

Standard Chartered Bank  
(Hong Kong) Limited

Condensed Consolidated  
Interim Financial Statements (unaudited)

For the period ended  
30 June 2018

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The directors are pleased to announce the unaudited consolidated interim results of Standard Chartered Bank (Hong Kong) Limited (the “Bank”) and its subsidiaries (together referred to as the “Group”) for the six months ended 30 June 2018.

**2018 First Half Results**

Profit before taxation increased by HK\$2,018 million from HK\$4,617 million to HK\$6,635 million. Net interest income increased by 26 per cent to HK\$7,021 million. Net fee and commission income decreased by 8 per cent over the corresponding period in 2017. Total operating income increased by 9 per cent to HK\$13,606 million.

Operating expenses decreased by 5 per cent over the corresponding period to HK\$7,629 million. Total impairments decreased by HK\$282 million over the corresponding period.

Profit after taxation was HK\$5,916 million, an increase of HK\$1,932 million over HK\$3,984 million recorded in the first half of 2017.

**Condensed consolidated income statement (unaudited)****For the period ended 30 June 2018***(Expressed in millions of Hong Kong dollars)*

	Note	6 months ended 30 June 2018	6 months ended 30 June 2017
Interest income	3	9,733	7,652
Interest expense	4	(2,712)	(2,091)
<b>Net interest income</b>		<b>7,021</b>	5,561
Fee and commission income		3,711	4,284
Fee and commission expense		(376)	(659)
Net fee and commission income	5	3,335	3,625
Net trading income	6	1,096	1,345
Other operating income	7	2,154	1,905
		6,585	6,875
<b>Total operating income</b>		<b>13,606</b>	12,436
Staff costs		(3,291)	(3,165)
Premises and equipment		(1,665)	(1,722)
Others		(2,673)	(3,126)
<b>Operating expenses</b>	8	<b>(7,629)</b>	(8,013)
<b>Operating profit before impairment</b>		<b>5,977</b>	4,423
Credit impairment	9	(96)	(401)
Other impairment	10	(423)	(400)
<b>Operating profit after impairment</b>		<b>5,458</b>	3,622
Share of profit of associates		1,177	995
<b>Profit before taxation</b>		<b>6,635</b>	4,617
Taxation	11	(719)	(633)
<b>Profit after taxation</b>		<b>5,916</b>	3,984

The notes on pages 7 to 55 form part of these condensed consolidated interim financial statements.

**Condensed consolidated statement of comprehensive income (unaudited)****For the period ended 30 June 2018***(Expressed in millions of Hong Kong dollars)*

	<b>6 months ended 30 June 2018</b>	<i>6 months ended 30 June 2017</i>
<b>Profit after taxation</b>	<b>5,916</b>	3,984
<b>Other comprehensive income:</b>		
<u>Items that will not be reclassified to the income statement:</u>		
Own credit adjustment:		
– Own credit gains/(losses) on financial liabilities designated at fair value through profit or loss	<b>344</b>	(499)
Defined benefit plans:		
– Remeasurement of net defined benefit liability	<b>84</b>	100
– Related tax effect	<b>(14)</b>	(17)
<u>Items that may be reclassified subsequently to the income statement:</u>		
Debt securities at fair value through other comprehensive income/ Available-for-sale securities		
– Changes in fair value recognised during the period	<b>(24)</b>	330
– Changes in fair value transferred to the income statement on disposal	<b>(39)</b>	(9)
– Transfer to the income statement on fair value hedged items attributable to hedged risk	<b>100</b>	(163)
– Expected credit loss	<b>7</b>	–
– Share of impact from associate	<b>158</b>	(123)
– Related tax effect	<b>(7)</b>	(6)
Cash flow hedges:		
– Changes in fair value recognised during the period	<b>513</b>	111
– Transferred to the income statement on termination of hedging derivatives	<b>33</b>	7
– Related tax effect	<b>(90)</b>	(20)
Exchange difference	<b>(240)</b>	433
Other comprehensive income for the period, net of tax	<b>825</b>	144
<b>Total comprehensive income for the period</b>	<b>6,741</b>	4,128

The notes on pages 7 to 55 form part of these condensed consolidated interim financial statements.

**Condensed consolidated statement of financial position as at 30 June 2018 (unaudited)***(Expressed in millions of Hong Kong dollars)*

	Note	At 30 June 2018	At 31 December 2017
<b>Assets</b>			
Cash and balances with banks, central banks and other financial institutions		12,061	18,350
Placements with banks and other financial institutions	13	163,174	150,256
Hong Kong SAR Government certificates of indebtedness		44,751	42,341
Financial assets at fair value through profit or loss	14	31,398	22,819
Investment securities	17	239,080	207,927
Advances to customers	15	524,369	480,867
Amounts due from immediate holding company		58,378	59,075
Amounts due from fellow subsidiaries		21,578	24,208
Interest in associate		12,095	11,638
Property, plant and equipment	18	42,521	40,632
Goodwill and intangible assets		1,431	1,392
Current tax assets		–	11
Deferred tax assets		82	275
Other assets	19	15,285	15,258
		<u>1,166,203</u>	<u>1,075,049</u>
<b>Liabilities</b>			
Hong Kong SAR currency notes in circulation		44,751	42,341
Deposits and balances of banks and other financial institutions		29,837	19,613
Deposits from customers	21	878,290	833,899
Financial liabilities at fair value through profit or loss	22	26,003	19,775
Debt securities in issue	23	3,525	3,066
Amounts due to immediate holding company		59,262	44,246
Amounts due to fellow subsidiaries		11,969	9,477
Current tax liabilities		936	439
Deferred tax liabilities		484	470
Other liabilities	24	24,795	21,292
Subordinated liabilities	25	5,923	6,003
		<u>1,085,775</u>	<u>1,000,621</u>
<b>Equity</b>			
Share capital		20,256	20,256
Reserves		58,220	52,220
Shareholders' equity	26	78,476	72,476
Other equity instruments		1,952	1,952
		<u>80,428</u>	<u>74,428</u>
		<u>1,166,203</u>	<u>1,075,049</u>

The notes on pages 7 to 55 form part of these condensed consolidated interim financial statements.

**Condensed consolidated statement of changes in equity (unaudited)****For the period ended 30 June 2018***(Expressed in millions of Hong Kong dollars)*

	Attributable to equity shareholders of the Group												
	Share capital	Own credit adjustment reserve	Available-for-sale investment reserve	FVOCI reserve – Debt	FVOCI reserve – Equity	Exchange reserve	Cash flow hedge reserve	Revaluation reserve	Retained earnings	Share option equity reserve	Capital contribution reserve	Other equity instruments	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
At 1 January 2017	20,256	-	(274)	-	-	(856)	(192)	146	46,448	184	-	-	65,712
Transfer of own credit adjustment, net of taxation	-	363	-	-	-	-	-	-	(363)	-	-	-	-
Total comprehensive income	-	(499)	29	-	-	433	98	-	4,067	-	-	-	4,128
Dividend paid <sup>1</sup>	-	-	-	-	-	-	-	-	(122)	-	-	-	(122)
Movement in respect of share-based compensation plans	-	-	-	-	-	-	-	-	-	40	-	-	40
At 30 June 2017	20,256	(136)	(245)	-	-	(423)	(94)	146	50,030	224	-	-	69,758
Total comprehensive income	-	118	222	-	-	434	112	-	4,692	-	-	-	5,578
Dividend paid <sup>1</sup>	-	-	-	-	-	-	-	-	(3,246)	-	-	-	(3,246)
Movement in respect of share-based compensation plans	-	-	-	-	-	-	-	-	-	94	-	-	94
Other equity instruments issued, net of expenses	-	-	-	-	-	-	-	-	-	-	-	1,952	1,952
Effect of deemed disposal of interest in an associate	-	-	-	-	-	255	-	(146)	146	-	-	-	255
Effect of transfer of a subsidiary to a commonly controlled entity	-	-	-	-	-	-	-	-	-	-	37	-	37
At 31 December 2017	20,256	(18)	(23)	-	-	266	18	-	51,622	318	37	1,952	74,428
Impact of HKFRS 9/IFRS 9 transition adjustments <sup>2</sup> (note 34(a))	-	-	23	(315)	161	-	-	-	(502)	-	-	-	(633)
At 1 January 2018	20,256	(18)	-	(315)	161	266	18	-	51,120	318	37	1,952	73,795
Total comprehensive income	-	344	-	195	-	(240)	456	-	5,986	-	-	-	6,741
Dividend paid <sup>1</sup>	-	-	-	-	-	-	-	-	(172)	-	-	-	(172)
Movement in respect of share-based compensation plans	-	-	-	-	-	-	-	-	-	64	-	-	64
At 30 June 2018	20,256	326	-	(120)	161	26	474	-	56,934	382	37	1,952	80,428

<sup>1</sup> During the six months ended 30 June 2018, there were no dividends declared and paid in respect of 'A' and 'B' ordinary shares (year ended 31 December 2017: HK\$1.61276 per share totaling HK\$3,124 million). Total dividend of HK\$172 million (year ended 31 December 2017: HK\$244 million) were paid in respect of the US\$500 million 6.25% perpetual non-cumulative convertible preference shares and the US\$250 million 5% perpetual non-cumulative subordinated capital securities classified as equity.

<sup>2</sup> The details of transition adjustments as at 1 January 2018 in relation to the adoption of Hong Kong Financial Reporting Standard 9 ("HKFRS 9")/International Financial Reporting Standard 9 ("IFRS 9") Financial Instruments are disclosed in note 34.

The notes on pages 7 to 55 form part of these condensed consolidated interim financial statements.

**Condensed consolidated cash flow statement (unaudited)****For the period ended 30 June 2018***(Expressed in millions of Hong Kong dollars)*

	<b>For 6 months ended 30 June 2018 HK\$'M</b>	<i>For 6 months ended 30 June 2017 HK\$'M</i>
<b>Operating activities</b>		
Profit before taxation	<b>6,635</b>	4,617
Adjustments for non-cash items and other adjustments included within income statement	<b>361</b>	571
Change in operating assets	<b>(46,310)</b>	(91,940)
Change in operating liabilities	<b>84,334</b>	30,093
Income tax paid	<b>(7)</b>	(2)
<b>Net cash from/(used in) operating activities</b>	<b>45,013</b>	(56,661)
<b>Investing activities</b>		
Payment for purchase of intangible assets	<b>(126)</b>	–
Payment for purchase of property, plant and equipment	<b>(4,989)</b>	(6,429)
Proceeds from disposal of property, plant and equipment	<b>665</b>	378
Proceeds from disposal of an associate	<b>1,076</b>	–
Dividend received from an associate	<b>18</b>	–
<b>Net cash used in investing activities</b>	<b>(3,356)</b>	(6,051)
<b>Financing activities</b>		
Interest paid on subordinated liabilities	<b>(272)</b>	(172)
Dividend paid to shareholders of the Group	<b>(172)</b>	(122)
<b>Net cash used in financing activities</b>	<b>(444)</b>	(294)
<b>Net increase/(decrease) in cash and cash equivalents</b>	<b>41,213</b>	(63,006)
<b>Cash and cash equivalents at 1 January</b>	<b>143,700</b>	140,893
Effect of foreign exchange	<b>(1,315)</b>	6,155
<b>Cash and cash equivalents at 30 June</b>	<b>183,598</b>	84,042

The notes on pages 7 to 55 form part of these condensed consolidated interim financial statements.



## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 1. Principal activities

Standard Chartered Bank (Hong Kong) Limited (the “Bank”) is a licensed bank registered under the Hong Kong Banking Ordinance. The principal activities of the Bank and its subsidiaries (together referred to as the “Group”) are the provision of banking and related financial services.

### 2. Significant accounting policies

#### (a) Statement of compliance

These condensed consolidated interim financial statements have been prepared in compliance with Hong Kong Accounting Standard (“HKAS”) 34, Interim Financial Reporting, issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”) and International Accounting Standard (“IAS”) 34 Interim Financial Reporting, issued by the International Accounting Standards Board (“IASB”).

The preparation of the condensed consolidated interim financial statements in conformity with HKAS 34/IAS 34 requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses on a year-to-date basis. Actual results may differ from these estimates. In preparing the condensed consolidated interim financial statements, the significant judgement made by management in applying the Group’s accounting policies and the key sources of estimation uncertainty were the same as those that were applied to the consolidated financial statements for the year ended 31 December 2017, except for the treatment of financial instruments under HKFRS 9/IFRS 9 as explained in note 2(b).

The condensed consolidated interim financial statements should be read in conjunction with the consolidated financial statements for the year ended 31 December 2017, which have been prepared in accordance with Hong Kong Financial Reporting Standards (“HKFRSs”) and International Financial Reporting Standards (“IFRSs”).

The condensed consolidated interim financial statements are unaudited.

#### (b) Basis of preparation

Except as described below, the accounting policies applied in preparing these condensed consolidated interim financial statements are materially consistent with those applied in preparing the consolidated financial statements for the year ended 31 December 2017.

Except for the adoption of HKFRS 9/IFRS 9 (see note 2(b)(i)) and HKFRS 15/IFRS 15 Revenue from contracts with customers (see note 2(b)(ii)), none of the revised accounting standards which became effective from 1 January 2018, have a material impact on the condensed consolidated interim financial statements.

#### (i) HKFRS 9/IFRS 9 Financial Instruments

On 1 January 2018, the Group adopted HKFRS 9/IFRS 9 which replaces HKAS 39/IAS 39 Financial Instruments: Recognition and Measurement and introduces new requirements for: the classification and measurement of financial instruments, the recognition and measurement of credit impairment provisions, and provides for a simplified approach to hedge accounting.

The Group has further chosen:

- to continue to apply HKAS 39/IAS 39 hedging requirements rather than those of HKFRS 9/IFRS 9.
- not to restate comparative periods on the basis that it is not possible to do so without the use of hindsight.

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (I) HKFRS 9/IFRS 9 Financial Instruments (continued)

##### (i) Classification and measurement of financial instruments

###### Classification

The Group classifies its financial assets into the following measurement categories: amortised cost; fair value through other comprehensive income; and fair value through profit or loss. Financial liabilities are classified as either amortised cost, or held at fair value through profit or loss. Management determines the classification of its financial assets and liabilities at initial recognition of the instrument or, where applicable, at the time of reclassification.

##### (1) Financial assets held at amortised cost and fair value through other comprehensive income

Debt instruments held at amortised cost or held at fair value through other comprehensive income (“FVOCI”) have contractual terms that give rise to cash flows that are solely payments of principal and interest (“SPPI characteristics”). Principal is the fair value of the financial asset at initial recognition but this may change over the life of the instrument as amounts are repaid. Interest consists of consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period and for other basic lending risks and costs, as well as a profit margin.

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

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

Whether financial assets are held at amortised cost or at FVOCI depend on the objectives of the business models under which the assets are held. A business model refers to how the Group manages financial assets to generate cash flows.

The Group makes an assessment of the objective of a business model in which an asset is held at the individual product business line, and where applicable within business lines depending on the way the business is managed and information is provided to management. Factors considered include:

- how the performance of the product business line is evaluated and reported to the Group’s management;
- how managers of the business model are compensated, including whether management is compensated based on the fair value of assets or the contractual cash flows collected;

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (i) HKFRS 9/IFRS 9 Financial Instruments (continued)

- the risks that affect the performance of the business model and how those risks are managed;
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and expectations about future sales activity.

Financial assets which have SPPI characteristics and that are held within a business model whose objective is to hold financial assets to collect contractual cash flows (“hold to collect”) are recorded at amortised cost. Conversely, financial assets which have SPPI characteristics but are held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets (“hold to collect and sell”) are classified as held at FVOCI.

Both hold to collect business model and a hold to collect and sell business model involve holding financial assets to collect the contractual cash flows. However, the business models are distinct by reference to the frequency and significance that asset sales play in meeting the objective under which a particular group of financial assets is managed. Hold to collect business models are characterised by asset sales that are incidental to meeting the objectives under which a group of assets is managed. Sales of assets under a hold to collect business model can be made to manage increases in the credit risk of financial assets but sales for other reasons should be both infrequent and insignificant.

Cash flows from the sale of financial assets under a hold to collect and sell business model in contrast are integral to achieving the objectives under which a particular group of financial assets are managed. This may be the case where frequent sales of financial assets are required to manage the Group’s daily liquidity requirements or to meet regulatory requirements to demonstrate liquidity of financial instruments. Sales of assets under hold to collect and sell business models are therefore both more frequent and more significant in value than those under the hold to collect model.

##### *Equity instruments designated as held at FVOCI*

Non-trading equity instruments acquired for strategic purposes rather than capital gain may be irrevocably designated at initial recognition at FVOCI on an instrument by instrument basis. Gains and losses arising from changes in the fair value of these instruments, including foreign exchange gains and losses, are recognised directly in equity and are never reclassified to profit or loss even on derecognition.

##### (2) Financial assets and liabilities held at fair value through profit or loss

Financial assets which are not held at amortised cost or not held at fair value through other comprehensive income are held at fair value through profit or loss. Financial assets and liabilities held at fair value through profit or loss are either mandatorily classified as fair value through profit or loss or irrevocably designated at fair value through profit or loss at initial recognition.

##### *Mandatorily classified at fair value through profit or loss*

Financial assets and liabilities which are mandatorily held at fair value through profit or loss are split between two sub-categories as follows:

- Trading, including
  - financial assets and liabilities held for trading, which are those acquired principally for the purpose of selling in the short term; and
  - derivatives.

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (I) HKFRS 9/IFRS 9 Financial Instruments (continued)

- Non-trading mandatorily at fair value through profit or loss, including
  - instruments (other than trading or derivatives) in a business which has a fair value business model;
  - hybrid financial assets that contain one or more embedded derivatives;
  - financial assets that would otherwise be measured at amortised cost or FVOCI but which do not have SPPI characteristics;
  - equity instruments that have not been designated as held at FVOCI; and
  - financial liabilities that constitute contingent consideration in a business combination.

##### *Designated at fair value through profit or loss*

Financial assets and liabilities may be designated at fair value through profit or loss when the designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities on a different basis (“accounting mismatch”).

To reduce accounting mismatches, the Group has designated certain financial liabilities at fair value through profit or loss where the liabilities either:

- have fixed rates of interest and interest rate swaps or other interest rate derivatives have been entered with the intention of significantly reducing interest rate risk; or
- are exposed to foreign currency risk and derivatives have been acquired with the intention of significantly reducing exposure to market changes; or
- have been acquired to fund trading asset portfolios or assets.

Financial liabilities may also be designated at fair value through profit or loss where they are managed on a fair value basis or have a bifurcately embedded derivative where the Group is not able to separately value the embedded derivative component.

##### (3) Financial liabilities held at amortised cost

Financial liabilities that are not financial guarantees or loan commitments and that are not classified as financial liabilities held at fair value through profit or loss are classified as financial liabilities held at amortised cost.

##### *Financial guarantee contracts and loan commitments*

The Group issues financial guarantee contracts and loan commitments in return for fees. Under a financial guarantee contract, the Group undertakes to meet a customer’s obligations under the terms of a debt instrument if the customer fails to do so. Loan commitments are firm commitments to provide credit under prespecified terms and conditions. Financial guarantee contracts and loan commitments issued at below market interest rates are initially recognised as liabilities at fair value, whilst financial guarantees and loan commitments issued at market rates are recorded off balance sheet. Subsequently these instruments are measured at the higher of the expected credit loss provision, and the amount initially recognised less the cumulative amount of income recognised in accordance with the principles of HKFRS 15/IFRS 15.

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (i) HKFRS 9/IFRS 9 Financial Instruments (continued)

###### Fair value of financial assets and liabilities

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal market for the asset or liability, or in the absence of a principal market, the most advantageous market to which the Group has access at that date. The fair value of a liability includes the risk that the bank will not be able to honour its obligations.

The fair value of financial instruments is generally measured on the basis of the individual financial instrument. However, when a group of financial assets and financial liabilities is managed on the basis of its net exposure to either market risk or credit risk, the fair value of the group of financial instruments is measured on a net basis.

The fair values of quoted financial assets and liabilities in active markets are based on current prices. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. If the market for a financial instrument, and for unlisted securities, is not active, the Group establishes fair value by using valuation techniques.

###### Initial recognition

Purchases and sales of financial assets and liabilities held at fair value through profit or loss, and debt securities classified as financial assets held at fair value through other comprehensive income are initially recognised on the trade-date (the date on which the Group commits to purchase or sell the asset). Loans and advances and other financial assets held at amortised cost are recognised on settlement date (the date on which cash is advanced to the borrowers).

All financial instruments are initially recognised at fair value, which is normally the transaction price, plus directly attributable transaction costs for financial assets which are not subsequently measured at fair value through profit or loss.

In certain circumstances, the initial fair value may be based on a valuation technique which may lead to the recognition of profits or losses at the time of initial recognition. However, these profits or losses can only be recognised when the valuation technique used is based solely on observable market data. In those cases where the initially recognised fair value is based on a valuation model that uses unobservable inputs, the difference between the transaction price and the valuation model is not recognised immediately in the income statement but is amortised or released to the income statement as the inputs become observable, or the transaction matures or is terminated.

###### Subsequent measurement

##### (1) Financial assets and financial liabilities held at amortised cost

Financial assets and financial liabilities held at amortised cost are subsequently carried at amortised cost using the effective interest method (see note 2(b)(i)(iii)). Foreign exchange gains and losses are recognised in the income statement.

Where a financial instrument carried at amortised cost is the hedged item in a qualifying fair value hedge relationship, its carrying value is adjusted by the fair value gain or loss attributable to the hedged risk.

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (1) HKFRS 9/IFRS 9 Financial Instruments (continued)

##### (2) Financial assets held at FVOCI

Debt instruments held at FVOCI are subsequently carried at fair value, with all unrealised gains and losses arising from changes in fair value (including any related foreign exchange gains or losses) recognised in other comprehensive income and accumulated in a separate component of equity. Foreign exchange gains and losses on the amortised cost are recognised in the income statement. Changes in expected credit losses are recognised in the income statement and are accumulated in a separate component of equity. On derecognition, the cumulative fair value gains or losses, net of the cumulative expected credit loss in reserve, are transferred to the income statement.

Equity investments designated at FVOCI are subsequently carried at fair value with all unrealised gains and losses arising from changes in fair value (including any related foreign exchange gains or losses) recognised in other comprehensive income and accumulated in a separate component of equity. On derecognition, the cumulative reserve is transferred to retained earnings and is not recycled to the income statement.

##### (3) Financial assets and liabilities held at fair value through profit or loss

Financial assets and liabilities mandatorily held at fair value through profit or loss and financial assets designated at fair value through profit or loss are subsequently carried at fair value, with gains and losses arising from changes in fair value recorded in the net trading income line in the income statement unless the instrument is part of a cash flow hedging relationship. Contractual interest income on financial assets held at fair value through profit or loss is recognised as interest income in a separate line in the income statement.

##### (4) Financial liabilities designated at fair value through profit or loss

Financial liabilities designated at fair value through profit or loss are held at fair value, with changes in fair value recognised in the net trading income line in the income statement, other than that attributable to changes in credit risk. Fair value changes attributable to credit risk are recognised in other comprehensive income and recorded in a separate category of reserves unless this is expected to create or enlarge an accounting mismatch, in which case the entire change in fair value of the financial liability designated fair value through profit or loss is recognised in the income statement.

#### **Derecognition of financial instruments**

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership. If substantially all the risks and rewards have been neither retained nor transferred and the Group has retained control, the assets continue to be recognised to the extent of the Group's continuing involvement.

Where financial assets have been modified, the modified terms are assessed on a qualitative and quantitative basis to determine whether a fundamental change in the nature of the instrument has occurred, such as whether the derecognition of the pre-existing instrument and the recognition of a new instrument is appropriate.

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (i) HKFRS 9/IFRS 9 Financial Instruments (continued)

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of the consideration received (including any new asset obtained less any new liability assumed) and any cumulative gain or loss that had been recognised in other comprehensive income is recognised in the income statement except for equity instruments elected FVOCI and cumulative fair value adjustments attributable to the credit risk of a liability that are held in other comprehensive income.

Financial liabilities are derecognised when they are extinguished. A financial liability is extinguished when the obligation is discharged, cancelled or expired and this is evaluated both qualitatively and quantitatively.

If the Group purchases its own debt, it is derecognised and the difference between the carrying amount of the liability and the consideration paid is included in 'other operating income' except for the cumulative fair value adjustments attributable to the credit risk of a liability that are held in other comprehensive income which are never recycled to the income statement.

##### **Modified financial instruments**

Financial assets and financial liabilities whose original contractual terms have been modified, including those loans subject to forbearance strategies, are considered to be modified instruments. Modifications may include changes to the tenor, cash flows and or interest rates amongst other factors.

Where derecognition of financial assets is appropriate, the newly recognised residual loans are assessed to determine whether the assets should be classified as purchased or originated credit impaired assets ("POCI").

Where derecognition is not appropriate, the gross carrying amount of the applicable instruments are recalculated as the present value of the renegotiated or modified contractual cash flows discounted at the original effective interest rate (or credit adjusted effective interest rate for POCI financial assets). The difference between the recalculated values and the pre-modified gross carrying values of the instruments are recorded as a modification gain or loss in the income statement.

##### **Reclassifications**

Financial liabilities are not reclassified subsequent to initial recognition.

Reclassifications of financial assets are made when, and only when, the business model for those assets changes. Such changes are expected to be infrequent and arise as a result of significant external or internal changes such as the termination of a line of business or the purchase of a subsidiary whose business model is to realise the value of pre-existing held for trading financial assets through a hold to collect model.

Financial assets are reclassified at their fair value on the date of reclassification and previously recognised gains and losses are not restated. Moreover, reclassifications of financial assets between financial assets held at amortised cost and financial assets held at fair value through other comprehensive income do not affect effective interest rate or expected credit loss computations.

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (i) HKFRS 9/IFRS 9 Financial Instruments (continued)

###### (1) Reclassified from amortised cost

Where financial assets held at amortised cost are reclassified to financial assets held at fair value through profit or loss, the difference between the fair value of the assets at the date of reclassification and the previously recognised amortised cost is recognised in the income statement.

For financial assets held at amortised cost that are reclassified to fair value through other comprehensive income, the difference between the fair value of the assets at the date of reclassification and the previously recognised gross carrying value is recognised in other comprehensive income. Additionally, the related cumulative expected credit loss amounts relating to the reclassified financial assets are reclassified from loan loss provisions to a separate reserve in other comprehensive income at the date of reclassification.

###### (2) Reclassified from fair value through other comprehensive income

Where financial assets held at fair value through other comprehensive income are reclassified to financial assets held at fair value through profit or loss, the cumulative gain or loss previously recognised in other comprehensive income is transferred to the income statement.

For financial assets held at fair value through other comprehensive income that are reclassified to financial assets held at amortised cost, the cumulative gain or loss previously recognised in other comprehensive income is adjusted against the fair value of the financial asset such that the financial asset is recorded at a value as if it had always been held at amortised cost. In addition, the related cumulative expected credit losses held within other comprehensive income are reversed against the gross carrying value of the reclassified assets at the date of reclassification.

###### (3) Reclassified from fair value through profit or loss

Where financial assets held at fair value through profit or loss are reclassified to financial assets held at fair value through other comprehensive income or financial assets held at amortised cost, the fair value at the date of reclassification is used to determine the effective interest rate on the financial asset going forward. In addition, the date of reclassification is used as the date of initial recognition for the calculation of expected credit losses. Where financial assets held at fair value through profit or loss are reclassified to financial assets held at amortised cost, the fair value at the date of reclassification becomes the gross carrying value of the financial asset.

##### (ii) Impairment

The Group's expected credit losses ("ECL") calculations are outputs of complex models with a number of underlying assumptions. The significant judgements and estimates in determining ECL include:

- the Group's criteria for assessing if there has been a significant increase in credit risk;
- development of ECL models, including the choice of inputs relating to macroeconomic variables.



## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (i) HKFRS 9/IFRS 9 Financial Instruments (continued)

The calculation of credit-impairment provisions also involves expert credit judgement to be applied by the credit risk management team based upon counterparty information they receive from various sources including relationship managers and on external market information.

ECL are determined for all financial debt instruments that are classified at amortised cost or fair value through other comprehensive income, undrawn commitments and financial guarantees.

An expected credit loss represents the present value of expected cash shortfalls over the residual term of a financial asset, undrawn commitment or financial guarantee.

A cash shortfall is the difference between the cash flows that are due in accordance with the contractual terms of the instrument and the cash flows that the Group expects to receive over the contractual life of the instrument.

##### **Measurement**

Expected credit losses are computed as unbiased, probability weighted amounts which are determined by evaluating a range of reasonably possible outcomes, the time value of money, and considering all reasonable and supportable information including that which is forward looking.

For material portfolios, the estimate of expected cash shortfalls is determined by multiplying the probability of default ("PD") with the loss given default ("LGD") with the expected exposure at the time of default ("EAD"). For less material Retail loan portfolios, the Group has adopted simplified approaches based on historical roll rates or loss rates.

Forward looking economic assumptions are incorporated into the PD, LGD and EAD where relevant and where they influence credit risk, such as GDP growth rates, interest rates, house price indices and commodity prices amongst others. These assumptions are incorporated using the Group's most likely forecast for a range of macroeconomic assumptions. These forecasts are determined using all reasonable and supportable information, which includes both internally developed forecasts and those available externally, and are consistent with those used for budgeting, forecasting and capital planning.

To account for the potential non-linearity in credit losses, multiple forward-looking scenarios are incorporated into the range of reasonably possible outcomes for all material portfolios. For example, where there is a greater risk of downside credit losses than upside gains, multiple forward-looking economic scenarios are incorporated into the range of reasonably possible outcomes, both in respect of determining the PD (and where relevant, the LGD and EAD) and in determining the overall expected credit loss amounts. These scenarios are determined using a Monte Carlo approach centered around the Group's most likely forecast of macroeconomic assumptions.

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (i) HKFRS 9/IFRS 9 Financial Instruments (continued)

The period over which cash shortfalls are determined is generally limited to the maximum contractual period for which the Group is exposed to credit risk. However, for certain revolving credit facilities, which include credit cards or overdrafts, the Group's exposure to credit risk is not limited to the contractual period. For these instruments, the Group estimates an appropriate life based on the period that the Group is exposed to credit risk, which includes the effect of credit risk management actions such as the withdrawal of undrawn facilities.

For credit-impaired financial instruments, the estimate of cash shortfalls may require the use of expert credit judgement. As a practical expedient, the Group may also measure credit impairment on the basis of an instrument's fair value using an observable market price.

The estimate of expected cash shortfalls on a collateralised financial instrument reflects the amount and timing of cash flows that are expected from foreclosure on the collateral less the costs of obtaining and selling the collateral, regardless of whether foreclosure is deemed probable.

Cash flows from unfunded credit enhancements held are included within the measurement of expected credit losses if they are part of, or integral to, the contractual terms of the instrument (this includes financial guarantees, unfunded risk participations and other non-derivative credit insurance).

Cash shortfalls are discounted using the effective interest rate (or credit-adjusted effective interest rate for POCI instruments) on the financial instrument as calculated at initial recognition or if the instrument has a variable interest rate, the current effective interest rate determined under the contract.

<u>Instruments</u>	<u>Location of expected credit loss provisions</u>
Financial assets held at amortised cost	Loss provisions: netted against gross carrying value <sup>1</sup>
Debt instruments at FVOCI	Other comprehensive income (FVOCI Reserve) <sup>2</sup>
Loan commitments and financial guarantees	Other liabilities <sup>3</sup>

<sup>1</sup> Purchased or originated credit impaired assets do not attract an ECL provision on initial recognition. An ECL provision will be recognised only if there is an increase in expected credit losses from that considered at initial recognition.

<sup>2</sup> Debt securities classified as FVOCI are held at fair value. The ECL attributed to these instruments is held as a separate reserve within OCI and is recycled to the profit and loss account along with any fair value measurement gains or losses held within FVOCI when the applicable instruments are derecognised.

<sup>3</sup> ECL on loan commitments and financial guarantees is recognised as a liability provision. Where a financial instrument includes both a loan (i.e. financial asset component) and an undrawn commitment (i.e. loan commitment component), and it is not possible to separately identify the ECL on these components, ECL amounts on the loan commitment are recognised together with ECL amounts on the financial asset. To the extent the combined ECL exceeds the gross carrying amount of the financial asset, the ECL is recognised as a liability provision.

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (i) HKFRS 9/IFRS 9 Financial Instruments (continued)

###### Recognition

###### (1) 12 months expected credit losses (stage 1)

Expected credit losses are recognised at the time of initial recognition of a financial instrument and represent the lifetime cash shortfalls arising from possible default events up to 12 months into the future from the balance sheet date. Expected credit losses continue to be determined on this basis until there is either a significant increase in the credit risk of an instrument or the instrument becomes credit-impaired. If an instrument is no longer considered to exhibit a significant increase in credit risk, expected credit losses will revert to being determined on a 12-month basis.

###### (2) Significant increase in credit risk (stage 2)

If a financial asset experiences a significant increase in credit risk (“SICR”) since initial recognition, an expected credit loss provision is recognised for default events that may occur over the lifetime of the asset.

Significant increase in credit risk is assessed by comparing the risk of default of an exposure at the reporting date to the risk of default at origination (after taking into account the passage of time). Significant does not mean statistically significant nor is it assessed in the context of changes in ECL. Whether a change in the risk of default is significant or not is assessed using a number of quantitative and qualitative factors, the weight of which depends on the type of product and counterparty. Financial assets that are 30 or more days past due and not credit-impaired will always be considered to have experienced a significant increase in credit risk. For less material portfolios where a loss rate or roll rate approach is applied to compute ECL significant increase in credit risk is primarily based on 30 days past due.

Quantitative factors include an assessment of whether there has been significant increase in the forward-looking PD since origination. A forward-looking PD is one that is adjusted for future economic conditions to the extent these are correlated to changes in credit risk. We compare the residual lifetime PD at the balance sheet date to the residual lifetime PD that was expected at the time of origination for the same point in the term structure and determine whether both the absolute and relative change between the two exceeds predetermined thresholds. To the extent that the differences between the measures of default outlined exceed the defined thresholds, the instrument is considered to have experienced a significant increase in credit risk.

Qualitative factors assessed include those linked to current credit risk management processes, such as lending placed on non-purely precautionary early alert (and subject to closer monitoring).

A non-purely precautionary early alert account is one which exhibits risk or potential weaknesses of a material nature requiring closer monitoring, supervision, or attention by management. Weaknesses in such account, if left uncorrected, could result in deterioration of repayment prospects and the likelihood of being downgraded. Indicators could include a rapid erosion of position within the industry, concerns over management’s ability to manage operations, weak/deteriorating operating results, liquidity strain and overdue balances amongst other factors.

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (i) HKFRS 9/IFRS 9 Financial Instruments (continued)

##### (3) Credit impaired (or defaulted) exposures (stage 3)

Financial assets that are credit impaired (or in default) represent those that are at least 90 days past due in respect of principal and/or interest. Financial assets are also considered to be credit impaired where the obligors are unlikely to pay on the occurrence of one or more observable events that have a detrimental impact on the estimated future cash flows of the financial asset. It may not be possible to identify a single discrete event but instead the combined effect of several events may cause financial assets to become credit impaired.

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

- Significant financial difficulty of the issuer or borrower;
- Breach of contract such as default or a past due event;
- For economic or contractual reasons relating to the borrower’s financial difficulty, the lenders of the borrower have granted the borrower concessions that lenders would not otherwise consider, which include forbearance actions;
- Pending or actual bankruptcy or other financial reorganisation to avoid or delay discharge of the borrower’s obligations;
- The disappearance of an active market for the applicable financial asset due to financial difficulties of the borrower;
- Purchase or origination of a financial asset at a deep discount that reflects incurred credit losses.

Irrevocable lending commitments to a credit impaired obligor that have not yet been drawn down are also included within the stage 3 credit impairment provision to the extent that the commitment cannot be withdrawn.

Loss provisions against credit impaired financial assets are determined based on an assessment of the recoverable cash flows under a range of scenarios, including the realisation of any collateral held where appropriate. The loss provisions held represent the difference between the present value of the cash flows expected to be recovered, discounted at the instrument’s original effective interest rate, and the gross carrying value of the instrument prior to any credit impairment.

#### **Expert Credit Judgement**

For Corporate & Institutional, Commercial and Private Banking, borrowers are graded by credit risk management on a credit grading (“CG”) scale from CG1 to CG14. Once a borrower starts to exhibit credit deterioration, it will move along the credit grading scale in the performing book and when it is classified as CG12 the credit assessment and oversight of the loan will normally be performed by Group Special Assets Management (“GSAM”).

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (i) HKFRS 9/IFRS 9 Financial Instruments (continued)

Borrowers graded CG12 exhibit well defined weaknesses in areas such as management and/or performance but there is no current expectation of a loss of principal or interest. Where the impairment assessment indicates that there will be a loss of principal on a loan as the most likely scenario, the borrower is graded CG14 while borrowers where there is no loss in principal but only an impairment provision on the discount to reflect the net present value of the asset in the likely scenario under HKFRS 9/IFRS 9 assessment is considered CG13. (Instruments graded CG13 or CG14 are regarded as Non-Performing Loans, i.e. stage 3 or credit impaired exposures).

For individually significant financial assets within stage 3, GSAM will consider all judgements that have an impact on the expected future cash flows of the asset. These include: the business prospects, industry and geo-political climate of the customer, quality of realisable value of collateral, the Group's legal position relative to other claimants and any renegotiation/forbearance/modification options. The difference between the loan carrying amount and the discounted expected future cash flows will result in the stage 3 credit impairment amount. The future cash flow calculation involves significant judgements and estimates. As new information becomes available and further negotiations/forbearance measures are taken the estimates of the future cash flows will be revised, and will have an impact on the future cash flow analysis.

For financial assets which are not individually significant, such as the Retail portfolio or small business loans, which comprise a large number of homogenous loans that share similar characteristics, statistical estimates and techniques are used, as well as credit scoring analysis.

Retail banking clients are considered credit impaired where they are more than 90 days past due. Retail products are also considered credit impaired if the borrower files for bankruptcy or other forbearance program, the borrower is deceased or the business is closed in the case of a small business, or if the borrower surrenders the collateral, or there is an identified fraud on the account. Additionally, if the account is unsecured and the borrower has other credit accounts with the Group that are considered credit impaired, the account may be also be credit impaired.

Techniques used to compute impairment amounts use models which analyse historical repayment and default rates over a time horizon. Where various models are used, judgement is required to analyse the available information provided and select the appropriate model or combination of models to use.

Expert credit judgement is also applied to determine whether any post-model adjustments are required for credit risk elements which are not captured by the models.

#### **Modified financial instruments**

Where the original contractual terms of a financial asset have been modified for credit reasons and the instrument has not been derecognised, the resulting modification loss is recognised within impairment in the income statement within a corresponding decrease in the gross carrying value of the asset. If the modification involved a concession that the bank would not otherwise consider, the instrument is considered to be credit impaired and is considered forborne.

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (i) HKFRS 9/IFRS 9 Financial Instruments (continued)

ECL for modified financial assets that have not been derecognised and are not considered to be credit-impaired will be recognised on a 12-month basis, or a lifetime basis, if there is a significant increase in credit risk. These assets are assessed to determine whether there has been a significant increase in credit risk subsequent to the modification. Although loans may be modified for non-credit reasons, a significant increase in credit risk may occur.

In addition to the recognition of modification gains and losses, the revised carrying value of modified financial assets will impact the calculation of expected credit losses, with any increase or decrease in ECL recognised within impairment.

##### *Forborne loans*

Forborne loans are those loans that have been modified in response to customers' financial difficulties.

Forbearance strategies assist clients who are temporarily in financial distress and are unable to meet their original contractual repayment terms. Forbearance can be initiated by the client, the Group or a third party including government sponsored programmes or a conglomerate of credit institutions. Forbearance may include debt restructuring such as new repayment schedules, payment deferrals, tenor extensions, interest only payments, lower interest rates, forgiveness of principal, interest or fees, or relaxation of loan covenants.

Forborne loans that have been modified (and not derecognised) on terms that are not consistent with those readily available in the market and/or where we have granted a concession compared to the original terms of the loans are considered credit impaired if there is a detrimental impact on cash flows. The modification loss is recognised in the income statement within impairment and the gross carrying value of the loan reduced by the same amount.

##### **Write-offs of credit impaired instruments and reversal of impairment**

To the extent a financial debt instrument is considered irrecoverable, the applicable portion of the gross carrying value is written off against the related loan provision. Such loans are written off after all the necessary procedures have been completed, it is decided that there is no realistic probability of recovery and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the income statement. If, in a subsequent period, the amount of the credit impairment loss decreases and the decrease can be related objectively to an event occurring after the credit impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised credit impairment loss is reversed by adjusting the provision account. The amount of the reversal is recognised in the income statement.

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (i) HKFRS 9/IFRS 9 Financial Instruments (continued)

###### *Improvement in credit risk/curing*

A period may elapse from the point at which instruments enter lifetime expected credit losses (stage 2 or stage 3) and are reclassified back to 12 month expected credit losses (stage 1). For financial assets that are credit-impaired (stage 3), a transfer to stage 2 or stage 1 is only permitted where the instrument is no longer considered to be credit-impaired. An instrument will no longer be considered credit-impaired when there is no shortfall of cash flows compared to the original contractual terms.

For financial assets within stage 2, these can only be transferred to stage 1 when they are no longer considered to have experienced a significant increase in credit risk.

Where significant decrease in credit risk was determined using quantitative measures, the instruments will be automatically transferred back to stage 1 when the original PD based transfer criteria are no longer met. Where instruments were transferred to stage 2 due to an assessment of qualitative factors, the issues that led to the reclassification must be cured before the instruments can be reclassified to stage 1. This includes instances where management actions led to instruments being classified as stage 2, requiring that action to be resolved before loans are reclassified to stage 1.

A forbore loan can only be removed from the disclosure (cured) if the loan is performing (stage 1 or 2) and a further two year probation period is met.

In order for a forbore loan to become performing, the following criteria have to be satisfied:

- At least a year has passed with no default based upon the forbore contract terms
- The customer is likely to repay its obligations in full without realising security
- The customer has no accumulated impairment against amount outstanding

Subsequent to the criteria above, a further two year probation period has to be fulfilled, whereby regular payments are made by the customer and none of the exposures to the customer are more than 30 days past due.

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 2. Significant accounting policies (continued)

#### (b) Basis of preparation (continued)

##### (I) HKFRS 9/IFRS 9 Financial Instruments (continued)

##### (iii) Net interest income and other gains or losses arising from financial instruments

Interest income for financial assets held at either FVOCI or amortised cost, and interest expense on all financial liabilities held at amortised cost is recognised in the income statement using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the expected life of the instrument. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to the gross carrying amount of a financial asset or the amortised cost of a financial liability. When calculating the effective interest rate for financial instruments other than credit impaired assets, the Group estimates cash flows considering all contractual terms of the financial instrument (for example, prepayment, extension, call and similar options) but does not consider expected credit losses. The calculation of effective interest rate includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability and all other premiums or discounts.

Interest income for financial assets that are either held at FVOCI or amortised cost that have become credit impaired subsequent to initial recognition (stage 3) and have had amounts written off, is recognised using the credit adjusted effective interest rate.

This rate is calculated in the same manner as the effective interest rate except that expected credit losses are included in the expected cash flows. Interest income is therefore recognised on the amortised cost of the financial asset including expected credit losses. Should the credit risk on a stage 3 financial asset improve such that the financial asset is no longer considered credit impaired, interest income recognition reverts to a computation based on the rehabilitated gross carrying value of the financial asset.

Dividends on equity instruments are recognised in the income statement within other operating income when the Group's right to receive payment is established. Foreign exchange gains and losses on monetary items are recognised in net trading income.

##### (II) HKFRS 15/IFRS 15 Revenue from Contracts with Customers

HKFRS 15/IFRS 15 is effective from 1 January 2018 and replaces HKAS 18/IAS 18 Revenue. HKFRS 15/IFRS 15 is conceptually similar to HKAS 18/IAS 18, but includes more granular guidance on how to recognise and measure revenue, and also introduces additional disclosure requirements. The Group performed an assessment of the new standard and concluded that the current treatment of revenue from contracts with customers is consistent with the new principles, and there is no transitional impact to retained earnings.

#### (c) Basis of consolidation

These condensed consolidated interim financial statements cover the consolidated positions of Standard Chartered Bank (Hong Kong) Limited and all its subsidiaries, unless otherwise stated, and include the attributable share of the results and reserves of its associate.



**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***3. Interest income**

	<b>6 months ended 30 June 2018 HK\$'M</b>	<b>6 months ended 30 June 2017 HK\$'M</b>
Interest income arising from financial assets:–		
– not measured at fair value through profit or loss	<b>9,250</b>	7,528
– held for trading	<b>390</b>	121
– mandatorily at fair value through profit or loss other than held for trading	<b>93</b>	–
– designated at fair value through profit or loss	<b>–</b>	3
	<b>9,733</b>	7,652

**4. Interest expense**

	<b>6 months ended 30 June 2018 HK\$'M</b>	<b>6 months ended 30 June 2017 HK\$'M</b>
Interest expense arising from financial liabilities:–		
– not measured at fair value through profit or loss	<b>2,639</b>	1,998
– held for trading	<b>40</b>	24
– designated at fair value through profit or loss	<b>33</b>	69
	<b>2,712</b>	2,091

**5. Net fee and commission income**

Net fee and commission income in the condensed consolidated income statement includes the following:

	<b>6 months ended 30 June 2018 HK\$'M</b>	<b>6 months ended 30 June 2017 HK\$'M</b>
Net fee and commission income, other than amounts included in determining the effective interest rate, arising from financial assets or financial liabilities that are not at fair value through profit or loss:		
– fee and commission income	<b>855</b>	1,100
– fee and commission expense	<b>167</b>	95
Net fee and commission income from trust and other fiduciary activities that result in the holding or investing of assets on behalf of its customers:		
– fee and commission income	<b>257</b>	209
– fee and commission expense	<b>77</b>	62

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***6. Net trading income**

	<b>6 months ended 30 June 2018 HK\$'M</b>	<b>6 months ended 30 June 2017 HK\$'M</b>
Net gains on instruments held for trading	<b>1,134</b>	1,375
Net gains on financial assets designated at fair value through profit or loss	–	22
Net losses on non-trading financial assets mandatorily at fair value through profit or loss	<b>(37)</b>	–
Net losses on financial liabilities designated at fair value through profit or loss	<b>(1)</b>	(52)
	<b>1,096</b>	1,345

**7. Other operating income**

	<b>6 months ended 30 June 2018 HK\$'M</b>	<b>6 months ended 30 June 2017 HK\$'M</b>
Rental income from operating lease assets	<b>1,943</b>	1,779
Dividend income from financial assets at fair value through other comprehensive income/available-for-sale securities	<b>10</b>	13
Net gains from disposal of debt securities at fair value through other comprehensive income/available-for-sale securities	<b>39</b>	9
Net losses on disposal of financial instruments measured at amortised cost	<b>(15)</b>	(3)
Net gains on disposal and write-off of fixed assets	<b>82</b>	34
Others	<b>95</b>	73
	<b>2,154</b>	1,905

**8. Operating expenses**

	<b>6 months ended 30 June 2018 HK\$'M</b>	<b>6 months ended 30 June 2017 HK\$'M</b>
Staff costs		
– contributions to defined contribution plans	<b>133</b>	86
– expense in respect of the defined benefits plan	<b>39</b>	42
– equity-settled share-based payment expenses	<b>65</b>	32
– salaries and other staff costs	<b>3,054</b>	3,005
Depreciation (note 18)	<b>1,102</b>	1,053
Premises and equipment expense, excluding depreciation		
– rental of premises	<b>403</b>	420
– others	<b>160</b>	249
Amortisation of other intangible assets	<b>87</b>	71
Auditor's remuneration	<b>7</b>	9
Others	<b>2,579</b>	3,046
	<b>7,629</b>	8,013

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***9. Credit impairment**

	<b>6 months ended 30 June 2018 HK\$'M</b>	<b>6 months ended 30 June 2017 HK\$'M</b>
Net impairment charges/(releases) on advances to customers:		
– collective impairment releases	–	(95)
– individual impairment charges	–	496
	<u>–</u>	<u>401</u>
	-----	-----
Net expected credit loss charges/(releases) on:		
– placements with banks and other financial institutions	2	–
– advances to customers	106	–
– debt securities at amortised cost	(1)	–
– debt securities at fair value through other comprehensive income	7	–
– loan commitments and financial guarantees	(18)	–
	<u>96</u>	<u>–</u>
	-----	-----
	<u>96</u>	<u>401</u>
	=====	=====

**10. Other impairment**

	<b>6 months ended 30 June 2018 HK\$'M</b>	<b>6 months ended 30 June 2017 HK\$'M</b>
Charges for risk participation transactions	78	–
Charges for property, plant and equipment (note 18)	346	378
Others	(1)	22
	<u>423</u>	<u>400</u>
	=====	=====

**11. Taxation**

	<b>6 months ended 30 June 2018 HK\$'M</b>	<b>6 months ended 30 June 2017 HK\$'M</b>
Hong Kong profits tax	530	596
Overseas taxation	1	4
Deferred taxation	188	33
	<u>719</u>	<u>633</u>
	=====	=====

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 12. Segmental reporting

The Group manages its businesses by four client segments: Corporate and Institutional, Commercial, Private Banking and Retail:

- **Corporate & Institutional Banking (CIB)** supports clients with their transaction banking, corporate finance, financial markets and borrowing needs, providing solutions to clients in some of the world's fastest-growing economies and most active trade corridors. The Group's clients include large corporations, governments, and banks.
- **Commercial Banking** serves local corporations and medium-sized enterprises. The Group aims to be its clients' main international bank, providing a full range of international financial solutions in areas such as trade finance, cash management, financial markets and corporate finance.
- **Private Banking** offers a full suite of investment, credit and wealth planning solutions to grow and protect the wealth of high net worth individuals across the Group's footprint.
- **Retail Banking** serves individuals and small businesses with a focus on affluent and emerging affluent in many of the world's fastest-growing cities. The Group provides digital banking services with a human touch to its clients across deposits, payments, financing products and Wealth Management, as well as supporting client's business banking needs.

Besides the four client segments, Treasury Markets and certain items which are not managed directly by a client segment, including unallocated central costs are reported in "Central & Other Items". Financial information is presented internally to the Bank's senior management using these segments.

The Group comprises only one geographical segment as over 90% of the business is based in Hong Kong. Geographical segment is classified by the location of the principal operations of the subsidiary or, in the case of the Bank, the location of the branch responsible for reporting the results or advancing the funds.

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***12. Segmental reporting (continued)****(a) Segment results, assets and liabilities**

Revenue and expenses are allocated to the reportable segments with reference to income generated by those segments and the expenses incurred by those segments or which otherwise arise from the depreciation or amortisation of assets attributable to those segments.

<b>6 months ended 30 June 2018</b>	<b>Corporate &amp; Institutional Banking HK\$'M</b>	<b>Commercial Banking HK\$'M</b>	<b>Private Banking HK\$'M</b>	<b>Retail Banking HK\$'M</b>	<b>Central &amp; Other Items HK\$'M</b>	<b>Consolidated Total HK\$'M</b>
<i>Operating income</i>						
– Net interest income	1,955	886	348	3,651	241	7,081
– Other operating income	3,096	475	408	3,001	430	7,410
	<u>5,051</u>	<u>1,361</u>	<u>756</u>	<u>6,652</u>	<u>671</u>	<u>14,491</u>
Operating expenses <sup>1</sup>	<u>(2,795)</u>	<u>(748)</u>	<u>(758)</u>	<u>(3,251)</u>	<u>(35)</u>	<u>(7,587)</u>
Operating profit/(loss) before impairment and taxation	<u>2,256</u>	<u>613</u>	<u>(2)</u>	<u>3,401</u>	<u>636</u>	<u>6,904</u>
Credit impairment and other impairment	<u>(218)</u>	<u>(61)</u>	<u>–</u>	<u>(178)</u>	<u>(6)</u>	<u>(463)</u>
Profit/(loss) before taxation	<u>2,038</u>	<u>552</u>	<u>(2)</u>	<u>3,223</u>	<u>630</u>	<u>6,441</u>
<b>At 30 June 2018</b>						
Segment assets	<u>415,056</u>	<u>69,325</u>	<u>39,404</u>	<u>262,361</u>	<u>414,316</u>	<u>1,200,462</u>
Segment liabilities	<u>380,530</u>	<u>105,996</u>	<u>53,380</u>	<u>442,941</u>	<u>78,216</u>	<u>1,061,063</u>

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***12. Segmental reporting (continued)****(a) Segment results, assets and liabilities (continued)**

<i>6 months ended 30 June 2017</i>	<i>Corporate &amp; Institutional Banking HK\$'M</i>	<i>Commercial Banking HK\$'M</i>	<i>Private Banking HK\$'M</i>	<i>Retail Banking HK\$'M</i>	<i>Central &amp; Other Items HK\$'M</i>	<i>Consolidated Total HK\$'M</i>
<i>Operating income</i>						
- Net interest income	1,152	752	314	3,216	268	5,702
- Other operating income	3,466	446	309	2,612	451	7,284
	<u>4,618</u>	<u>1,198</u>	<u>623</u>	<u>5,828</u>	<u>719</u>	<u>12,986</u>
Operating expenses <sup>1</sup>	<u>(2,599)</u>	<u>(802)</u>	<u>(684)</u>	<u>(3,001)</u>	<u>(10)</u>	<u>(7,096)</u>
Operating profit/(loss) before impairment loss and taxation	2,019	396	(61)	2,827	709	5,890
Credit impairment and other impairment	(520)	(63)	(1)	(217)	-	(801)
Profit/(loss) before taxation	<u>1,499</u>	<u>333</u>	<u>(62)</u>	<u>2,610</u>	<u>709</u>	<u>5,089</u>
<i>At 31 December 2017</i>						
Segment assets	<u>392,367</u>	<u>66,906</u>	<u>34,171</u>	<u>262,210</u>	<u>341,971</u>	<u>1,097,625</u>
Segment liabilities	<u>346,698</u>	<u>106,711</u>	<u>53,805</u>	<u>421,696</u>	<u>76,060</u>	<u>1,004,970</u>

<sup>1</sup> Operating expenses in Corporate & Institutional Banking segment included depreciation charges of HK\$988 million (30 June 2017: HK\$958 million) for commercial aircraft and vessels leased to customers under operating leases.

**(b) Reconciliation of reportable segment operating income, profit before taxation, assets and liabilities**

	<b>6 months ended 30 June 2018 HK\$'M</b>	<b>6 months ended 30 June 2017 HK\$'M</b>
<b>Operating income</b>		
Reportable segment revenue	<b>14,491</b>	12,986
Income relating to Financial Market products	<b>118</b>	(122)
Cost of free funds	<b>189</b>	86
Others	<b>(1,192)</b>	(514)
Total operating income	<u><b>13,606</b></u>	<u>12,436</u>

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***12. Segmental reporting (continued)****(b) Reconciliation of reportable segment operating income, profit before taxation, assets and liabilities (continued)**

	<b>6 months ended 30 June 2018 HK\$'M</b>	<b>6 months ended 30 June 2017 HK\$'M</b>
<b>Profit before taxation</b>		
Reportable segment profit before taxation	<b>6,441</b>	5,089
Income relating to Financial Market products	<b>118</b>	(122)
Cost of free funds	<b>189</b>	86
Reallocations of impairment charges	<b>(57)</b>	–
Others	<b>(56)</b>	(436)
	<hr/> <b>6,635</b> <hr/>	<hr/> 4,617 <hr/>
Profit before taxation	<hr/> <b>6,635</b> <hr/>	<hr/> 4,617 <hr/>
	<b>At 30 June 2018 HK\$'M</b>	<b>At 31 December 2017 HK\$'M</b>
<b>Assets</b>		
Reportable segment assets	<b>1,200,462</b>	1,097,625
Assets of group companies not included in consolidated total assets	<b>(3,560)</b>	(3,180)
Amounts due from immediate holding company and fellow subsidiaries	<b>79,956</b>	83,283
Others	<b>(110,655)</b>	(102,679)
	<hr/> <b>1,166,203</b> <hr/>	<hr/> 1,075,049 <hr/>
Total assets	<hr/> <b>1,166,203</b> <hr/>	<hr/> 1,075,049 <hr/>
	<b>At 30 June 2018 HK\$'M</b>	<b>At 31 December 2017 HK\$'M</b>
<b>Liabilities</b>		
Reportable segment liabilities	<b>1,061,063</b>	1,004,970
Liabilities of group companies not included in consolidated total liabilities	<b>(911)</b>	(1,774)
Amounts due to immediate holding company and fellow subsidiaries	<b>71,231</b>	53,723
Others	<b>(45,608)</b>	(56,298)
	<hr/> <b>1,085,775</b> <hr/>	<hr/> 1,000,621 <hr/>
Total liabilities	<hr/> <b>1,085,775</b> <hr/>	<hr/> 1,000,621 <hr/>

Income and profit before taxation recognised in the condensed consolidated interim financial statements represent an arm's length compensation for the services provided and risks borne. For internal management reporting purposes, income and profit before taxation are allocated on a global perspective. In addition, for internal management reporting purposes, a charge is allocated to reportable segments for the use of interest-free funds.

Reportable segment assets and liabilities include assets and liabilities which are not booked on the condensed consolidated statement of financial position but which contribute to the reportable segment's income and profit before taxation.

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***13. Placements with banks and other financial institutions**

	<i>At 30 June 2018 HK\$'M</i>	<i>At 31 December 2017 HK\$'M</i>
Placements with banks and other financial institutions		
– maturing within one month	<b>72,617</b>	63,984
– maturing between one month and one year	<b>85,345</b>	80,377
– maturing between one year to five years	<b>4,599</b>	5,175
– maturing between five years to ten years	<b>622</b>	720
	<b>163,183</b>	150,256
Less: Expected credit loss provision (note 16)	<b>(9)</b>	–
	<b>163,174</b>	150,256

**14. Financial assets at fair value through profit or loss**

	<i>At 30 June 2018 HK\$'M</i>	<i>At 31 December 2017 HK\$'M</i>
Trading assets	<b>24,754</b>	22,483
Non-trading financial assets mandatorily at fair value through profit or loss	<b>6,644</b>	–
Financial assets designated at fair value through profit or loss	–	336
	<b>31,398</b>	22,819



**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***15. Advances to customers**

	<i>At 30 June 2018 HK\$'M</i>	<i>At 31 December 2017 HK\$'M</i>
<b>(a) Advances to customers</b>		
Gross advances to customers	<b>524,610</b>	480,239
Trade bills	<b>1,312</b>	1,778
	<u><b>525,922</b></u>	<u>482,017</u>
Less:		
Expected credit loss provision: (note 16)	<b>(1,553)</b>	–
Impairment provision: (note 34(c))		
– collectively assessed	–	(243)
– individually assessed	–	(907)
	<u><b>(1,553)</b></u>	<u>(1,150)</u>
	<u><b>524,369</b></u>	<u>480,867</u>
<b>(b) Impaired advances to customers</b>		
Gross impaired advances to customers	<b>2,409</b>	3,278
Less:		
Stage 3 expected credit loss provision (note 16)	<b>(898)</b>	–
Impairment provision: individually assessed	–	(907)
	<u><b>1,511</b></u>	<u>2,371</u>
Gross impaired advances to customers as a % of gross advances to customers	<u><b>0.46%</b></u>	<u>0.68%</u>
Fair value of collateral held against the covered portion of impaired advances to customers	<b>1,071</b>	1,344
Covered portion of impaired advances to customers	<b>706</b>	1,064
Uncovered portion of impaired advances to customers	<u><b>1,703</b></u>	<u>2,214</u>

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



**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***17. Investment securities**

	<b>At 30 June 2018 HK\$'M</b>	<b>At 31 December 2017 HK\$'M</b>
At fair value through other comprehensive income/Available-for-sale securities:		
Debt securities		
– Treasury bills	<b>115,800</b>	86,608
– Certificates of deposit held	<b>20,551</b>	19,378
– Other debt securities	<b>100,212</b>	96,190
	<b>236,563</b>	202,176
Equity shares	<b>227</b>	701
	<b>236,790</b>	202,877
At amortised cost/Loans and receivables:		
Debt instruments – other debt securities	<b>2,300</b>	5,050
Less: Expected credit loss provision (note 16)	<b>(10)</b>	–
	<b>239,080</b>	207,927

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***18. Property, Plant and Equipment**

	<i>Buildings and leasehold land held for own use HK\$'M</i>	<i>Equipment, furniture &amp; fixtures HK\$'M</i>	<i>Operating lease assets HK\$'M</i>	<i>Sub-total HK\$'M</i>	<i>Investment properties HK\$'M</i>	<i>Total property, plant and equipment HK\$'M</i>
<b>Cost or valuation:</b>						
At 1 January 2018	2,780	518	44,424	47,722	866	48,588
Additions	40	81	4,868	4,989	–	4,989
Transferred to assets classified as assets held for sale	–	–	(1,111)	(1,111)	–	(1,111)
Disposals and write-offs	(2)	(32)	(626)	(660)	–	(660)
Reclassification	(3)	3	–	–	–	–
At 30 June 2018	<u>2,815</u>	<u>570</u>	<u>47,555</u>	<u>50,940</u>	<u>866</u>	<u>51,806</u>
<b>Representing:</b>						
Cost	2,815	570	47,555	50,940	–	50,940
Valuation	–	–	–	–	866	866
	<u>2,815</u>	<u>570</u>	<u>47,555</u>	<u>50,940</u>	<u>866</u>	<u>51,806</u>
<b>Accumulated depreciation:</b>						
At 1 January 2018	951	229	6,776	7,956	–	7,956
Charge for the period (note 8)	62	52	988	1,102	–	1,102
Impairment (note 10)	–	–	346	346	–	346
Transferred to assets classified as assets held for sale	–	–	(42)	(42)	–	(42)
Attributable to assets sold or written off	(2)	(32)	(43)	(77)	–	(77)
At 30 June 2018	<u>1,011</u>	<u>249</u>	<u>8,025</u>	<u>9,285</u>	<u>–</u>	<u>9,285</u>
<b>Net book value:</b>						
At 30 June 2018	<u>1,804</u>	<u>321</u>	<u>39,530</u>	<u>41,655</u>	<u>866</u>	<u>42,521</u>

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***18. Property, Plant and Equipment (continued)**

	<i>Buildings and leasehold land held for own use HK\$'M</i>	<i>Equipment, furniture &amp; fixtures HK\$'M</i>	<i>Operating lease assets HK\$'M</i>	<i>Sub-total HK\$'M</i>	<i>Investment properties HK\$'M</i>	<i>Total property, plant and equipment HK\$'M</i>
<b>Cost or valuation:</b>						
At 1 January 2017	2,959	458	41,689	45,106	958	46,064
Additions	161	185	12,854	13,200	–	13,200
Disposals and write-offs	(317)	(148)	(10,119)	(10,584)	–	(10,584)
Reclassifications	(23)	23	–	–	–	–
Fair value adjustments	–	–	–	–	(92)	(92)
At 31 December 2017	2,780	518	44,424	47,722	866	48,588
<b>Representing:</b>						
Cost	2,780	518	44,424	47,722	–	47,722
Valuation	–	–	–	–	866	866
	2,780	518	44,424	47,722	866	48,588
<b>Accumulated depreciation:</b>						
At 1 January 2017	942	237	5,414	6,593	–	6,593
Charge for the period	106	107	1,998	2,211	–	2,211
Impairment	–	–	572	572	–	572
Attributable to assets sold or written off	(97)	(115)	(1,208)	(1,420)	–	(1,420)
At 31 December 2017	951	229	6,776	7,956	–	7,956
<b>Net book value:</b>						
At 31 December 2017	1,829	289	37,648	39,766	866	40,632

**19. Other assets**

	<b>At 30 June 2018 HK\$'M</b>	<b>At 31 December 2017 HK\$'M</b>
Prepayments and accrued income	2,852	2,892
Sundry debtors	3,010	2,913
Acceptances and endorsements	2,176	3,047
Unsettled trades and others	6,178	4,449
Assets held for sale <sup>1</sup>	1,069	1,957
	<b>15,285</b>	<b>15,258</b>

<sup>1</sup> As of 30 June 2018, assets held for sale included commercial aircraft. As of 31 December 2017, assets held for sale included the Group's interest in Asia Commercial Joint Stock Bank which was subsequently sold on 9 January 2018.

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***20. Investments in subsidiaries**

The principal subsidiaries of the Bank are Standard Chartered Leasing Group Limited, Standard Chartered Securities (Hong Kong) Limited and Standard Chartered Trade Support (HK) Limited.

**21. Deposits from customers**

	<i>At 30 June 2018 HK\$'M</i>	<i>At 31 December 2017 HK\$'M</i>
Current accounts	<b>178,348</b>	165,554
Savings accounts	<b>458,234</b>	484,275
Time, call and notice deposits	<b>239,714</b>	177,029
Deposits and balances of central banks	<b>1,994</b>	7,041
	<b>878,290</b>	833,899

**22. Financial liabilities at fair value through profit or loss**

	<i>At 30 June 2018 HK\$'M</i>	<i>At 31 December 2017 HK\$'M</i>
Trading liabilities	<b>14,338</b>	8,301
Financial liabilities designated at fair value through profit or loss:		
– Structured deposits from banks and customers	<b>4,860</b>	3,940
– Debt securities issued	<b>6,805</b>	7,534
	<b>11,665</b>	11,474
	<b>26,003</b>	19,775

**23. Debt securities in issue**

	<i>At 30 June 2018 HK\$'M</i>	<i>At 31 December 2017 HK\$'M</i>
Certificates of deposit	<b>2,343</b>	1,870
Senior debt securities	<b>1,182</b>	1,196
	<b>3,525</b>	3,066

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***24. Other liabilities**

	<i>At 30 June 2018 HK\$'M</i>	<i>At 31 December 2017 HK\$'M</i>
Accruals and deferred income	4,061	4,086
Provision for liabilities and charges	147	129
Expected credit loss provision on loan commitments and financial guarantees (note 16)	70	–
Acceptances and endorsements	2,176	3,047
Unsettled trades and others	18,341	14,030
	<u>24,795</u>	<u>21,292</u>

**25. Subordinated liabilities**

	<i>At 30 June 2018 HK\$'M</i>	<i>At 31 December 2017 HK\$'M</i>
US\$750 million 5.875% Fixed Rate Notes 2020	5,923	6,003

Subordinated liabilities are unsecured and subordinated to the claims of other creditors with an interest rate of 5.875 per cent per annum, payable semi-annually, to the maturity date on 24 June 2020.

**26. Shareholders' equity**

The Hong Kong Monetary Authority ("HKMA") requires the Bank and its subsidiaries to maintain a minimum level of impairment allowance for advances to customers which is in excess of the expected credit loss provision required under Hong Kong Financial Reporting Standards. Of the retained earnings as at 30 June 2018 an amount of HK\$4,228 million (31 December 2017: HK\$5,145 million) has been reserved for this purpose.

**27. Off-balance sheet exposures, capital commitments and contingencies****(a) Contingent liabilities and commitments**

	<i>At 30 June 2018 HK\$'M</i>	<i>At 31 December 2017 HK\$'M</i>
<u>Contractual or notional amounts</u>		
Direct credit substitutes	8,073	6,919
Transaction-related contingencies	8,002	7,341
Trade-related contingencies	10,132	10,560
Forward asset purchases	198	197
Forward forward deposits placed	1,025	1,527
Other commitments:		
which are not unconditionally cancellable:		
with original maturity of not more than one year	476	1,178
with original maturity of more than one year	26,205	27,827
which are unconditionally cancellable	351,095	321,564
	<u>405,206</u>	<u>377,113</u>
Credit risk weighted amount	<u>32,897</u>	<u>33,013</u>

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***27. Off-balance sheet exposures, capital commitments and contingencies (continued)****(a) Contingent liabilities and commitments (continued)**

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

**(b) Derivatives**

	<i>At 30 June 2018 HK\$'M</i>	<i>At 31 December 2017 HK\$'M</i>
<u>Notional amounts</u>		
Exchange rate contracts	3,477,487	2,833,192
Interest rate contracts	440,645	336,595
Others	33,329	35,609
	<u>3,951,461</u>	<u>3,205,396</u>

Derivatives are financial instruments that derive their value with reference to changes in interest or exchange rates, credit risk, financial instrument prices and indices. The notional amounts of these instruments indicate the volume of transactions outstanding and do not represent amounts at risk.

Fair values and credit risk weighted amounts of derivatives

	<i>At 30 June 2018</i>			<i>At 31 December 2017</i>		
	<i>Fair value assets HK\$'M</i>	<i>Fair value liabilities HK\$'M</i>	<i>Credit risk weighted amount HK\$'M</i>	<i>Fair value assets HK\$'M</i>	<i>Fair value liabilities HK\$'M</i>	<i>Credit risk weighted amount HK\$'M</i>
Exchange rate contracts	19,650	20,324	6,480	21,577	22,415	4,420
Interest rate contracts	2,881	2,966	1,391	2,439	2,321	1,163
Others	652	1,418	1,068	697	2,318	969
	<u>23,183</u>	<u>24,708</u>	<u>8,939</u>	<u>24,713</u>	<u>27,054</u>	<u>6,552</u>

The credit risk weighted amount refers to the amount as calculated in accordance with the Banking (Capital) Rules of the Hong Kong Banking Ordinance. The amount calculated is dependent upon the status of the counterparty and maturity characteristics of each type of contract.



**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***27. Off-balance sheet exposures, capital commitments and contingencies (continued)****(c) Capital commitment**

Capital commitments in respect of property, plant and equipment purchases not provided for in the consolidated financial statements were as follows:

	<i>At 30 June 2018 HK\$'M</i>	<i>At 31 December 2017 HK\$'M</i>
Contracted for	<b>1,977</b>	3,640
Authorised but not contracted for	<b>127</b>	41
	<b>2,104</b>	3,681

**(d) Contingencies**

The Group receives legal claims against it arising in the normal course of business. The Group considers none of these matters as material. Where appropriate the Group recognises a provision for liabilities when it is probable that an outflow of economic resources embodying economic benefits will be required and for which a reliable estimate can be made of the obligation.

The Securities and Futures Commission ("SFC") in Hong Kong has been investigating Standard Chartered Securities (Hong Kong) Limited's ("SCSHK") role as a joint sponsor of an initial public offering of a company listed on the Stock Exchange of Hong Kong in 2009. The SFC is pursuing disciplinary action against SCSHK, and there may be financial consequences for SCSHK in connection with this action.

**28. Material related-party transactions**

There were no significant changes to the nature of the related party transactions described in the 2017 consolidated financial statements that have a material effect on the financial position or performance of the Group during the six months ended 30 June 2018. All related party transactions that took place in the six months ended 30 June 2018 were similar in nature to those disclosed in the 2017 consolidated financial statements.

**29. Ultimate and immediate holding company**

The Bank's ultimate holding company is Standard Chartered PLC ("SCPLC"), a company registered in England and Wales. SCPLC has listings on the London Stock Exchange and the Stock Exchange of Hong Kong. In addition, SCPLC is also listed on the Bombay and National Stock Exchanges of India in the form of Indian Depository Receipts.

The Group's immediate holding company is Standard Chartered Bank, a company registered in England and Wales.

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***30. Currency risk**

The Group had the following non-structural foreign currency positions which exceeded 10% of the net non-structural position in all foreign currencies. The net option position is calculated on the basis of the delta-weighted positions of all foreign exchange option contracts.

	<i>At</i> <b>30 June</b> <i>2018</i> <b>HK\$'M</b>	<i>At</i> <i>31 December</i> <i>2017</i> <b>HK\$'M</b>
<b>US dollars exposure</b>		
Spot assets	<b>379,208</b>	339,429
Spot liabilities	<b>(372,624)</b>	(328,208)
Forward purchases	<b>1,693,571</b>	1,378,261
Forward sales	<b>(1,696,274)</b>	(1,385,414)
	<u><b>3,881</b></u>	<u>4,068</u>
Net long non-structural position	<u><b>3,881</b></u>	<u>4,068</u>
<b>Chinese Renminbi exposure</b>		
Spot assets	<b>46,580</b>	53,737
Spot liabilities	<b>(57,536)</b>	(45,149)
Forward purchases	<b>663,253</b>	581,943
Forward sales	<b>(652,847)</b>	(590,659)
	<u><b>(550)</b></u>	<u>(128)</u>
Net short non-structural position	<u><b>(550)</b></u>	<u>(128)</u>

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

	<i>At</i> <b>30 June</b> <i>2018</i> <b>HK\$'M</b>	<i>At</i> <i>31 December</i> <i>2017</i> <b>HK\$'M</b>
Chinese Renminbi	<b>12,095</b>	11,639
US dollars	<b>2,314</b>	3,263
	<u><b>14,409</b></u>	<u>14,902</u>

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***31. Financial instruments****(a) Valuation of financial instruments carried at fair value**

Valuation of financial assets and liabilities held at fair value are subject to a review independent of the business by Valuation Control. For those financial assets and liabilities whose fair value is determined by reference to externally quoted prices or market observable pricing inputs to valuation models, an assessment is made against external market data and consensus services. Financial instruments held at fair value in the condensed consolidated statement of financial position have been classified into a valuation hierarchy that reflects the significance of the inputs used in the fair value measurements.

**Valuation methodologies**

The valuation hierarchy is set out below:

	Level 1	Level 2	Level 3
Fair value determined using:	Unadjusted quoted price in an active market for identical assets and liabilities	Directly or indirectly observable inputs other than unadjusted quoted prices included within Level 1 that are observable <sup>1</sup>	Significant inputs for the asset or liability that are not based on observable market data (unobservable inputs) (see note 31 (a) (i))

<sup>1</sup> These included valuation models such as discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants. These models incorporate assumptions and inputs that other market participants would use in their valuations, such as discount rates, default rates, credit spreads and option volatilities. These inputs need to be directly or indirectly observable in order to be classified as level 2.

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***31. Financial instruments (continued)****(a) Valuation of financial instruments carried at fair value (continued)**

The tables below show the classification of financial instruments held at fair value into the valuation hierarchy set out above:

	<i>At 30 June 2018</i>			
	<i>Level 1 HK\$'M</i>	<i>Level 2 HK\$'M</i>	<i>Level 3 HK\$'M</i>	<i>Total HK\$'M</i>
Financial assets at fair value through profit or loss:				
– Trading assets				
– Debt securities	8,225	11,635	304	20,164
– Advances to customers	–	1,260	267	1,527
– Positive fair values of derivatives	1	3,059	–	3,060
– Equity shares	3	–	–	3
– Non-trading financial assets mandatorily at fair value through profit or loss:				
– Debt securities	–	283	1,068	1,351
– Advances to customers	–	1,662	3,169	4,831
– Equity shares	–	–	462	462
Amounts due from immediate holding company				
– Positive fair values of derivatives	55	18,282	–	18,337
Amounts due from fellow subsidiaries				
– Positive fair values of derivatives	1	1,785	–	1,786
Investment securities at fair value through other comprehensive income				
– Treasury bills	111,516	4,284	–	115,800
– Certificates of deposit held	–	20,551	–	20,551
– Debt securities	31,933	68,279	–	100,212
– Equity shares	–	–	227	227
<b>Total assets measured at fair value</b>	<b>151,734</b>	<b>131,080</b>	<b>5,497</b>	<b>288,311</b>
Financial liabilities at fair value through profit or loss:				
– Trading liabilities				
– Short positions in securities	7,305	3,528	–	10,833
– Negative fair values of derivatives	6	3,499	–	3,505
– Financial liabilities designated at fair value				
– Structured bank and customer deposits	–	4,860	–	4,860
– Debt securities issued	–	5,856	949	6,805
Amounts due to immediate holding company				
– Negative fair values of derivatives	36	20,259	–	20,295
Amounts due to fellow subsidiaries				
– Negative fair values of derivatives	1	907	–	908
<b>Total liabilities measured at fair value</b>	<b>7,348</b>	<b>38,909</b>	<b>949</b>	<b>47,206</b>

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***31. Financial instruments (continued)****(a) Valuation of financial instruments carried at fair value (continued)**

	At 31 December 2017			Total
	Level 1	Level 2	Level 3	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Financial assets at fair value through profit or loss:				
– Trading assets				
– Debt securities	8,045	10,573	24	18,642
– Advances to customers	–	2,649	–	2,649
– Positive fair values of derivatives	1	1,191	–	1,192
– Financial assets designated at fair value through profit or loss				
– Debt securities	–	336	–	336
Amounts due from immediate holding company				
– Positive fair values of derivatives	44	22,765	–	22,809
– Debt securities	–	7	–	7
Amounts due from fellow subsidiaries				
– Positive fair values of derivatives	–	712	–	712
Available-for-sale securities				
– Treasury bills	86,608	–	–	86,608
– Certificates of deposit held	37	19,341	–	19,378
– Debt securities	36,843	59,347	–	96,190
– Equity shares	–	–	701	701
<b>Total assets measured at fair value</b>	<b>131,578</b>	<b>116,921</b>	<b>725</b>	<b>249,224</b>
Financial liabilities at fair value through profit or loss:				
– Trading liabilities				
– Short positions in securities	3,274	2,539	–	5,813
– Negative fair values of derivatives	3	2,485	–	2,488
– Financial liabilities designated at fair value through profit or loss				
– Structured bank and customer deposits	–	3,940	–	3,940
– Debt securities issued	–	6,370	1,164	7,534
Amounts due to immediate holding company				
– Negative fair values of derivatives	32	23,543	–	23,575
Amounts due to fellow subsidiaries				
– Negative fair values of derivatives	2	989	–	991
<b>Total liabilities measured at fair value</b>	<b>3,311</b>	<b>39,866</b>	<b>1,164</b>	<b>44,341</b>

There were no significant transfers between level 1 and level 2 instruments during 2017 and 2018.

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***31. Financial instruments (continued)****(a) Valuation of financial instruments carried at fair value (continued)**

## (i) Valuation of financial instruments with significant unobservable inputs

The movements during the period for level 3 financial assets and liabilities are as follows:

*Financial assets*

	<i>Financial assets at fair value through profit or loss HK\$'M</i>	<i>Available- for-sales securities/ Financial assets at fair value through other comprehensive income HK\$'M</i>	<i>Total level 3 assets HK\$'M</i>
At 31 December 2017 – HKAS 39/IAS 39	24	701	725
Impact of adoption of HKFRS 9/IFRS 9			
– reclassification to fair value through profit or loss	4,456	(474)	3,982
– re-measurement	87	–	87
	<hr/>	<hr/>	<hr/>
At 1 January 2018 – HKFRS 9/IFRS 9	4,567	227	4,794
Total losses recognised in the income statement			
– Net trading income	(27)	–	(27)
Purchases	1,569	–	1,569
Sales	(312)	–	(312)
Settlements	(370)	–	(370)
Transferred into level 3 <sup>1</sup>	2	–	2
Transferred out of level 3 <sup>1</sup>	(159)	–	(159)
	<hr/>	<hr/>	<hr/>
At 30 June 2018	5,270	227	5,497
	<hr/>	<hr/>	<hr/>
Total losses recognised in the income statement relating to assets held at 30 June 2018			
– Net trading income	(16)	–	(16)
	<hr/>	<hr/>	<hr/>

<sup>1</sup> Transfers into/(out of) level 3 during the period relate to financial instruments where the valuation parameters became unobservable/(observable) during the period.

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***31. Financial instruments (continued)****(a) Valuation of financial instruments carried at fair value (continued)**

## (i) Valuation of financial instruments with significant unobservable inputs (continued)

*Financial liabilities*

	<i>Financial liabilities designated at fair value through profit or loss HK\$'M</i>	<i>Total level 3 liabilities HK\$'M</i>
At 1 January 2018	<b>1,164</b>	<b>1,164</b>
Total gains recognised in the income statement		
– Net trading income	<b>(10)</b>	<b>(10)</b>
Settlements	<b>(205)</b>	<b>(205)</b>
At 30 June 2018	<b>949</b>	<b>949</b>
Total gains recognised in the income statement relating to liabilities held at 30 June 2018		
– Net trading income	<b>(9)</b>	<b>(9)</b>

*Financial assets*

	<i>Financial assets at fair value through profit or loss HK\$'M</i>	<i>Amounts due from immediate holding company HK\$'M</i>	<i>Available-for-sale securities HK\$'M</i>	<i>Total level 3 assets HK\$'M</i>
At 1 January 2017	–	24	487	511
Total gains recognised in the income statement				
– Net trading income	–	20	–	20
Sales	–	–	(32)	(32)
Total gains recognised in the available-for-sale investment reserve	–	–	258	258
Purchases	24	–	8	32
Settlements	–	(44)	(20)	(64)
At 31 December 2017	<b>24</b>	<b>–</b>	<b>701</b>	<b>725</b>
Total gains recognised in the income statement relating to assets held at 31 December 2017				
– Net trading income	<b>–</b>	<b>20</b>	<b>–</b>	<b>20</b>

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***31. Financial instruments (continued)****(a) Valuation of financial instruments carried at fair value (continued)****(i) Valuation of financial instruments with significant unobservable inputs (continued)***Financial liabilities*

	<i>Financial liabilities designated at fair value through profit or loss</i>	<i>Total level 3 liabilities</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
At 1 January 2017	1,686	1,686
Total gains recognised in the income statement		
– Net trading income	(48)	(48)
Issuances	1,224	1,224
Settlements	(1,698)	(1,698)
	<hr/>	<hr/>
At 31 December 2017	<u>1,164</u>	<u>1,164</u>
Total gains recognised in the income statement relating to liabilities held at 31 December 2017		
– Net trading income	(48)	(48)
	<hr/>	<hr/>

The following table presents the key valuation techniques used to measure the fair value of level 3 financial instruments which are held at fair value, the significant unobservable inputs and the range of values for those inputs and the weighted average of those inputs.

<u>Type of instruments<sup>3</sup></u>	<u>Principal valuation technique</u>	<u>Significant unobservable inputs</u>	<u>Range<sup>1</sup></u>	<u>Weighted average<sup>2</sup></u>
Debt securities	Discounted cash flows	Price/Yield	1.0% to 4.5% (2017: 5%)	4.1% (2017: 5%)
Advances to customers	Discounted cash flows	Recovery rates	91.64% to 97.15% (2017: nil)	96.01% (2017: nil)
Debt securities in issue	Discounted cash flows	Credit spreads	1.3% to 4.0% (2017: 0.9% to 4.0%)	2.8% (2017: 2.6%)

<sup>1</sup> The ranges of values shown represent the highest and lowest levels used in the valuation of the level 3 financial instruments as at 30 June 2018 and 31 December 2017. The ranges of values used are reflective of the underlying characteristics of these level 3 financial instruments based on the market conditions at the reporting date. However, these ranges of values may not represent the uncertainty in fair value measurements of these level 3 financial instruments.

<sup>2</sup> Weighted average for non-derivative financial instruments have been calculated by weighting inputs by the relative fair value.

<sup>3</sup> There are certain level 3 equity shares, which are mainly measured using unadjusted net asset value, which are excluded from this table.



**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***31. Financial instruments (continued)****(a) Valuation of financial instruments carried at fair value (continued)****(i) Valuation of financial instruments with significant unobservable inputs (continued)**

The following section describes the significant unobservable inputs identified in the above valuation technique table.

*Yield*

Yield is the interest rate that is used to discount the future cash flows in a discounted cash flow model. An increase in the yield, in isolation, would result in a decrease in a fair value measurement.

*Recovery rates*

Recovery rates are the expectation of the rate of recovery resulting from the liquidation of a particular loan. As the probability of default increases for a given instrument, the valuation of that instrument will increasingly reflect its expected recovery level assuming default. An increase in the recovery rate, in isolation, would result in a favourable movement in the fair value of the loan.

*Credit spreads*

Credit spreads represent the additional yield that a market participant would demand for taking exposures to the credit risk of an instrument.

**(ii) Sensitivities in respect of the fair values of level 3 assets and liabilities**

Where the fair value of financial instruments are measured using valuation techniques that incorporate one or more significant inputs which are based on unobservable market data, we apply a 10 per cent increase or decrease on the values of these unobservable parameter inputs, to generate a range of reasonably possible alternative valuations in accordance with the requirements of HKFRS 7/IFRS 7, Financial Instruments: Disclosures. The percentage shift is determined by statistical analysis performed on a set of reference prices, which included certain equity indices, credit indices and volatility indices, based on the composition of our level 3 financial instruments. Favourable and unfavourable changes are determined on the basis of changes in the value of the instrument as a result of varying the levels of the unobservable parameters. This level 3 sensitivity analysis assumes a one way market move and does not consider offsets for hedges.

	<i>At 30 June 2018</i>					
	<i>Held at fair value through profit or loss</i>			<i>Held at fair value through other comprehensive income</i>		
	<i>Net exposure HK\$'M</i>	<i>Favourable changes HK\$'M</i>	<i>Unfavourable changes HK\$'M</i>	<i>Net exposure HK\$'M</i>	<i>Favourable changes HK\$'M</i>	<i>Unfavourable changes HK\$'M</i>
Debt securities	1,372	1,436	1,318	-	-	-
Advances to customers	3,436	3,483	3,396	-	-	-
Equity shares	462	508	416	227	250	204
Debt securities issued	(949)	(885)	(967)	-	-	-
	<u>4,321</u>	<u>4,542</u>	<u>4,163</u>	<u>227</u>	<u>250</u>	<u>204</u>

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***31. Financial instruments (continued)****(a) Valuation of financial instruments carried at fair value (continued)**

(ii) Sensitivities in respect of the fair values of level 3 assets and liabilities (continued)

	At 31 December 2017					
	Held at fair value through profit or loss			Available-for-sale securities		
	Net exposure HK\$'M	Favourable changes HK\$'M	Unfavourable changes HK\$'M	Net exposure HK\$'M	Favourable changes HK\$'M	Unfavourable changes HK\$'M
Debt securities	24	25	23	-	-	-
Equity securities	-	-	-	701	771	631
Debt securities issued	(1,164)	(1,088)	(1,180)	-	-	-
	<u>(1,140)</u>	<u>(1,063)</u>	<u>(1,157)</u>	<u>701</u>	<u>771</u>	<u>631</u>

These reasonably possible alternatives could have increased or decreased the values of financial instruments held at fair value through profit or loss and those classified as fair value through other comprehensive income/available-for-sale by the amounts disclosed below.

Financial instruments	Fair value changes	At 30 June 2018	At 31 December 2017
		HK\$'M	HK\$'M
Held at fair value through profit or loss	Possible increase	221	77
	Possible decrease	158	17
Held at fair value through other comprehensive income/Available-for-sale	Possible increase	23	70
	Possible decrease	23	70

**(b) Valuation of financial instruments carried at amortised cost**

All financial instruments are stated at fair value or amounts not materially different from their fair value as at 30 June 2018 and 31 December 2017, except for subordinated liabilities.

The following table summarises the carrying amounts and fair values (including the valuation hierarchy) of subordinated liabilities. The values in the table below are stated as at 30 June 2018 and 31 December 2017 and may be different from the actual amounts that will be received on the settlement or maturity of the subordinated liabilities.

	At 30 June 2018			At 31 December 2017		
	Carrying amount	Fair value Level 1	Fair value Level 2	Carrying amount	Fair value Level 1	Fair value Level 2
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Subordinated liabilities – US\$750 million						
5.875% Fixed Rate Notes 2020	<u>5,923</u>	<u>6,136</u>	<u>-</u>	<u>6,003</u>	<u>6,263</u>	<u>-</u>
Subordinated liabilities – US\$800 million						
4.30% Fixed Rate debt 2026 (included in “amounts due to immediate holding company”)	<u>6,277</u>	<u>-</u>	<u>6,280</u>	<u>6,252</u>	<u>-</u>	<u>6,316</u>

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 31. Financial instruments (continued)

#### (b) Valuation of financial instruments carried at amortised cost (continued)

The basis for establishing the fair value of financial instruments that are not carried at fair value is set out in note 38(b) to the 2017 consolidated financial statements of the Group.

### 32. Share based payments

SCPLC operates a number of share-based arrangements in which the Group's employees participate.

#### 2011 Standard Chartered Share Plan ("the 2011 Plan")

The 2011 Plan was approved by SCPLC's shareholders in May 2011 and is the SCPLC's main plan. Since approval, it has been used to deliver various types of share awards:

- Long-term Incentive plan ("LTIP") awards: granted with vesting subject to performance measures. Performance measures attached to awards granted previously include: total shareholder return ("TSR"); return on equity ("RoE") with a Common Equity Tier 1 ("CET1") underpin; strategic measures; earnings per share ("EPS") growth; and return on risk-weighted assets ("RoRWA"). Each measure is assessed independently over a three-year period. Awards granted from 2016 have an individual conduct gateway requirement that results in the award lapsing if not met.
- Deferred awards are used to deliver the deferred portion of variable remuneration, in line with both market practice and regulatory requirements. These awards vest in instalments on anniversaries of the award specified at the time of grant. Deferred awards are not subject to any plan limit. This enables the SCPLC to meet regulatory requirements relating to deferral levels, and is in line with market practice.
- Restricted share awards, made outside of the annual performance process as replacement buy-out awards to new joiners who forfeit awards on leaving their previous employers vest on anniversaries of the award date specified at the time of grant. In line with similar plans operated by our competitors, restricted share awards are not subject to an annual limit and do not have any performance measures.
- Underpin shares are subject to a combination of two performance measures: EPS growth and RoRWA. The weighting between the two elements is split equally, one half of the award depending on each measure, assessed independently. These awards vest after three or five years. Underpin shares formed part of the variable remuneration awarded to executive directors and senior management in respect of 2014 performance.

Under the 2011 Plan, no grant is payable to receive an award. The remaining life of the 2011 Plan during which new awards can be made is four years.

## Notes to condensed consolidated interim financial statements (unaudited)

(Expressed in millions of Hong Kong dollars)

### 32. Share based payments (continued)

#### **2001 Performance Share Plan (“2001 PSP”)**

The SCPLC’s previous plan for delivering performance shares was the 2001 PSP and there remain outstanding vested awards. Under the 2001 PSP, half the award was dependent upon TSR performance and the balance was subject to a target of defined EPS growth. Both measures used the same three-year period and were assessed independently. No further awards will be granted under 2001 PSP.

#### **2006 Restricted Share Scheme (“2006 RSS”)/2007 Supplementary Restricted Share Scheme (“2007 SRSS”)**

The SCPLC’s previous plans for delivering restricted shares were the 2006 RSS and 2007 SRSS both now replaced by the 2011 Plan. There remain outstanding vested awards under these plans. Awards were generally in the form of nil cost options and did not have any performance measures. Generally deferred restricted share awards vested equally over three years and for non-deferred awards half vested two years after the date of grant and the balance after three years. No further awards will be granted under the 2006 RSS and 2007 SRSS.

#### **All Employee Sharesave Plans (comprised of the “2004 International Sharesave Plan”, the “2004 UK Sharesave Plan” and the “2013 Sharesave Plan”)**

Under the All Employee Sharesave Plans, employees may open a savings contract. Within a period of six months after the third anniversary, as appropriate, employees may purchase ordinary shares in SCPLC at a discount of up to 20 per cent on the share price at the date of invitation (this is known as the “option exercise price”). There are no performance measures attached to options granted under the All Employee Sharesave Plans and no grant price is payable to receive an option. In some countries in which the SCPLC operates, it is not possible to operate Sharesave plans, typically due to securities law and regulatory restrictions. In these countries the SCPLC offers an equivalent cash-based plan to its employees. The 2004 International Sharesave and the 2004 UK Sharesave plans are now closed and no further awards will be granted under these plans.

The 2013 Sharesave Plan was approved by SCPLC’s shareholders in May 2013 and all future Sharesave invitations are made under this plan. The remaining life of the 2013 Sharesave Plan is five years.

#### **Valuation of share awards**

Details of the valuation models used in determining the fair values of share awards granted under the SCPLC’s share plans are detailed in the Group’s consolidated financial statement for the year ended 31 December 2017.

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***32. Share based payments (continued)****Reconciliation of share award movements for the period to 30 June 2018**

	<u>2011 Plan</u>					<i>Weighted average Sharesave exercise price (£)</i>
	<i>LTIP</i>	<i>Deferred/ Restricted shares</i>	<i>PSP</i>	<i>RSS</i>	<i>2013 Sharesave</i>	
Outstanding at 1 January 2018	2,431,307	3,100,042	7,629	15,815	981,765	5.86
Granted	91,349	1,248,508	–	–	–	–
Notional dividend	23,113	20,825	–	–	–	–
Lapsed	–	(41,219)	–	(1,910)	(114,260)	7.47
Exercised	–	(1,041,900)	(1,825)	(13,905)	(4,747)	5.56
Outstanding at 30 June 2018	<u>2,545,769</u>	<u>3,286,256</u>	<u>5,804</u>	<u>–</u>	<u>862,758</u>	<u>5.65</u>
Exercisable at 30 June 2018	<u>–</u>	<u>617,143</u>	<u>5,804</u>	<u>–</u>	<u>5,783</u>	<u>5.85</u>
Range of exercise prices (£)	<u>–</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>5.30-9.38</u>	
Weighted average contractual remaining life (years)	<u>7.81</u>	<u>8.35</u>	<u>3.18</u>	<u>–</u>	<u>1.48</u>	

**33. New accounting standards in issue but not effective*****HKFRS 16/IFRS 16 Leases***

The effective date of HKFRS 16/IFRS 16 is 1 January 2019. HKFRS 16/IFRS 16 introduces a single lessee accounting model and requires a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognise a right-of-use asset representing its right to use the underlying leased asset and a lease liability representing its obligation to make lease payments. HKFRS 16/IFRS 16 substantially carries forward the lessor accounting requirements in HKAS 17/IAS 17 Leases. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently.

***Update on implementation***

The work to assess the impact of the standard is ongoing and it is not yet practicable to quantify the effect of HKFRS 16/IFRS 16 on these consolidated financial statements. The Group will have a balance sheet increase in lease liabilities and right-of-use assets on adoption of HKFRS 16/IFRS 16.

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***34. Impact of Transition to HKFRS 9/IFRS 9 Financial Instruments on 1 January 2018****(a) Impact of HKFRS 9/IFRS 9 on Shareholders' Equity**

The impact of transition to HKFRS 9/IFRS 9 in respect of classification and measurement; adoption of the expected credit loss provision ("ECL") methodology; share of impact from associate; and related tax effects are set out by category of reserve in the table below.

	Share capital	Own credit adjustment reserve	Available-for-sale reserve	FVOCI reserve - Debt	FVOCI reserve - Equity	Exchange reserve	Cash flow hedge reserve	Retained earnings	Share option reserve	Capital contribution reserve	Other equity instruments	Total
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
As at 31 December 2017	20,256	(18)	(23)	-	-	266	18	51,622	318	37	1,952	74,428
Impact of changes in classification and measurement:												
- reclassifications <sup>1</sup>	-	-	23	(319)	161	-	-	135	-	-	-	-
- re-measurements <sup>2</sup>	-	-	-	-	-	-	-	87	-	-	-	87
	-	-	23	(319)	161	-	-	222	-	-	-	87
Impact of adoption of expected credit loss provision <sup>3</sup>	-	-	-	14	-	-	-	(743)	-	-	-	(729)
Impact of HKFRS 9/IFRS 9 on share of associate	-	-	-	(10)	-	-	-	(90)	-	-	-	(100)
Related tax effects	-	-	-	-	-	-	-	109	-	-	-	109
Total impact of HKFRS 9/IFRS 9 transition	-	-	23	(315)	161	-	-	(502)	-	-	-	(633)
As at 1 January 2018	20,256	(18)	-	(315)	161	266	18	51,120	318	37	1,952	73,795

<sup>1</sup> Available-for-sale category has been removed under HKFRS 9/IFRS 9. Unrealised gains and losses have been transferred to fair value through other comprehensive income ("FVOCI") reserves where the instruments are held as FVOCI, or retained earnings where the instruments are held at fair value through profit or loss ("FVTPL"). The Group has elected to hold HK\$ 227 million of equity instruments at FVOCI. These principally relate to investments held for strategic purposes, including investments in industry utilities. Fair value gains and losses arising on these investments are held within the FVOCI reserve - equity, and are never recycled to the income statement. Only dividend income received is reported in the income statement.

<sup>2</sup> Represents the re-measurement impact of financial assets that are now measured at fair value under HKFRS 9/IFRS 9.

<sup>3</sup> The impact from adopting expected credit losses on retained earnings was HK\$743 million (see note 34(c) for further details). As FVOCI debt instruments are held at fair value on the balance sheet, the expected credit loss charged to retained earnings is recognised as a credit to the FVOCI reserve. The FVOCI reserve relating to FVOCI debt instruments will be recycled to the income statement on disposal of the instruments.

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***34. Impact of Transition to HKFRS 9/IFRS 9 Financial Instruments on 1 January 2018 (continued)****(b) Impact of HKFRS 9/IFRS 9 on consolidated statement of financial position as of 1 January 2018**

The table below sets out the impact of adopting HKFRS 9/IFRS 9 on the Group's consolidated statement of financial position as of 1 January 2018.

	<i>HKAS 39/IAS 39</i> 31 December 2017 HK\$'M	<i>Classification &amp;</i> <i>measurement</i> <sup>1</sup> HK\$'M	<i>Expected credit</i> <i>losses</i> <sup>2</sup> HK\$'M	<i>Other impacts</i> <sup>3</sup> HK\$'M	<i>HKFRS 9/IFRS 9</i> 1 January 2018 HK\$'M
Cash and balances at banks, central banks and other financial institutions	18,350	-	-	-	18,350
Placements with banks and other financial institutions	150,256	-	(7)	-	150,249
Hong Kong SAR Government certificates of indebtedness	42,341	-	-	-	42,341
Financial assets at fair value through profit or loss	22,819	4,543	-	-	27,362
Investment securities	207,927	(1,569)	(11)	-	206,347
Advances to customers	480,867	(2,887)	(623)	-	477,357
Amounts due from immediate holding company	59,075	-	-	-	59,075
Amounts due from fellow subsidiaries	24,208	-	-	-	24,208
Interest in associate	11,638	-	-	(100)	11,538
Property, plant and equipment	40,632	-	-	-	40,632
Goodwill and intangible assets	1,392	-	-	-	1,392
Current tax assets	11	-	-	-	11
Deferred tax assets	275	-	-	92	367
Other assets	15,258	-	-	-	15,258
	<u>1,075,049</u>	<u>87</u>	<u>(641)</u>	<u>(8)</u>	<u>1,074,487</u>

**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***34. Impact of Transition to HKFRS 9/IFRS 9 Financial Instruments on 1 January 2018 (continued)****(b) Impact of HKFRS 9/IFRS 9 on consolidated statement of financial position as of 1 January 2018 (continued)**

	HKAS 39/IAS 39 31 December 2017 HK\$'M	Classification & measurement <sup>1</sup> HK\$'M	Expected credit losses <sup>2</sup> HK\$'M	Other impacts <sup>3</sup> HK\$'M	HKFRS 9/IFRS 9 1 January 2018 HK\$'M
Hong Kong SAR currency notes in circulation	42,341	-	-	-	42,341
Deposits and balances of banks and other financial institutions	19,613	-	-	-	19,613
Deposits from customers	833,899	-	-	-	833,899
Financial liabilities at fair value through profit or loss	19,775	-	-	-	19,775
Debt securities in issue	3,066	-	-	-	3,066
Amounts due to immediate holding company	44,246	-	-	-	44,246
Amounts due to fellow subsidiaries	9,477	-	-	-	9,477
Current tax liabilities	439	-	-	(17)	422
Deferred tax liabilities	470	-	-	-	470
Other liabilities	21,292	-	88	-	21,380
Subordinated liabilities	6,003	-	-	-	6,003
	<u>1,000,621</u>	<u>-</u>	<u>88</u>	<u>(17)</u>	<u>1,000,692</u>
Share capital	20,256	-	-	-	20,256
Reserves	52,220	87	(729)	9	51,587
<b>Shareholders' equity</b>	<u>72,476</u>	<u>87</u>	<u>(729)</u>	<u>9</u>	<u>71,843</u>
Other equity instruments	1,952	-	-	-	1,952
	<u>74,428</u>	<u>87</u>	<u>(729)</u>	<u>9</u>	<u>73,795</u>
	<u>1,075,049</u>	<u>87</u>	<u>(641)</u>	<u>(8)</u>	<u>1,074,487</u>

<sup>1</sup> Classification and measurement reclassifications primarily relate to the following:

- a small number of products in Retail Banking and a small number of contracts within the corporate lending portfolios that do not meet the SPPI criteria have been de-designated from an amortised cost basis and recognised as FVTPL.
- a small portfolio of strategic equity instruments which are irrevocably designated at FVOCI.
- certain equity and debt securities classified as loan and receivables under HKAS 39/IAS 39 have been de-designated and recognised as FVTPL as a result of business model assessment.

<sup>2</sup> Impact of additional expected credit loss provisions (see note 34 (a)).

<sup>3</sup> Includes the change in the Group's share of net assets from associate in adopting HKFRS 9/IFRS 9, and the related tax effect of the HKFRS 9/IFRS 9 adjustments.



**Notes to condensed consolidated interim financial statements (unaudited)***(Expressed in millions of Hong Kong dollars)***34. Impact of Transition to HKFRS 9/IFRS 9 Financial Instruments on 1 January 2018 (continued)****(c) Impact of expected credit losses**

The table sets out a comparison of impairment loss provisions under HKAS 39/IAS 39 to those under HKFRS 9/IFRS 9 as of 1 January 2018.

	<i>Impairment provision under HKAS 39/ IAS 39 HK\$'M (note 15(a))</i>	<i>Additional expected credit loss provision under HKFRS 9/ IFRS 9 HK\$'M (note 34(a))</i>	<i>Expected credit loss provision under HKFRS 9/ IFRS 9 HK\$'M (note 16)</i>
Provision on:			
– Placements with banks and other financial institutions	–	7	7
– Advances to customers	1,150	623	1,773
– Debt securities at amortised cost	–	11	11
– Debt securities at fair value through other comprehensive income	–	14	14
– Loan commitments and financial guarantees	–	88	88
	<u>1,150</u>	<u>743</u>	<u>1,893</u>

**35. Comparative figures**

Upon the adoption of HKFRS 9/IFRS 9, the following items are re-grouped on the consolidated income statement and the consolidated statement of financial position to align with the presentation of the Bank's ultimate holding company, SCPLC:–

- Net gains/losses from financial instruments designated or mandatorily at fair value through profit or loss are presented within “net trading income”
- Net gains/losses from disposal of financial instruments at FVOCI/available-for-sale securities are presented within “other operating income”
- Trading assets and financial assets designated or mandatorily at fair value through profit or losses are presented together as “financial assets at fair value through profit or loss”
- Trading liabilities and financial liabilities designated at fair value through profit or losses are presented together as “financial liabilities at fair value through profit or loss”

By order of the Board

Yee Mann Hau  
Executive Director and Chief Financial Officer

Hong Kong  
31 July 2018