,818</u> | <u>213</u> |
| 2012 | | | | |
| Mainland entities | 5,751 | 863 | 6,614 | 21 |
| Companies and individuals outside Mainland where the credit is granted for use in Mainland | 5,210 | 1,834 | 7,044 | 227 |
| Other counterparties where the exposures are considered to be non-bank Mainland exposures | 7 | 6 | 13 | – |
| | <u>10,968</u> | <u>2,703</u> | <u>13,671</u> | <u>248</u> |

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

(Expressed in millions of Hong Kong dollars)

11 Currency concentration

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

| | USD HK\$'M | GBP HK\$'M | JPY HK\$'M | EUR HK\$'M | CNY HK\$'M | CAD HK\$'M | CHF HK\$'M | AUD HK\$'M | NZD HK\$'M | Others HK\$'M | Total HK\$'M |
|---|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|------------------|-----------------|
| 2013 | | | | | | | | | | | |
| Hong Kong dollar equivalents | | | | | | | | | | | |
| Spot assets | 80,767 | 2,634 | 729 | 1,394 | 44,838 | 280 | 153 | 5,281 | 46 | 2,807 | 138,929 |
| Spot liabilities | (67,248) | (1,515) | (666) | (2,109) | (22,658) | (2,264) | (239) | (11,220) | (1,220) | (1,894) | (111,033) |
| Forward purchases | 174,230 | 255 | 4,779 | 1,156 | 135,916 | 2,248 | 110 | 7,673 | 1,385 | 537 | 328,289 |
| Forward sales | (188,697) | (1,419) | (4,853) | (501) | (157,197) | (285) | (9) | (1,608) | (85) | (1,442) | (356,096) |
| Net options position | 48 | (14) | (2) | – | (1) | 2 | – | (23) | (84) | – | (74) |
| Net (short) / long non-structural position | (900) | (59) | (13) | (60) | 898 | (19) | 15 | 103 | 42 | 8 | 15 |
| Net structural position | – | – | – | – | 29 | – | – | – | – | (32) | (3) |
| 2012 | | | | | | | | | | | |
| Hong Kong dollar equivalents | | | | | | | | | | | |
| Spot assets | 68,691 | 1,290 | 1,455 | 1,801 | 25,976 | 253 | 270 | 6,667 | 203 | 1,988 | 108,594 |
| Spot liabilities | (63,618) | (1,540) | (950) | (1,965) | (16,764) | (2,049) | (261) | (8,494) | (1,031) | (2,080) | (98,752) |
| Forward purchases | 165,491 | 365 | 6,298 | 2,555 | 116,027 | 1,882 | 5 | 3,453 | 918 | 84 | 297,078 |
| Forward sales | (170,345) | (161) | (6,839) | (2,351) | (125,096) | (13) | (12) | (1,005) | (3) | (18) | (305,843) |
| Net options position | (43) | 2 | 71 | (42) | (1) | (65) | – | (468) | (54) | (1) | (601) |
| Net long / (short) non-structural position | 176 | (44) | 35 | (2) | 142 | 8 | 2 | 153 | 33 | (27) | 476 |
| Net structural position | – | – | – | – | 31 | – | – | – | – | (46) | (15) |

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 with all material aspects, 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 the 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 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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

CORPORATE GOVERNANCE REPORT (CONTINUED)

1 Board and Management Committees (continued)

(b) Board Risk Management Committee

The Board Risk Management Committee is authorised by the Board 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, 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, 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, are non-executive directors (including the Board Risk Management Committee Chairman). The Board Risk Management Committee members are appropriately qualified to discharge their responsibilities as they have the relevant technical experience in risk disciplines.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

CORPORATE GOVERNANCE REPORT (CONTINUED)

1 Board and Management Committees (continued)

(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 business mandates, all matters involving Special Purpose Vehicles and transactions presenting 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 credit, business, risk management and other units.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

CORPORATE GOVERNANCE REPORT (CONTINUED)

1 Board and Management Committees (continued)

(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 Corporate Governance Report in the Annual Report of DBSH for details of the Board Compensation and Management Development Committee and major characteristics of the remuneration system.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

CORPORATE GOVERNANCE REPORT (CONTINUED)

2 Disclosure on Remuneration pursuant to the HKMA Supervisory Policy Manual CG-5 “Guideline on a Sound Remuneration System” (continued)

(b) Aggregate quantitative information on remuneration for senior management and key personnel for the year ended 31 December 2013 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 | 2013 | 2012 |
|--|---------------|-------------|
| Number of senior management | 10 | 10 |
| Number of key personnel | 1 | 1 |
| | HK\$’M | HK\$’M |
| Fixed remuneration | | |
| • Cash based | 32 | 31 |
| • Share based | – | – |
| • Other | – | – |
| Variable remuneration (Note i) | | |
| • Cash based | 36 | 32 |
| • Share based | 27 | 21 |
| • Other | – | – |
| | 95 | 84 |
| | HK\$’M | HK\$’M |
| Breakdown of deferred remuneration | 2013 | 2012 |
| | HK\$’M | HK\$’M |
| • Outstanding – vested | – | – |
| • Outstanding – unvested | 63 | 43 |
| • Awarded during the year | 27 | 21 |
| • Paid out during the year | 6 | 8 |
| • Reductions in current year due to ex-post adjustment – explicit (Note ii) | – | – |
| • Reductions in current year due to ex-post adjustment – implicit (Note iii) | – | – |

In 2013, there were two cases of sign-on award being paid to senior management or key personnel which amount to HK\$1,461,313 (2012: HK\$66,125).

No senior management or key personnel has been awarded with new guaranteed bonus or severance payments in 2013 (2012: Nil).

Note

- (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.

DBS BANK (HONG KONG) LIMITED AND ITS SUBSIDIARIES

CORPORATE GOVERNANCE REPORT (CONTINUED)

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 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. 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 staff are 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 appraises 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, Internal 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 latest external independent quality assessment was completed in 2013. Aside from reporting that Internal Audit "Generally Conformed" to the IIA Standards, the review which was conducted by KPMG highlighted several best practices in the Internal Audit team.

Group Audit was recognised for its crucial role in the Group's corporate governance framework and has won the runner-up for the Internal Audit Excellence Award in the 2013 Securities Investors Association of Singapore (SIAS) Investors' Choice Awards, jointly organised by the SIAS, IIA Singapore and Singapore Management University.