

NOTES TO THE INTERIM FINANCIAL INFORMATION

1. Basis of preparation and significant accounting policies

(a) Basis of preparation

The unaudited interim financial information has been prepared in accordance with HKAS 34 “Interim Financial Reporting” issued by the HKICPA.

(b) Significant accounting policies

Except for the initial adoption of the below mentioned amendments, the significant accounting policies adopted and methods of computation used in the preparation of the unaudited interim financial information are consistent with those adopted and used in the Group’s annual financial statements for the year ended 31 December 2019 and shall be read in conjunction with the Group’s Annual Report for 2019.

Amendments that are relevant to the Group and are initially adopted for the financial year beginning on 1 January 2020

The Group has initially applied the following amendments for the financial year beginning on 1 January 2020:

- HKAS 39, HKFRS 7 and HKFRS 9 (Amendments), “Interest Rate Benchmark Reform”. The amendments modify certain specific hedge accounting requirements to provide temporary relief allowing the continuous use of hedge accounting under the uncertainties caused by interest rate benchmark reform (“IBOR reform”) on the cash flows of the hedge relationships. Pursuant to the amendments, the relief would deem to be ended at the earlier of (i) when there is no longer uncertainty arising from IBOR reform over the cash flows of the hedging relationships, and (ii) when the hedging relationship to which the relief applied is discontinued, or in case of cash flow hedges, when the entire amount accumulated in the cash flow hedge reserve with respect to the discontinued hedging relationship has been reclassified to profit or loss.

The amendments have been applied retrospectively. There is no material impact on the Group’s financial statements.

- HKFRS 16 (Amendments), “COVID-19-Related Rent Concessions”. The amendments provide a practical expedient that lessees are exempted from evaluating whether rent concessions occurring as a direct consequence of the COVID-19 pandemic are lease modifications and, instead, account for those rent concessions as if they were not lease modifications.

The amendments are effective on 1 June 2020 and applicable to COVID-19-related rent concessions that reduce lease payments from 1 January 2020 to 30 June 2021. The Group has elected to early adopt the amendments and applied the practical expedient to all qualifying COVID-19-related rent concessions granted to the Group during the interim reporting period. The adoption of the amendments does not have a material impact on the Group’s financial statements.

- HKAS 1 and HKAS 8 (Amendments), “Definition of Material”. The amendments clarify the definition of materiality of information and align the definition used across other accounting standards. The amendments have been applied prospectively. The application of the amendments does not have a material impact on the Group’s financial statements.
- HKFRS 3 (Amendments), “Definition of a Business”. The amendments clarify the definition of a business, with the objective of assisting entities to determine whether a business combination transaction should be accounted for as a business combination or as an asset acquisition. The amendments have been applied prospectively. The application of this amendments does not have a material impact on the Group’s financial statements.

NOTES TO THE INTERIM FINANCIAL INFORMATION

1. Basis of preparation and significant accounting policies (continued)

(c) *Standard and amendments issued that are relevant to the Group but not yet mandatorily effective and have not been early adopted by the Group in 2020*

Standard/ Amendments	Content	Applicable for financial years beginning on/after
HKAS 16 (Amendments)	Property, Plant and Equipment: Proceeds before Intended Use	1 January 2022
HKAS 28 (2011) and HKFRS 10 (Amendments)	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture	To be determined
HKAS 37 (Amendments)	Onerous Contracts – Cost of Fulfilling a Contract	1 January 2022
HKFRS 3 (Amendments)	Reference to the Conceptual Framework	1 January 2022
HKFRS 17	Insurance Contracts	1 January 2021

- HKAS 16 (Amendments), “Property, Plant and Equipment: Proceeds before Intended Use”. The amendments prohibit an entity from deducting from the cost of an item of property, plant and equipment the proceeds from selling items produced before that asset is available for use. The related sales proceeds together with the costs of providing these items as determined by HKAS 2, should be included in profit and loss. The amendments are applied retrospectively, but only to items of property, plant and equipment made available for use on or after the beginning of the earliest period presented in the financial statements in which the entity first applies the amendments. The application of the amendments will not have a material impact on the Group’s financial statements.
- HKAS 37 (Amendments), “Onerous Contracts – Cost of Fulfilling a Contract”. The amendments clarify that for the purpose of assessing whether a contract is onerous, the cost of fulfilling the contract includes both the incremental costs of fulfilling that contract and an allocation of other costs that relate directly to fulfilling contracts. The amendments are applied to contracts for which exist at the date when the amendments are first applied, with the cumulative effect of applying the amendments to be recognised as an opening balance adjustment to retained earnings or other component of equity, as appropriate. The comparatives are not restated. The application of the amendments will not have a material impact on the Group’s financial statements.
- HKFRS 3 (Amendments), “Reference to the Conceptual Framework”. The amendments update a reference in HKFRS 3 to the Conceptual Framework for Financial Reporting issued in 2018. The amendments also add to HKFRS 3 an exception to its requirement for an entity to refer to the Conceptual Framework to determine what constitutes an asset or a liability, that for some types of liabilities and contingent liabilities, an entity applying HKFRS 3 should instead refer to HKAS 37. The exception has been added to avoid an unintended consequence of updating the reference to the Conceptual Framework. The application of the amendments will not have a material impact on the Group’s financial statements.

NOTES TO THE INTERIM FINANCIAL INFORMATION

1. Basis of preparation and significant accounting policies (continued)

(c) Standard and amendments issued that are relevant to the Group but not yet mandatorily effective and have not been early adopted by the Group in 2020 (continued)

- HKFRS 17, “Insurance Contracts”. HKFRS 17 aims at replacing the current insurance contracts standard HKFRS 4, an interim standard that leads to highly divergent accounting practices that exist in the insurers’ local jurisdictions. The new standard establishes the principles for the recognition, measurement, presentation and disclosure of insurance contracts, with an objective to ensure that an entity provides relevant information that faithfully represents insurance contracts. Early application of the standard is permitted but only if the entity also applies HKFRS 9 and HKFRS 15. In June 2020, the IASB issued amendments to IFRS 17 deferring the effective date of IFRS 17 to the reporting periods beginning on or after 1 January 2023. At the time of the issuance of this interim financial statements, the change to the effective date have not yet been reflected in HKFRS. It is expected that the change to the effective date will also be adopted by the HKICPA to HKFRS 17. The Group is considering the financial impact of the standard and the timing of its application.
- Please refer to Note 2.1(b) of the Group’s Annual Report for 2019 for brief explanations of remaining amendments.

(d) Improvements to HKFRSs

“Improvements to HKFRSs” contains numerous amendments to HKFRSs which HKICPA considers not urgent but necessary. The amendments comprise clarification to changes in presentation, recognition or measurement purpose, amendments to the basis for conclusions as well as terminology or editorial amendments related to each HKFRS. These improvements will not have a material impact on the Group’s financial statements.

2. Critical accounting estimates and judgements in applying accounting policies

The nature and assumptions related to the Group’s accounting estimates in this reporting period are consistent with those used in the Group’s financial statements for the year ended 31 December 2019.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management

The Group is exposed to financial risks as a result of engaging in a variety of business activities. The principal financial risks are credit risk, market risk (including currency risk and interest rate risk) and liquidity risk. This note summarises the Group's exposures to these risks.

3.1 Credit risk

(A) Advances and other accounts

Advances with a specific repayment date are classified as overdue when the principal or interest is past due and remains unpaid. Advances repayable by regular instalments are classified as overdue when an instalment payment is past due and remains unpaid. Advances repayable on demand are classified as overdue either when a demand for repayment has been served on the borrower but repayment has not been made in accordance with the instruction or when the advances have remained continuously to exceed the approved limit that was advised to the borrower.

Advances are credit-impaired when one or more events that have a detrimental impact on the estimated future cash flows have occurred such as past due for more than 90 days or the borrower is unlikely to pay in full for the credit obligations to the Group. Credit-impaired advances are classified as Stage 3 and lifetime expected credit losses will be recognised.

Evidence that an advance is credit-impaired include observable data about the following events:

- Significant financial difficulty incurred by the borrower;
- A breach of contract, such as a default or delinquency in principal or interest payment;
- For economic or legal reasons related to the borrower's financial difficulty, the Group has granted to the borrower a concession that it would not otherwise consider;
- Probable that the borrower will become bankrupt or undergo other financial reorganisation;
or
- Other observable data indicating that there is a measurable decrease in the estimated future cash flows from such advances.

Advances classified as Stage 3 may not necessarily result in impairment loss where the advances are fully collateralised.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Advances and other accounts (continued)

Gross advances and other accounts before impairment allowances are analysed by internal credit grade and stage classification as follows:

	At 30 June 2020			
	Stage 1 HK\$'m	Stage 2 HK\$'m	Stage 3 HK\$'m	Total HK\$'m
Advances to customers				
Pass	1,491,529	2,322	–	1,493,851
Special mention	2,962	3,121	–	6,083
Substandard or below	–	–	3,817	3,817
	1,494,491	5,443	3,817	1,503,751
Trade bills				
Pass	13,265	–	–	13,265
Special mention	2	–	–	2
Substandard or below	–	–	–	–
	13,267	–	–	13,267
Advances to banks and other financial institutions				
Pass	1,403	–	–	1,403
Special mention	–	–	–	–
Substandard or below	–	–	–	–
	1,403	–	–	1,403
	1,509,161	5,443	3,817	1,518,421
Impairment allowances	(5,392)	(325)	(2,341)	(8,058)
	1,503,769	5,118	1,476	1,510,363

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Advances and other accounts (continued)

	At 31 December 2019			
	Stage 1 HK\$m	Stage 2 HK\$m	Stage 3 HK\$m	Total HK\$m
Advances to customers				
Pass	1,385,770	1,592	–	1,387,362
Special mention	2,683	2,621	–	5,304
Substandard or below	–	–	3,217	3,217
	1,388,453	4,213	3,217	1,395,883
Trade bills				
Pass	20,727	–	–	20,727
Special mention	–	–	–	–
Substandard or below	–	–	–	–
	20,727	–	–	20,727
Advances to banks and other financial institutions				
Pass	3,387	–	–	3,387
Special mention	–	–	–	–
Substandard or below	–	–	–	–
	3,387	–	–	3,387
	1,412,567	4,213	3,217	1,419,997
Impairment allowances	(4,564)	(297)	(2,175)	(7,036)
	1,408,003	3,916	1,042	1,412,961

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Advances and other accounts (continued)

Reconciliation of impairment allowances for advances and other accounts is as follows:

	At 30 June 2020			
	Stage 1 HK\$'m	Stage 2 HK\$'m	Stage 3 HK\$'m	Total HK\$'m
Impairment allowances				
At 1 January 2020	4,564	297	2,175	7,036
Transfer to Stage 1	75	(73)	(2)	–
Transfer to Stage 2	(43)	50	(7)	–
Transfer to Stage 3	(7)	(18)	25	–
Changes arising from transfer of stage	(62)	145	458	541
Other changes (including new assets and derecognised assets)	893	(73)	(50)	770
Write-offs	–	–	(305)	(305)
Recoveries	–	–	76	76
Unwind of discount on impairment allowances	–	–	(4)	(4)
Exchange difference	(28)	(3)	(25)	(56)
At 30 June 2020	5,392	325	2,341	8,058
Charged to income statement (Note 12)				1,311

	At 31 December 2019			
	Stage 1 HK\$'m	Stage 2 HK\$'m	Stage 3 HK\$'m	Total HK\$'m
Impairment allowances				
At 1 January 2019	3,748	546	1,130	5,424
Transfer to Stage 1	154	(143)	(11)	–
Transfer to Stage 2	(26)	103	(77)	–
Transfer to Stage 3	(15)	(184)	199	–
Changes arising from transfer of stage	(131)	84	1,216	1,169
Other changes (including new assets and derecognised assets)	832	(105)	(44)	683
Write-offs	–	–	(462)	(462)
Recoveries	–	–	213	213
Unwind of discount on impairment allowances	–	–	(4)	(4)
Exchange difference	2	(4)	15	13
At 31 December 2019	4,564	297	2,175	7,036

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Advances and other accounts (continued)

(a) Impaired advances

Impaired advances to customers are analysed as follows:

	At 30 June 2020		At 31 December 2019	
	Impaired HK\$'m	Classified or impaired HK\$'m	Impaired HK\$'m	Classified or impaired HK\$'m
Gross advances to customers	3,817	3,817	3,217	3,217
Percentage of gross advances to customers	0.25%	0.25%	0.23%	0.23%
Impairment allowances made in respect of such advances	2,341	2,341	2,175	2,175

Classified or impaired advances to customers represent advances which are either classified as “substandard”, “doubtful” or “loss” under the Group’s classification of loan quality, or classified as Stage 3.

The impairment allowances were made after taking into account the value of collateral in respect of the credit-impaired advances.

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Current market value of collateral held against the covered portion of impaired advances to customers	2,911	2,187
Covered portion of impaired advances to customers	1,627	1,011
Uncovered portion of impaired advances to customers	2,190	2,206

As at 30 June 2020, there were no impaired trade bills and advances to banks and other financial institutions (31 December 2019: Nil).

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Advances and other accounts (continued)

(b) Advances overdue for more than three months

The gross amount of advances overdue for more than three months is analysed as follows:

	At 30 June 2020		At 31 December 2019	
	Amount HK\$'m	% of gross advances to customers	Amount HK\$'m	% of gross advances to customers
Gross advances to customers which have been overdue for:				
– six months or less but over three months	426	0.03%	145	0.01%
– one year or less but over six months	647	0.04%	836	0.06%
– over one year	1,578	0.11%	948	0.07%
Advances overdue for over three months	2,651	0.18%	1,929	0.14%
Impairment allowances made in respect of such advances – Stage 3	2,005		1,651	

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Current market value of collateral held against the covered portion of such advances to customers	1,049	487
Covered portion of such advances to customers	708	315
Uncovered portion of such advances to customers	1,943	1,614

Collateral held against overdue or impaired loans is principally represented by charges over business assets such as commercial, residential premises and vessels for corporate loans and mortgages over residential properties for personal loans.

As at 30 June 2020, there were no trade bills and advances to banks and other financial institutions overdue for more than three months (31 December 2019: Nil).

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Advances and other accounts (continued)

(c) Rescheduled advances

	At 30 June 2020		At 31 December 2019	
	Amount HK\$'m	% of gross advances to customers	Amount HK\$'m	% of gross advances to customers
Rescheduled advances to customers net of amounts included in "Advances overdue for more than three months"	147	0.01%	239	0.02%

Rescheduled advances are those advances that have been restructured and renegotiated between the bank and borrowers because of deterioration in the financial position of the borrower or the inability of the borrower to meet the original repayment schedule, and the revised repayment terms, either of interest or the repayment period, are "non-commercial" to the Group. Rescheduled advances, which have been overdue for more than three months under the revised repayment terms, are included in "Advances overdue for more than three months".

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Advances and other accounts (continued)

(d) Concentration of advances to customers

(i) Sectoral analysis of gross advances to customers

The following analysis of the gross advances to customers by industry sector is based on the categories with reference to the completion instructions for the HKMA return of loans and advances.

	At 30 June 2020					
	Gross advances to customers HK\$'m	% covered by collateral or other security	Classified or impaired HK\$'m	Overdue HK\$'m	Impairment allowances - Stage 3 HK\$'m	Impairment allowances - Stages 1 and 2 HK\$'m
Loans for use in Hong Kong						
Industrial, commercial and financial						
- Property development	139,340	23.42%	-	5	-	710
- Property investment	64,716	67.94%	106	162	4	138
- Financial concerns	27,217	0.85%	-	-	-	46
- Stockbrokers	6,147	32.45%	-	-	-	2
- Wholesale and retail trade	36,031	40.14%	171	291	100	322
- Manufacturing	60,077	9.04%	66	68	5	209
- Transport and transport equipment	75,570	24.28%	319	3	-	234
- Recreational activities	205	12.22%	-	3	-	3
- Information technology	24,321	0.81%	92	93	4	28
- Others	132,303	48.02%	6	259	2	459
Individuals						
- Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	21,239	99.51%	16	170	-	23
- Loans for purchase of other residential properties	288,778	99.94%	114	1,279	1	187
- Credit card advances	12,340	-	130	460	116	174
- Others	104,862	93.58%	105	629	89	589
Total loans for use in Hong Kong	993,146	59.28%	1,125	3,422	321	3,124
Trade financing	82,074	13.72%	536	586	311	236
Loans for use outside Hong Kong	428,531	5.85%	2,156	2,657	1,709	2,355
Gross advances to customers	1,503,751	41.56%	3,817	6,665	2,341	5,715

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Advances and other accounts (continued)

(d) Concentration of advances to customers (continued)

(i) Sectoral analysis of gross advances to customers (continued)

	At 31 December 2019					
	Gross advances to customers HK\$'m	% covered by collateral or other security	Classified or impaired HK\$'m	Overdue HK\$'m	Impairment allowances – Stage 3 HK\$'m	Impairment allowances – Stages 1 and 2 HK\$'m
Loans for use in Hong Kong						
Industrial, commercial and financial						
– Property development	137,663	21.53%	–	9	–	695
– Property investment	49,073	81.98%	–	158	–	62
– Financial concerns	28,353	0.89%	–	–	–	53
– Stockbrokers	815	98.27%	–	–	–	1
– Wholesale and retail trade	39,880	36.86%	88	283	87	210
– Manufacturing	42,719	12.98%	193	222	95	174
– Transport and transport equipment	66,511	27.29%	325	69	–	180
– Recreational activities	2,161	1.19%	–	–	–	3
– Information technology	22,464	0.90%	–	48	–	76
– Others	125,909	47.30%	6	138	4	365
Individuals						
– Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	19,855	99.68%	18	161	–	10
– Loans for purchase of other residential properties	277,288	99.93%	96	1,374	–	97
– Credit card advances	14,663	–	127	579	113	159
– Others	97,380	91.08%	71	504	63	358
Total loans for use in Hong Kong	924,734	59.98%	924	3,545	362	2,443
Trade financing	75,764	14.75%	318	340	237	154
Loans for use outside Hong Kong	395,385	6.74%	1,975	1,988	1,576	2,263
Gross advances to customers	1,395,883	42.45%	3,217	5,873	2,175	4,860

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Advances and other accounts (continued)

(d) Concentration of advances to customers (continued)

(ii) Geographical analysis of gross advances to customers

The following geographical analysis of advances to customers is based on the locations of the counterparties, after taking into account the transfer of risk. For an advance to customer guaranteed by a party situated in a location different from the customer, the risk will be transferred to the location of the guarantor.

Gross advances to customers

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Hong Kong	1,227,493	1,124,812
Chinese Mainland	119,294	126,075
Others	156,964	144,996
	1,503,751	1,395,883
Impairment allowances made in respect of the gross advances to customers – Stages 1 and 2		
Hong Kong	4,074	3,228
Chinese Mainland	460	492
Others	1,181	1,140
	5,715	4,860

Overdue advances

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Hong Kong	4,408	4,341
Chinese Mainland	668	607
Others	1,589	925
	6,665	5,873
Impairment allowances made in respect of the overdue advances – Stage 3		
Hong Kong	1,156	975
Chinese Mainland	395	423
Others	689	489
	2,240	1,887

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Advances and other accounts (continued)

(d) Concentration of advances to customers (continued)

(ii) Geographical analysis of gross advances to customers (continued)

Classified or impaired advances

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Hong Kong	2,173	1,766
Chinese Mainland	486	507
Others	1,158	944
	3,817	3,217
Impairment allowances made in respect of the classified or impaired advances – Stage 3		
Hong Kong	1,236	1,132
Chinese Mainland	411	436
Others	694	607
	2,341	2,175

(B) Repossessed assets

The estimated market value of repossessed assets held by the Group as at 30 June 2020 amounted to HK\$50 million (31 December 2019: HK\$33 million). The repossessed assets comprise properties in respect of which the Group has acquired access or control (e.g. through court proceedings or voluntary actions by the proprietors concerned) for release in full or in part of the obligations of the borrowers.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(C) Debt securities and certificates of deposit

The following tables present an analysis of the carrying value of debt securities and certificates of deposit by issue rating and stage classification. In the absence of such issue ratings, the ratings designated for the issuers are reported.

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Investment in securities at fair value through other comprehensive income		
– Stage 1		
Aaa	95,287	105,381
Aa1 to Aa3	198,238	171,367
A1 to A3	360,925	358,381
Lower than A3	24,437	24,952
Unrated	23,098	24,621
	701,985	684,702
– Stage 2	–	–
– Stage 3	–	–
	701,985	684,702
Of which: impairment allowances	(233)	(160)
Investment in securities at amortised cost		
– Stage 1		
Aaa	51,856	57,569
Aa1 to Aa3	5,934	4,687
A1 to A3	36,481	26,263
Lower than A3	20,180	15,956
Unrated	7,326	6,554
	121,777	111,029
– Stage 2	–	–
– Stage 3	–	–
	121,777	111,029
Impairment allowances	(53)	(46)
	121,724	110,983
Financial assets at fair value through profit or loss		
Aaa	2,847	3,030
Aa1 to Aa3	17,754	28,350
A1 to A3	9,237	18,779
Lower than A3	9,932	11,834
Unrated	2,978	6,111
	42,748	68,104

As at 30 June 2020, there were no impaired or overdue debt securities and certificates of deposit (31 December 2019: Nil).

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(D) Credit risk management in response to COVID-19 pandemic

The rapid global spread of COVID-19 pandemic during the first half of 2020 has severely disrupted the economic activities and operations of our customers, the Group has taken a series of risk control measures in response to the adverse impact from the pandemic:

- The Group coordinated with the HKMA in launching various relief measures for individuals and commercial customers, in order to alleviate the financial pressure and the impact of the pandemic. The underwriting standards of the loans under relief measures are consistent with other credits and the repayment terms are revised on commercial basis. Therefore, loans under relief measures do not automatically trigger the migration to Stage 2 and Stage 3, and are not classified as rescheduled advances.
- The Group has conducted risk-based assessments on those industries which are more affected by the impact of COVID-19 pandemic (including Trading, Retail, Aviation, Tourism (including hospitality), Catering, Entertainment etc.). Impacts of the pandemic on affected customers, their respective mitigation measures and short-term refinancing plans were also assessed, vulnerable borrowers were identified and put into the watchlist for on-going close monitoring. The loan classification and internal ratings of these borrowers were reviewed according to their latest situation.
- The Group performed stress tests of different scenarios of containment of COVID-19 pandemic to assess the potential impacts on credit loss and asset quality.
- The Group reviewed and updated the forward looking macro-economic factors used in ECL computation to reflect the uncertain economic outlook and possible further deterioration in the economic environments due to impact of COVID-19 pandemic, which resulted in an increase in Stage 1 and Stage 2 impairment allowance. In addition, the Group performed internal rating review of major customers being put into watchlist due to COVID-19 pandemic impacts, resulting in downgrades of those affected borrowers hence leading to additional Stage 1 and Stage 2 impairment allowance to withstand the uncertainty of future economic conditions.

In the current challenging economic situation, the Group will continue to maintain effective risk management framework and prudent underwriting standards to avoid significant deterioration in asset quality.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.2 Market risk

(A) VaR

The Group uses the VaR to measure and report general market risks to the RMC and senior management on a periodic basis. The Group adopts a uniformed VaR calculation model, using a historical simulation approach and two years of historical market data, to calculate the VaR of the Group and its subsidiaries over a one-day holding period with a 99% confidence level, and sets up the VaR limit of the Group and its subsidiaries.

The following table sets out the VaR for all general market risk exposures¹ of the Group.

	Year	At 30 June HK\$'m	Minimum for the first half of year HK\$'m	Maximum for the first half of year HK\$'m	Average for the first half of year HK\$'m
VaR for all market risk	2020	38.7	17.5	44.1	30.6
	2019	48.1	23.2	48.1	30.5
VaR for foreign exchange risk	2020	27.5	6.5	29.3	14.8
	2019	11.7	7.7	21.1	14.6
VaR for interest rate risk in the trading book	2020	26.0	13.2	35.6	24.7
	2019	20.7	9.8	24.5	17.6
VaR for equity risk in the trading book	2020	0.8	0.3	2.9	0.8
	2019	0.6	0.2	2.5	0.5
VaR for commodity risk	2020	0.4	–	2.5	0.6
	2019	41.5	10.4	42.1	22.2

Note:

1. Structural FX positions have been excluded.

Although there is a valuable guide to market risk, VaR should always be viewed in the context of its limitations. For example:

- the use of historical market data as a proxy for estimating future events may not encompass all potential events, particularly those which are extreme in nature;
- the use of a one-day holding period assumes that all positions can be liquidated or hedged in one day. This may not fully reflect the market risk arising at times of severe illiquidity, when a one-day holding period may be insufficient to liquidate or hedge all positions fully;
- the use of a 99% confidence level, by definition, does not take into account losses that might occur beyond this level of confidence; and
- VaR is calculated on the basis of exposures outstanding at the close of business and therefore does not necessarily reflect intra-day exposures.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.2 Market risk (continued)

(A) VaR (continued)

The Group recognises these limitations by formulating stress test indicators and limits to assess and manage the market risk uncovered by VaR. The stress testing programme of the market risk includes sensitivity testing on changes in risk factors with various degrees of severity, as well as scenario analysis on historical events including the 1987 Equity Market Crash, 1994 Bond Market Crash, 1997 Asian Financial Crisis, 2001 9-11 event and 2008 Financial Tsunami, etc.

(B) Currency risk

The Group's assets and liabilities are denominated in major currencies, particularly HK Dollar, US Dollar and Renminbi. To ensure the currency risk exposure of the Group is kept to an acceptable level, risk limits (e.g. Position and VaR limit) are used to serve as a monitoring tool. Moreover, the Group seeks to minimise the gap between assets and liabilities in the same currency. Foreign exchange contracts (e.g. FX swaps) are usually used to manage FX risk associated with foreign currency-denominated assets and liabilities.

The following is a summary of the Group's major foreign currency exposures arising from trading, non-trading and structural positions and is prepared with reference to the completion instructions for the HKMA return of foreign currency position. The net options position is calculated based on the basis of delta-weighted positions of all foreign exchange options contracts.

	At 30 June 2020							
	Equivalent in million of HK\$							
	US Dollars	Pound Sterling	Japanese Yen	Euro	Renminbi	Australian Dollars	Other foreign currencies	Total foreign currencies
Spot assets	1,003,765	26,515	103,656	46,384	309,133	33,627	73,917	1,596,997
Spot liabilities	(846,803)	(19,719)	(8,096)	(29,380)	(305,425)	(28,429)	(76,347)	(1,314,199)
Forward purchases	904,882	22,655	12,329	50,404	502,372	15,799	53,243	1,561,684
Forward sales	(1,045,047)	(29,227)	(107,856)	(67,352)	(504,014)	(20,973)	(50,752)	(1,825,221)
Net options position	(144)	(25)	1	7	(73)	(31)	59	(206)
Net long/(short) position	16,653	199	34	63	1,993	(7)	120	19,055

	At 31 December 2019							
	Equivalent in million of HK\$							
	US Dollars	Pound Sterling	Japanese Yen	Euro	Renminbi	Australian Dollars	Other foreign currencies	Total foreign currencies
Spot assets	932,480	29,513	123,344	40,611	311,496	37,785	70,914	1,546,143
Spot liabilities	(841,543)	(17,530)	(13,099)	(25,326)	(301,348)	(24,821)	(67,572)	(1,291,239)
Forward purchases	987,326	21,177	35,349	49,566	529,913	20,718	50,290	1,694,339
Forward sales	(1,076,832)	(33,139)	(145,612)	(64,801)	(538,358)	(33,632)	(54,187)	(1,946,561)
Net options position	144	56	4	(86)	(293)	(15)	(24)	(214)
Net long/(short) position	1,575	77	(14)	(36)	1,410	35	(579)	2,468

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.2 Market risk (continued)

(B) Currency risk (continued)

	At 30 June 2020					
	Equivalent in million of HK\$					
	US Dollars	Malaysian Baht	Philippine Ringgit	Philippine Peso	Other foreign currencies	Total foreign currencies
Net structural position	29,721	2,561	2,841	1,793	4,616	41,532

	At 31 December 2019					
	Equivalent in million of HK\$					
	US Dollars	Malaysian Baht	Philippine Ringgit	Philippine Peso	Other foreign currencies	Total foreign currencies
Net structural position	29,052	2,625	2,903	1,737	4,523	40,840

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.2 Market risk (continued)

(C) Interest rate risk

The tables below summarise the Group's on-balance sheet exposure to interest rate risk as at 30 June 2020 and 31 December 2019. Included in the tables are the assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing date and maturity date.

	At 30 June 2020						
	Up to 1 month HK\$'m	1 to 3 months HK\$'m	3 to 12 months HK\$'m	1 to 5 years HK\$'m	Over 5 years HK\$'m	Non-interest bearing HK\$'m	Total HK\$'m
Assets							
Cash and balances and placements with banks and other financial institutions	248,950	14,846	38,525	395	-	106,942	409,658
Financial assets at fair value through profit or loss	3,762	13,959	4,941	9,702	13,978	11,633	57,975
Derivative financial instruments	-	-	-	-	-	44,265	44,265
Hong Kong SAR Government certificates of indebtedness	-	-	-	-	-	175,330	175,330
Advances and other accounts	1,192,580	231,205	31,570	42,578	6,081	6,349	1,510,363
Investment in securities							
– At FVOCI	69,558	162,954	168,400	186,968	114,105	6,177	708,162
– At amortised cost	1,151	1,200	19,792	42,415	57,166	-	121,724
Interests in associates and joint ventures	-	-	-	-	-	1,578	1,578
Investment properties	-	-	-	-	-	19,579	19,579
Properties, plant and equipment	-	-	-	-	-	50,208	50,208
Other assets (including current and deferred tax assets)	25,815	-	-	-	-	102,069	127,884
Total assets	1,541,816	424,164	263,228	282,058	191,330	524,130	3,226,726
Liabilities							
Hong Kong SAR currency notes in circulation	-	-	-	-	-	175,330	175,330
Deposits and balances from banks and other financial institutions	242,476	7,364	1,249	1,335	-	18,060	270,484
Financial liabilities at fair value through profit or loss	661	6,225	2,902	649	421	-	10,858
Derivative financial instruments	-	-	-	-	-	53,075	53,075
Deposits from customers	1,492,700	289,199	113,067	3,754	-	241,716	2,140,436
Debt securities and certificates of deposit in issue	-	-	-	-	-	-	-
Other accounts and provisions (including current and deferred tax liabilities)	8,252	48	104	807	359	128,231	137,801
Insurance contract liabilities	-	-	-	-	-	125,738	125,738
Subordinated liabilities	-	-	-	-	-	-	-
Total liabilities	1,744,089	302,836	117,322	6,545	780	742,150	2,913,722
Interest sensitivity gap	(202,273)	121,328	145,906	275,513	190,550	(218,020)	313,004

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.2 Market risk (continued)

(C) Interest rate risk (continued)

	At 31 December 2019						
	Up to 1 month HK\$'m	1 to 3 months HK\$'m	3 to 12 months HK\$'m	1 to 5 years HK\$'m	Over 5 years HK\$'m	Non-interest bearing HK\$'m	Total HK\$'m
Assets							
Cash and balances and placements with banks and other financial institutions	247,996	25,193	6,201	–	–	87,439	366,829
Financial assets at fair value through profit or loss	10,465	17,977	10,254	13,410	21,295	11,792	85,193
Derivative financial instruments	–	–	–	–	–	31,027	31,027
Hong Kong SAR Government certificates of indebtedness	–	–	–	–	–	163,840	163,840
Advances and other accounts	1,142,802	178,023	35,698	43,576	5,126	7,736	1,412,961
Investment in securities							
– At FVOCI	123,330	165,789	110,936	171,211	113,436	5,968	690,670
– At amortised cost	1,970	5,050	10,999	52,157	40,807	–	110,983
Interests in associates and joint ventures	–	–	–	–	–	1,632	1,632
Investment properties	–	–	–	–	–	20,110	20,110
Properties, plant and equipment	–	–	–	–	–	51,602	51,602
Other assets (including current and deferred tax assets)	14,170	–	–	–	–	77,039	91,209
Total assets	1,540,733	392,032	174,088	280,354	180,664	458,185	3,026,056
Liabilities							
Hong Kong SAR currency notes in circulation	–	–	–	–	–	163,840	163,840
Deposits and balances from banks and other financial institutions	236,979	1,271	897	1,628	–	27,114	267,889
Financial liabilities at fair value through profit or loss	2,843	6,046	9,202	724	391	–	19,206
Derivative financial instruments	–	–	–	–	–	32,921	32,921
Deposits from customers	1,409,054	295,979	139,866	4,577	–	159,797	2,009,273
Debt securities and certificates of deposit in issue	–	116	–	–	–	–	116
Other accounts and provisions (including current and deferred tax liabilities)	9,331	7	114	1,008	721	83,915	95,096
Insurance contract liabilities	–	–	–	–	–	117,269	117,269
Subordinated liabilities	–	12,954	–	–	–	–	12,954
Total liabilities	1,658,207	316,373	150,079	7,937	1,112	584,856	2,718,564
Interest sensitivity gap	(117,474)	75,659	24,009	272,417	179,552	(126,671)	307,492

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.3 Liquidity risk

(A) Liquidity coverage ratio and net stable funding ratio

	2020	2019
Average value of liquidity coverage ratio		
– First quarter	150.45%	183.00%
– Second quarter	131.38%	156.57%

Average value of liquidity coverage ratio is calculated based on the arithmetic mean of the liquidity coverage ratio as at the end of each working day in the quarter and the calculation methodology and instructions set out in the HKMA return of liquidity position.

	2020	2019
Quarter-end value of net stable funding ratio		
– First quarter	116.60%	121.36%
– Second quarter	117.49%	119.15%

Quarter-end value of net stable funding ratio is calculated based on the calculation methodology and instructions set out in the HKMA return of stable funding position.

Liquidity coverage ratio and net stable funding ratio are computed on the consolidated basis which comprise the positions of BOCHK and certain subsidiaries specified by the HKMA in accordance with the Banking (Liquidity) Rules.

The additional information of liquidity coverage ratio and net stable funding ratio disclosures is available under the section “Regulatory Disclosures” on BOCHK’s website at www.bochk.com.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.3 Liquidity risk (continued)

(B) Maturity analysis

The tables below analyse the Group's assets and liabilities as at 30 June 2020 and 31 December 2019 into relevant maturity groupings based on the remaining period at balance sheet date to the contractual maturity date.

	At 30 June 2020							
	On demand HK\$'m	Up to 1 month HK\$'m	1 to 3 months HK\$'m	3 to 12 months HK\$'m	1 to 5 years HK\$'m	Over 5 years HK\$'m	Indefinite HK\$'m	Total HK\$'m
Assets								
Cash and balances and placements with banks and other financial institutions	252,684	103,208	14,455	38,136	1,175	-	-	409,658
Financial assets at fair value through profit or loss	-	3,800	13,867	4,720	9,168	13,851	12,569	57,975
Derivative financial instruments	14,449	1,379	2,382	4,256	12,415	9,384	-	44,265
Hong Kong SAR Government certificates of indebtedness	175,330	-	-	-	-	-	-	175,330
Advances and other accounts	241,313	48,919	67,358	216,731	609,470	324,982	1,590	1,510,363
Investment in securities								
– At FVOCI	-	59,509	143,752	175,300	206,728	116,375	6,498	708,162
– At amortised cost	-	1,500	1,530	18,765	40,996	56,699	2,234	121,724
Interests in associates and joint ventures	-	-	-	-	-	-	1,578	1,578
Investment properties	-	-	-	-	-	-	19,579	19,579
Properties, plant and equipment	-	-	-	-	-	-	50,208	50,208
Other assets (including current and deferred tax assets)	53,597	39,073	995	6,174	15,499	12,523	23	127,884
Total assets	737,373	257,388	244,339	464,082	895,451	533,814	94,279	3,226,726
Liabilities								
Hong Kong SAR currency notes in circulation	175,330	-	-	-	-	-	-	175,330
Deposits and balances from banks and other financial institutions	182,633	77,903	7,364	1,249	1,335	-	-	270,484
Financial liabilities at fair value through profit or loss	-	661	6,228	2,902	649	418	-	10,858
Derivative financial instruments	13,253	1,312	1,846	4,255	17,817	14,592	-	53,075
Deposits from customers	1,289,941	444,475	289,199	113,067	3,754	-	-	2,140,436
Debt securities and certificates of deposit in issue	-	-	-	-	-	-	-	-
Other accounts and provisions (including current and deferred tax liabilities)	47,944	74,398	436	7,229	7,656	138	-	137,801
Insurance contract liabilities	43,569	1,296	1,194	5,832	22,214	51,633	-	125,738
Subordinated liabilities	-	-	-	-	-	-	-	-
Total liabilities	1,752,670	600,045	306,267	134,534	53,425	66,781	-	2,913,722
Net liquidity gap	(1,015,297)	(342,657)	(61,928)	329,548	842,026	467,033	94,279	313,004

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.3 Liquidity risk (continued)

(B) Maturity analysis (continued)

	At 31 December 2019							Total HK\$'m
	On demand HK\$'m	Up to 1 month HK\$'m	1 to 3 months HK\$'m	3 to 12 months HK\$'m	1 to 5 years HK\$'m	Over 5 years HK\$'m	Indefinite HK\$'m	
Assets								
Cash and balances and placements with banks and other financial institutions	244,794	90,641	24,799	5,810	785	-	-	366,829
Financial assets at fair value through profit or loss	-	10,389	17,233	9,537	12,515	21,278	14,241	85,193
Derivative financial instruments	11,662	2,593	3,574	4,996	5,212	2,990	-	31,027
Hong Kong SAR Government certificates of indebtedness	163,840	-	-	-	-	-	-	163,840
Advances and other accounts	211,627	46,455	57,860	167,062	619,292	309,478	1,187	1,412,961
Investment in securities								
– At FVOCI	-	113,646	141,953	119,015	195,027	114,737	6,292	690,670
– At amortised cost	-	2,151	5,124	10,634	51,789	40,780	505	110,983
Interests in associates and joint ventures	-	-	-	-	-	-	1,632	1,632
Investment properties	-	-	-	-	-	-	20,110	20,110
Properties, plant and equipment	-	-	-	-	-	-	51,602	51,602
Other assets (including current and deferred tax assets)	42,449	16,213	456	4,224	16,061	11,796	10	91,209
Total assets	674,372	282,088	250,999	321,278	900,681	501,059	95,579	3,026,056
Liabilities								
Hong Kong SAR currency notes in circulation	163,840	-	-	-	-	-	-	163,840
Deposits and balances from banks and other financial institutions	168,004	96,089	1,271	897	1,628	-	-	267,889
Financial liabilities at fair value through profit or loss	-	2,843	6,049	9,202	724	388	-	19,206
Derivative financial instruments	9,576	2,509	3,089	5,161	7,627	4,959	-	32,921
Deposits from customers	1,107,436	461,415	295,979	139,866	4,577	-	-	2,009,273
Debt securities and certificates of deposit in issue	-	-	116	-	-	-	-	116
Other accounts and provisions (including current and deferred tax liabilities)	45,568	35,537	2,137	3,603	8,079	172	-	95,096
Insurance contract liabilities	40,113	455	372	4,814	21,368	50,147	-	117,269
Subordinated liabilities	-	-	12,954	-	-	-	-	12,954
Total liabilities	1,534,537	598,848	321,967	163,543	44,003	55,666	-	2,718,564
Net liquidity gap	(860,165)	(316,760)	(70,968)	157,735	856,678	445,393	95,579	307,492

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.3 Liquidity risk (continued)

(B) Maturity analysis (continued)

The above maturity classifications have been prepared in accordance with relevant provisions under the Banking (Disclosure) Rules. The Group has reported assets such as advances and debt securities which have been overdue for not more than one month as "On demand". In the case of an asset that is repayable by different payments or instalments, only that portion of the asset that is actually overdue is reported as overdue. Any part of the asset that is not due is reported according to the residual maturity unless the repayment of the asset is in doubt in which case the amount is reported as "Indefinite". The above assets are stated after deduction of provisions, if any.

The analysis of debt securities by remaining period to maturity is based on contractual maturity date. The disclosure does not imply that the securities will be held to maturity.

The above analysis in respect of insurance contract liabilities represents the estimated timing of net cash outflows resulting from recognised insurance contract liabilities on the balance sheet.

3.4 Insurance risk

The Group is in the business of insuring against the risk of mortality, morbidity, disability, critical illness, accidents and related risks. The Group manages these risks through the application of its underwriting strategy, reinsurance arrangements and regular experience monitoring.

The underwriting strategy is intended to set premium pricing at an appropriate level that corresponds with the underlying exposure of the risks underwritten and the Group's underwriting procedures include screening processes, such as the review of health condition and family medical history to ensure alignment with the underwriting strategy.

Within the insurance process, concentrations of risk may arise where a particular event or a series of events could impact heavily on the Group's claim liabilities. Such concentrations may arise from a single insurance contract or through a small number of related contracts, and relate to circumstances where significant claim liabilities could arise.

For the in-force insurance contracts, most of the underlying insurance liabilities are related to endowment, universal life, annuity, whole life and unit-linked insurance products. For most of the insurance policies issued, the Group has a retention limit on any single life insured. The Group cedes the excess of the insured benefit over the limit to reinsurer under an excess of loss reinsurance arrangement. For some of the insurance business, the Group has entered into reinsurance arrangements that reinsure most of the insurance risk.

Uncertainty in the estimation of future benefit payments and premium receipts for long-term insurance contracts arises from the unpredictability of long-term changes in overall levels of mortality, morbidity and persistency. In this regard, the Group has conducted relevant experience studies and researches regularly to identify emerging trends. Results would be taken into account in pricing and underwriting management. The results of such studies are also considered in determining the assumptions of insurance liability which include an appropriate level of prudential margins.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.5 Capital management

The Group has adopted the foundation internal ratings-based (“FIRB”) approach to calculate the credit risk capital charge for the majority of its non-securitisation exposures. Small residual credit exposures are remained under the standardised (credit risk) (“STC”) approach. The Group has adopted the standardised credit valuation adjustment (“CVA”) method to calculate the capital charge for the CVA risk of the counterparty.

The Group continues to adopt the internal models (“IMM”) approach to calculate the general market risk capital charge for foreign exchange and interest rate exposures and, with the approval from the HKMA, exclude its structural FX positions in the calculation of the market risk capital charge. The Group continues to adopt the standardised (market risk) (“STM”) approach to calculate the market risk capital charge for the remaining exposures.

The Group continues to adopt the standardised (operational risk) (“STO”) approach to calculate the operational risk capital charge.

(A) Basis of regulatory consolidation

The consolidation basis for regulatory purposes comprises the positions of BOCHK and certain subsidiaries specified by the HKMA in accordance with the Banking (Capital) Rules. For accounting purposes, subsidiaries are consolidated in accordance with HKFRSs and the list of subsidiaries is set out in “Appendix – Subsidiaries of the Company”.

The Company, its subsidiaries of BOC Group Life Assurance Company Limited, BOCHK Asset Management (Cayman) Limited and BOC Insurance (International) Holdings Company Limited (including their subsidiaries), and certain subsidiaries of BOCHK are included within the accounting scope of consolidation but not included within the regulatory scope of consolidation.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.5 Capital management (continued)

(A) Basis of regulatory consolidation (continued)

The particulars of the above-mentioned subsidiaries of BOCHK are as follows:

Name	At 30 June 2020		At 31 December 2019	
	Total assets HK\$'m	Total equity HK\$'m	Total assets HK\$'m	Total equity HK\$'m
BOC Group Trustee Company Limited	200	200	200	200
BOCI-Prudential Trustee Limited	521	450	612	483
China Bridge (Malaysia) Sdn. Bhd.	21	14	56	36
Bank of China (Hong Kong) Nominees Limited	–	–	–	–
Bank of China (Hong Kong) Trustees Limited	12	12	12	11
BOC Financial Services (Nanning) Company Limited	168	9	173	42
BOCHK Information Technology (Shenzhen) Co., Ltd.	447	261	401	255
BOCHK Information Technology Services (Shenzhen) Co., Ltd.	409	348	418	348
Che Hsing (Nominees) Limited	1	1	1	1
Po Sang Financial Investment Services Company Limited	363	345	364	345
Po Sang Securities and Futures Limited	1,057	391	664	373
Sin Chiao Enterprises Corporation, Limited	6	6	6	6
Sin Hua Trustee Limited	4	4	5	5
Billion Express Development Inc.	–	–	–	–
Billion Orient Holdings Ltd.	–	–	–	–
Elite Bond Investments Ltd.	–	–	–	–
Express Capital Enterprise Inc.	–	–	–	–
Express Charm Holdings Corp.	–	–	–	–
Express Shine Assets Holdings Corp.	–	–	–	–
Express Talent Investment Ltd.	–	–	–	–
Gold Medal Capital Inc.	–	–	–	–
Gold Tap Enterprises Inc.	–	–	–	–
Maxi Success Holdings Ltd.	–	–	–	–
Smart Linkage Holdings Inc.	–	–	–	–
Smart Union Capital Investments Ltd.	–	–	–	–
Success Trend Development Ltd.	–	–	–	–
Wise Key Enterprises Corp.	–	–	–	–

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.5 Capital management (continued)

(A) Basis of regulatory consolidation (continued)

The principal activities of the above subsidiaries are set out in "Appendix – Subsidiaries of the Company".

There were no subsidiaries which are included within the regulatory scope of consolidation but not included within the accounting scope of consolidation as at 30 June 2020 (31 December 2019: Nil).

There were also no subsidiaries which are included within both the accounting scope of consolidation and the regulatory scope of consolidation where the methods of consolidation differ as at 30 June 2020 (31 December 2019: Nil).

The Group operates subsidiaries in different countries/regions where capital is governed by local rules and there may be restrictions on the transfer of funds or regulatory capital between the members of the Group.

(B) Capital ratio

The capital ratios are analysed as follows:

	At 30 June 2020	At 31 December 2019
CET1 capital ratio	18.52%	17.76%
Tier 1 capital ratio	20.52%	19.90%
Total capital ratio	23.11%	22.89%

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.5 Capital management (continued)

(B) Capital ratio (continued)

The consolidated capital base after deductions used in the calculation of the above capital ratios is analysed as follows:

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
CET1 capital: instruments and reserves		
Directly issued qualifying CET1 capital instruments	43,043	43,043
Retained earnings	184,542	164,113
Disclosed reserves	46,433	51,309
CET1 capital before regulatory deductions	274,018	258,465
CET1 capital: regulatory deductions		
Valuation adjustments	(169)	(65)
Deferred tax assets (net of associated deferred tax liabilities)	(63)	(62)
Gains and losses due to changes in own credit risk on fair valued liabilities	(49)	237
Cumulative fair value gains arising from the revaluation of land and buildings (own-use and investment properties)	(51,510)	(52,459)
Regulatory reserve for general banking risks	(5,667)	(11,077)
Total regulatory deductions to CET1 capital	(57,458)	(63,426)
CET1 capital	216,560	195,039
AT1 capital: instruments		
Qualifying AT1 capital instruments classified as equity under applicable accounting standards	23,476	23,476
AT1 capital	23,476	23,476
Tier 1 capital	240,036	218,515
Tier 2 capital: instruments and provisions		
Capital instruments subject to phase-out arrangements from Tier 2 capital	–	2,505
Collective provisions and regulatory reserve for general banking risks eligible for inclusion in Tier 2 capital	7,043	6,743
Tier 2 capital before regulatory deductions	7,043	9,248
Tier 2 capital: regulatory deductions		
Add back of cumulative fair value gains arising from the revaluation of land and buildings (own-use and investment properties) eligible for inclusion in Tier 2 capital	23,179	23,607
Total regulatory adjustments to Tier 2 capital	23,179	23,607
Tier 2 capital	30,222	32,855
Total regulatory capital	270,258	251,370

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.5 Capital management (continued)

(B) Capital ratio (continued)

The capital buffer ratios are analysed as follows:

	At 30 June 2020	At 31 December 2019
Capital conservation buffer ratio	2.500%	2.500%
Higher loss absorbency ratio	1.500%	1.500%
Countercyclical capital buffer ratio	0.778%	1.552%

The additional information of capital ratio disclosures is available under the section "Regulatory Disclosures" on BOCHK's website at www.bochk.com.

(C) Leverage ratio

The leverage ratio is analysed as follows:

	At 30 June 2020 HK\$m	At 31 December 2019 HK\$m
Tier 1 capital	240,036	218,515
Leverage ratio exposure	2,960,539	2,799,606
Leverage ratio	8.11%	7.81%

The additional information of leverage ratio disclosures is available under the section "Regulatory Disclosures" on BOCHK's website at www.bochk.com.

4. Fair values of financial assets and liabilities

All financial instruments for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy as defined in HKFRS 13, "Fair value measurement". The categorisation are determined with reference to the observability and significance of the inputs used in the valuation methods and based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1: based on quoted prices (unadjusted) in active markets for identical assets or liabilities. This category includes equity securities listed on exchange, debt instruments issued by certain governments and certain exchange-traded derivative contracts.
- Level 2: based on valuation techniques for which the lowest level input that is significant to the fair value measurement is observable, either directly or indirectly. This category includes majority of the over-the-counter ("OTC") derivative contracts, debt securities and certificates of deposit with quote from pricing services vendors, issued structured deposits and other debt instruments.

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

- Level 3: based on valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable. This category includes equity investment, debt instruments and certain OTC derivative contracts with significant unobservable components.

For financial instruments that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by reassessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

4.1 *Financial instruments measured at fair value*

The Group has an established governance structure and controls framework to ensure that fair values are either determined or validated by control units independent of the front offices. Control units have overall responsibility for independent verification of valuation results from front line businesses and all other significant fair value measurements. Specific controls include verification of observable pricing inputs; review and approval for new models and changes to models; calibration and back-testing of models against observed market transactions; analysis and investigation of significant daily valuation movements; review of significant unobservable inputs and valuation adjustments. Significant valuation issues are reported to senior management, Risk Committee and Audit Committee.

Generally, the unit of account for a financial instrument is the individual instrument. HKFRS 13 permits a portfolio exception, through an accounting policy election, to measure the fair value of a portfolio of financial assets and financial liabilities on the basis of the net open risk position when certain criteria are met. The Group applies valuation adjustments at an individual instrument level, consistent with that unit of account. According to its risk management policies and systems to manage derivative financial instruments, the fair value of certain derivative portfolios that meet those criteria is measured on the basis of the price to be received or paid for net open risk. Those portfolio-level adjustments are allocated to the individual assets and liabilities on the basis of the relative size of each of the individual instruments in the portfolio.

The Group uses valuation techniques or broker/dealer quotations to determine the fair value of financial instruments when unable to obtain the open market quotation in active markets.

The main parameters used in valuation techniques for financial instruments held by the Group include bond prices, interest rates, foreign exchange rates, equity and stock prices, commodity prices, volatilities and correlations, counterparty credit spreads and others, which are mostly observable and obtainable from open market.

The technique used to calculate the fair value of the following financial instruments is as below:

Debt securities and certificates of deposit and other debt instruments

The fair value of these instruments is determined by obtaining quoted market prices from exchange, dealer or independent pricing service vendors or using discounted cash flow technique. Discounted cash flow model is a valuation technique that measures present value using estimated expected future cash flows from the instruments and then discounts these flows using a discount rate or discount margin that reflects the credit spreads required by the market for instruments with similar risk. These inputs are observable or can be corroborated by observable or unobservable market data.

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.1 Financial instruments measured at fair value (continued)

Asset backed securities

For this class of instruments, external prices are obtained from independent third parties. The valuation of these securities, depending on the nature of transaction, is estimated from market standard cash flow models with input parameter which include spreads to discount rates, default and recovery rates and prepayment rates that may be observable or compiled through matrix pricing for similar issues.

Derivatives

OTC derivative contracts include forward, swap and option contracts on foreign exchange, interest rate, equity, commodity or credit. The fair values of these contracts are mainly measured using valuation techniques such as discounted cash flow models and option pricing models. The inputs can be observable or unobservable market data. Observable inputs include interest rate, foreign exchange rates, equity and stock prices, commodity prices, credit default swap spreads, volatilities and correlations. Unobservable inputs may be used for less commonly traded option products which are embedded in structured deposits. For certain complex derivative contracts, the fair values are determined based on broker/dealer price quotations.

Credit valuation adjustments (“CVAs”) and debit valuation adjustments (“DVAs”) are applied to the Group’s OTC derivatives. These adjustments reflect market factors movement, expectations of counterparty creditworthiness and the Group’s own credit spread respectively. They are mainly determined for each counterparty and are dependent on expected future values of exposures, default probabilities and recovery rates.

Subordinated liabilities

Fair value for subordinated notes is based on market prices or broker/dealer price quotations. Own credit adjustment for subordinated notes is calculated as the difference between the market value and the net present value calculated by the latest benchmark interest rate and own credit spreads of the subordinated notes determined on the beginning of measurement period.

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.1 Financial instruments measured at fair value (continued)

(A) Fair value hierarchy

	At 30 June 2020			
	Level 1 HK\$'m	Level 2 HK\$'m	Level 3 HK\$'m	Total HK\$'m
Financial assets				
Trading assets (Note 21)				
– Debt securities and certificates of deposit	–	23,842	–	23,842
– Equity securities	56	–	–	56
– Other debt instruments	–	3,594	–	3,594
Other financial assets mandatorily classified at fair value through profit or loss (Note 21)				
– Debt securities and certificates of deposit	–	14,972	822	15,794
– Equity securities	4,623	–	–	4,623
– Fund	4,485	987	1,482	6,954
Financial assets designated at fair value through profit or loss (Note 21)				
– Debt securities and certificates of deposit	725	2,387	–	3,112
Derivative financial instruments (Note 22)	14,466	29,799	–	44,265
Investment in securities at FVOCI (Note 24)				
– Debt securities and certificates of deposit	159,688	540,293	2,004	701,985
– Equity securities	2,459	1,596	2,122	6,177
Financial liabilities				
Financial liabilities at fair value through profit or loss (Note 28)				
– Trading liabilities	–	10,858	–	10,858
Derivative financial instruments (Note 22)	13,317	39,758	–	53,075
Subordinated liabilities (Note 34)				
– Subordinated notes	–	–	–	–

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.1 Financial instruments measured at fair value (continued)

(A) Fair value hierarchy (continued)

	At 31 December 2019			
	Level 1 HK\$'m	Level 2 HK\$'m	Level 3 HK\$'m	Total HK\$'m
Financial assets				
Trading assets (Note 21)				
– Debt securities and certificates of deposit	133	37,457	–	37,590
– Equity securities	37	–	–	37
– Other debt instruments	–	5,297	–	5,297
Other financial assets mandatorily classified at fair value through profit or loss (Note 21)				
– Debt securities and certificates of deposit	–	25,271	2,252	27,523
– Equity securities	2,618	–	–	2,618
– Fund	5,705	1,958	1,474	9,137
Financial assets designated at fair value through profit or loss (Note 21)				
– Debt securities and certificates of deposit	708	2,283	–	2,991
Derivative financial instruments (Note 22)	11,674	19,342	11	31,027
Investment in securities at FVOCI (Note 24)				
– Debt securities and certificates of deposit	197,156	485,679	1,867	684,702
– Equity securities	2,680	1,134	2,154	5,968
Financial liabilities				
Financial liabilities at fair value through profit or loss (Note 28)				
– Trading liabilities	–	19,206	–	19,206
Derivative financial instruments (Note 22)	9,717	23,204	–	32,921
Subordinated liabilities (Note 34)				
– Subordinated notes	–	12,954	–	12,954

There were no significant financial asset and liability transfers between level 1 and level 2 for the Group during the first half of 2020 and the year of 2019.

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items

	At 30 June 2020				
	Financial assets				
	Other financial assets mandatorily classified at FVPL			Investment in securities at FVOCI	
	Debt securities and certificates of deposit HK\$'m	Fund HK\$'m	Derivative financial instruments HK\$'m	Debt securities and certificates of deposit HK\$'m	Equity securities HK\$'m
At 1 January 2020	2,252	1,474	11	1,867	2,154
Gains/(losses)					
– Income statement					
– Net trading gain	–	–	20	–	–
– Net gain/(loss) on other financial instruments at fair value through profit or loss	199	(98)	–	–	–
– Other comprehensive income					
– Change in fair value	–	–	–	137	(32)
Additions	194	106	–	–	–
Disposals, redemptions and maturity	(1,823)	–	–	–	–
Transfer into level 3	–	–	–	–	–
Transfer out of level 3	–	–	(31)	–	–
At 30 June 2020	822	1,482	–	2,004	2,122
Total unrealised gains/(losses) for the period included in income statement for financial assets held as at 30 June 2020					
– Net trading gain	–	–	–	–	–
– Net gain/(loss) on other financial instruments at fair value through profit or loss	199	(98)	–	–	–
	199	(98)	–	–	–

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items (continued)

	At 31 December 2019				
	Financial assets				
	Other financial assets mandatorily classified at FVPL			Investment in securities at FVOCI	
	Debt securities and certificates of deposit HK\$'m	Fund HK\$'m	Derivative financial instruments HK\$'m	Debt securities and certificates of deposit HK\$'m	Equity securities HK\$'m
At 1 January 2019	1,909	915	7	1,618	1,144
Gains					
– Income statement					
– Net trading gain	–	–	11	–	–
– Net gain on other financial instruments at fair value through profit or loss	382	80	–	–	–
– Other comprehensive income					
– Change in fair value	–	–	–	249	446
Additions	156	412	–	–	564
Disposals, redemptions and maturity	(195)	–	–	–	–
Transfer into level 3	–	67	–	–	–
Transfer out of level 3	–	–	(7)	–	–
At 31 December 2019	2,252	1,474	11	1,867	2,154
Total unrealised gains for the year included in income statement for financial assets held as at 31 December 2019					
– Net trading gain	–	–	11	–	–
– Net gain on other financial instruments at fair value through profit or loss	382	80	–	–	–
	382	80	11	–	–

As at 30 June 2020 and 31 December 2019, financial instruments categorised as level 3 are mainly comprised of debt securities and certificates of deposit, fund, unlisted equity shares and certain OTC derivative contracts.

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items (continued)

For certain illiquid debt securities and certificates of deposit and fund, the Group obtains valuation quotations from counterparties which may be based on unobservable inputs with significant impact on the valuation. For certain OTC derivative contracts, the counterparty credit spreads used in valuation techniques are unobservable inputs with significant impact on valuation. Therefore, these instruments have been classified by the Group as level 3. Transfers out of level 3 in the first half of 2020 and year of 2019 were due to change of valuation observability. The Group has established internal control procedures to control the Group's exposure to such financial instruments.

The fair values of unlisted FVOCI equity shares are determined with reference to (i) multiples of comparable listed companies, such as average of the price/earning ratios of comparables; or (ii) dividend discount model calculation of the underlying equity investments; or (iii) net asset value, if neither appropriate comparables nor dividend discount model calculation is available or applicable.

Had the significant unobservable inputs applied on the valuation techniques increased/decreased by 5% (31 December 2019: 5%), the Group's other comprehensive income would have increased/decreased by HK\$53 million and HK\$51 million, respectively (31 December 2019: HK\$42 million and HK\$37 million, respectively). When the fair value of the unlisted FVOCI shares is affected by more than one unobservable input, the aforesaid impact reflects the most favourable or the most unfavourable change from varying inputs individually.

4.2 Financial instruments not measured at fair value

Fair value estimates are made at a specific point in time based on relevant market information and information about various financial instruments. The following methods and assumptions have been used to estimate the fair value of each class of financial instrument as far as practicable.

Balances with/from banks and other financial institutions and trade bills

Substantially all the financial assets and liabilities mature within one year from the balance sheet date and their carrying value approximates fair value.

Advances to customers and banks and other financial institutions

Substantially all the advances to customers and banks and other financial institutions are on floating rate terms, bear interest at prevailing market interest rates and their carrying value approximates fair value.

Investment in securities at amortised cost

The fair value of securities at amortised cost is determined by using the same approach as those debt securities and certificates of deposit and asset backed securities measured at fair value as described in Note 4.1. Besides, a discounted cash flow model is used for certain securities at amortised cost based on a current yield curve appropriate for the remaining term to maturity.

Deposits from customers

Substantially all the deposits from customers mature within one year from the balance sheet date and their carrying value approximates fair value.

Debt securities and certificates of deposit in issue

The fair value of these instruments is determined by using the same approach as those debt securities and certificates of deposit measured at fair value as described in Note 4.1.

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.2 Financial instruments not measured at fair value (continued)

The following tables set out the carrying values and fair values of the financial instruments not measured at fair value, except for the above with their carrying values being approximation of fair values.

	At 30 June 2020		At 31 December 2019	
	Carrying value HK\$'m	Fair value HK\$'m	Carrying value HK\$'m	Fair value HK\$'m
Financial assets				
Investment in securities at amortised cost (Note 24)	121,724	128,046	110,983	114,241
Financial liabilities				
Debt securities and certificates of deposit in issue (Note 30)	–	–	116	116

5. Net interest income

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Interest income		
Advances to customers, due from banks and other financial institutions	20,228	22,924
Investment in securities and financial assets at fair value through profit or loss	8,558	10,422
Others	150	259
	28,936	33,605
Interest expense		
Deposits from customers, due to banks and other financial institutions	(9,964)	(12,974)
Debt securities and certificates of deposit in issue	(1)	(68)
Subordinated liabilities	(80)	(360)
Lease liabilities	(28)	(27)
Others	(227)	(273)
	(10,300)	(13,702)
Net interest income	18,636	19,903

Included within interest income are HK\$22,204 million (first half of 2019: HK\$24,949 million) and HK\$6,427 million (first half of 2019: HK\$6,674 million), before hedging effect, for financial assets measured at amortised cost and at fair value through other comprehensive income respectively.

Included within interest expense are HK\$10,070 million (first half of 2019: HK\$13,178 million), before hedging effect, for financial liabilities that are not measured at fair value through profit or loss.

NOTES TO THE INTERIM FINANCIAL INFORMATION

6. Net fee and commission income

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Fee and commission income		
Securities brokerage	1,567	1,093
Loan commissions	1,389	1,623
Credit card business	924	1,635
Insurance	713	1,160
Funds distribution	442	464
Payment services	358	339
Trust and custody services	322	309
Bills commissions	278	352
Currency exchange	157	323
Safe deposit box	153	144
Others	495	678
	6,798	8,120
Fee and commission expense		
Credit card business	(588)	(1,158)
Insurance	(233)	(302)
Securities brokerage	(178)	(133)
Others	(364)	(481)
	(1,363)	(2,074)
Net fee and commission income	5,435	6,046
Of which arise from:		
Financial assets or financial liabilities not at fair value through profit or loss		
– Fee and commission income	1,501	1,889
– Fee and commission expense	(3)	(6)
	1,498	1,883
Trust and other fiduciary activities		
– Fee and commission income	421	403
– Fee and commission expense	(14)	(13)
	407	390

NOTES TO THE INTERIM FINANCIAL INFORMATION

7. Net trading gain

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Net gain/(loss) from:		
Foreign exchange and foreign exchange products	2,863	2,135
Interest rate instruments and items under fair value hedge	(787)	(489)
Commodities	250	126
Equity and credit derivative instruments	4	57
	2,330	1,829

8. Net gain on other financial instruments at fair value through profit or loss

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Net gain on other financial instruments mandatorily classified at fair value through profit or loss	71	2,141
Net gain on financial instruments designated at fair value through profit or loss	131	74
	202	2,215

9. Net gain on other financial assets

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Net gain on disposal/redemption of investment in securities at FVOCI	2,513	736
Net gain/(loss) on disposal/redemption of investment in securities at amortised cost	48	(18)
Others	10	(2)
	2,571	716

NOTES TO THE INTERIM FINANCIAL INFORMATION

10. Other operating income

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Dividend income		
– From investment in securities at FVOCI derecognised during the period	21	2
– From investment in securities at FVOCI held at the end of the period	103	122
Gross rental income from investment properties	301	329
Less: Outgoings in respect of investment properties	(20)	(29)
Others	59	77
	464	501

Included in the “Outgoings in respect of investment properties” is HK\$2 million (first half of 2019: HK\$1 million) of direct operating expenses related to investment properties that were not let during the period.

11. Net insurance benefits and claims and movement in liabilities

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Gross insurance benefits and claims and movement in liabilities		
Claims, benefits and surrenders paid	(7,413)	(9,218)
Movement in liabilities	(9,310)	(8,487)
	(16,723)	(17,705)
Reinsurers' share of benefits and claims and movement in liabilities		
Reinsurers' share of claims, benefits and surrenders paid	4,851	3,450
Reinsurers' share of movement in liabilities	3,061	2,818
	7,912	6,268
Net insurance benefits and claims and movement in liabilities	(8,811)	(11,437)

NOTES TO THE INTERIM FINANCIAL INFORMATION

12. Net charge of impairment allowances

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Net (charge)/reversal of impairment allowances on:		
Advances and other accounts	(1,311)	(717)
Investment in securities		
– At FVOCI	(75)	(46)
– At amortised cost	(7)	(4)
	(82)	(50)
Others	27	(26)
Net charge of impairment allowances	(1,366)	(793)

13. Operating expenses

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Staff costs (including directors' emoluments)		
– Salaries and other costs	4,114	4,010
– Pension cost	270	254
	4,384	4,264
Premises and equipment expenses (excluding depreciation)		
– Short-term leases, leases of low-value assets and variable lease payments	–	117
– Information technology	316	318
– Others	234	217
	550	652
Depreciation	1,529	1,402
Auditor's remuneration		
– Audit services	3	3
– Non-audit services	3	4
Other operating expenses	1,120	1,203
	7,589	7,528

NOTES TO THE INTERIM FINANCIAL INFORMATION

14. Net (loss)/gain from disposal of/fair value adjustments on investment properties

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Net (loss)/gain from fair value adjustments on investment properties	(507)	657

15. Net (loss)/gain from disposal/revaluation of properties, plant and equipment

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Net loss from disposal of equipment, fixtures and fittings	(1)	(1)
Net (loss)/gain from revaluation of premises	(2)	2
	(3)	1

16. Taxation

Taxation in the income statement represents:

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Current tax		
Hong Kong profits tax		
– Current period taxation	3,028	3,035
– Under-provision in prior periods	2	–
	3,030	3,035
Overseas taxation		
– Current period taxation	259	360
– Over-provision in prior periods	(7)	(25)
	3,282	3,370
Deferred tax		
Origination and reversal of temporary differences and unused tax credits	(219)	(94)
	3,063	3,276

Hong Kong profits tax has been provided at the rate of 16.5% (2019: 16.5%) on the estimated assessable profits arising in Hong Kong for the first half of 2020. Taxation on overseas profits has been calculated on the estimated assessable profits for the first half of 2020 at the rates of taxation prevailing in the countries/regions in which the Group operates.

NOTES TO THE INTERIM FINANCIAL INFORMATION

16. Taxation (continued)

The taxation on the Group's profit before taxation that differs from the theoretical amount that would arise using the taxation rate of Hong Kong is as follows:

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Profit before taxation	19,224	21,552
Calculated at a taxation rate of 16.5% (2019: 16.5%)	3,172	3,556
Effect of different taxation rates in other countries/regions	56	132
Income not subject to taxation	(317)	(683)
Expenses not deductible for taxation purposes	284	327
Utilisation of previously unrecognised tax losses	–	(1)
Over-provision in prior periods	(5)	(25)
Foreign withholding tax	(13)	85
Others	(114)	(115)
Taxation charge	3,063	3,276
Effective tax rate	15.9%	15.2%

17. Dividends

	Half-year ended 30 June 2020		Half-year ended 30 June 2019	
	Per share HK\$	Total HK\$'m	Per share HK\$	Total HK\$'m
Interim dividend	0.447	4,726	0.545	5,762

At a meeting held on 30 August 2020, the Board declared an interim dividend of HK\$0.447 per ordinary share for the first half of 2020 amounting to approximately HK\$4,726 million. This declared interim dividend is not reflected as a dividend payable in this interim financial information, but will be reflected as an appropriation of retained earnings for the year ending 31 December 2020.

18. Earnings per share

The calculation of basic earnings per share for the first half of 2020 is based on the consolidated profit for the period attributable to equity holders of the Company of approximately HK\$15,209 million (first half of 2019: HK\$17,254 million) and on the ordinary shares in issue of 10,572,780,266 shares (2019: 10,572,780,266 ordinary shares).

There was no dilution of earnings per share as no potential ordinary shares were in issue for the first half of 2020 (first half of 2019: Nil).

19. Retirement benefit costs

Retirement benefits are provided to eligible employees of the Group. In Hong Kong, defined contribution schemes for the Group's employees are ORSO schemes exempted under the MPF Schemes Ordinance and the BOC-Prudential Easy Choice MPF Scheme.

NOTES TO THE INTERIM FINANCIAL INFORMATION

19. Retirement benefit costs (continued)

Under the ORSO schemes, employees make monthly contributions to the ORSO schemes equal to 5% of their basic salaries, while the employer makes monthly contributions equal to 5% to 15% of the employees' monthly basic salaries, depending on years of service. The employees are entitled to receive 100% of the employer's contributions upon retirement, early retirement or termination of employment after completing 10 years of service. Employees with 3 to 9 years of service are entitled to receive the employer's contributions at a scale ranging from 30% to 90% upon termination of employment for other reasons other than summary dismissal. All employer's contributions received by employee are subject to MPF Schemes Ordinance.

With the implementation of the MPF Schemes Ordinance on 1 December 2000, the Group also launched the MPF Scheme according to the regulatory requirement. Since 2019, employees with 5 years of service or above are entitled to employer's voluntary contribution. The trustee of the Scheme is BOCI-Prudential Trustee and the investment manager is BOCI-Prudential Manager, which are related parties of the Company.

The Group's total contributions made to the ORSO schemes for the first half of 2020 amounted to approximately HK\$188 million (first half of 2019: approximately HK\$178 million), after a deduction of forfeited contributions of approximately HK\$4 million (first half of 2019: approximately HK\$4 million). For the MPF Scheme, the Group contributed approximately HK\$66 million (first half of 2019: approximately HK\$58 million) for the first half of 2020.

20. Cash and balances and placements with banks and other financial institutions

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Cash	16,763	19,028
Balances with central banks	178,535	150,249
Placements with central banks maturing within one month	32,806	9,541
Placements with central banks maturing between one and twelve months	4,013	2,444
Placements with central banks maturing over one year	1,175	785
	216,529	163,019
Balances with other banks and other financial institutions	57,387	75,518
Placements with other banks and other financial institutions maturing within one month	70,405	81,101
Placements with other banks and other financial institutions maturing between one and twelve months	48,592	28,166
	176,384	184,785
	409,676	366,832
Impairment allowances		
– Stage 1	(18)	(3)
– Stage 2	–	–
– Stage 3	–	–
	409,658	366,829

NOTES TO THE INTERIM FINANCIAL INFORMATION

21. Financial assets at fair value through profit or loss

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Securities		
Trading assets		
– Treasury bills	14,081	21,025
– Certificates of deposit	2,129	2,953
– Other debt securities	7,632	13,612
	23,842	37,590
– Equity securities	56	37
	23,898	37,627
Other financial assets mandatorily classified at fair value through profit or loss		
– Certificates of deposit	–	2
– Other debt securities	15,794	27,521
	15,794	27,523
– Equity securities	4,623	2,618
– Fund	6,954	9,137
	27,371	39,278
Financial assets designated at fair value through profit or loss		
– Certificates of deposit	–	–
– Other debt securities	3,112	2,991
	3,112	2,991
Total securities	54,381	79,896
Other debt instruments		
Trading assets	3,594	5,297
	57,975	85,193

NOTES TO THE INTERIM FINANCIAL INFORMATION

21. Financial assets at fair value through profit or loss (continued)

Total securities are analysed by place of listing as follows:

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Debt securities and certificates of deposit		
– Listed in Hong Kong	9,288	14,901
– Listed outside Hong Kong	9,504	14,036
– Unlisted	23,956	39,167
	42,748	68,104
Equity securities		
– Listed in Hong Kong	2,547	1,500
– Listed outside Hong Kong	2,132	1,155
	4,679	2,655
Fund		
– Listed in Hong Kong	414	–
– Listed outside Hong Kong	493	–
– Unlisted	6,047	9,137
	6,954	9,137
Total securities	54,381	79,896

Total securities are analysed by type of issuer as follows:

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Sovereigns	20,508	30,812
Public sector entities	1,478	1,526
Banks and other financial institutions	20,268	33,665
Corporate entities	12,127	13,893
Total securities	54,381	79,896

NOTES TO THE INTERIM FINANCIAL INFORMATION

22. Derivative financial instruments

The Group enters into exchange rate, interest rate, commodity, equity and credit related derivative financial instrument contracts for trading and risk management purposes.

Currency forwards represent commitments to purchase and sell foreign currency on a future date. Interest rate futures are contractual obligations to receive or pay a net amount based on changes in interest rates or buy or sell interest rate financial instruments on a future date at an agreed price in the financial market under the administration of the stock exchange. Forward rate agreements are individually negotiated interest rate futures that call for a cash settlement at a future date for the difference between a contract rate of interest and the current market rate, based on a notional principal amount.

Currency, interest rate and commodity swaps are commitments to exchange one set of cash flows or commodity for another. Swaps result in an exchange of currencies, interest rates (for example, fixed rate for floating rate), or precious metals (for example, silver swaps) or a combination of all these (for example, cross-currency interest rate swaps). Except for certain currency swap contracts, no exchange of principal takes place.

Foreign currency, interest rate, precious metal and equity options are contractual agreements under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, either to buy (a call option) or sell (a put option) at or by a set date or during a set period, a specific amount of the financial instrument at a predetermined price. In consideration for the assumption of foreign exchange and interest rate risk, the seller receives a premium from the purchaser. Options are negotiated over-the-counter between the Group and its counterparty or traded through the stock exchange (for example, exchange-traded stock option).

The contract/notional amounts and fair values of derivative financial instruments held by the Group are set out in the following tables. The contract/notional amounts of these instruments indicate the volume of transactions outstanding at the balance sheet dates and certain of them provide a basis for comparison with the fair values of instruments recognised on the balance sheet. However, they do not necessarily indicate the amounts of future cash flows involved or the current fair values of the instruments and, therefore, do not indicate the Group's exposure to credit or market risks. The derivative financial instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in foreign exchange rates, market interest rates, commodity prices or equity prices relative to their terms. The aggregate fair values of derivative financial instruments can fluctuate significantly from time to time.

NOTES TO THE INTERIM FINANCIAL INFORMATION

22. Derivative financial instruments (continued)

The following tables summarise the contract/notional amounts and fair values of each class of derivative financial instrument as at 30 June 2020 and 31 December 2019:

	At 30 June 2020		
	Contract/ notional amounts HK\$'m	Fair values	
		Assets HK\$'m	Liabilities HK\$'m
Exchange rate contracts			
Spot, forwards and futures	285,134	12,541	(8,325)
Swaps	1,470,679	7,568	(6,661)
Options	35,722	79	(71)
	1,791,535	20,188	(15,057)
Interest rate contracts			
Futures	1,381	1	(1)
Swaps	1,212,907	21,426	(32,385)
Options	4,698	–	–
	1,218,986	21,427	(32,386)
Commodity contracts	50,418	2,571	(5,546)
Equity contracts	3,597	79	(86)
Credit derivative contracts	–	–	–
	3,064,536	44,265	(53,075)

	At 31 December 2019		
	Contract/ notional amounts HK\$'m	Fair values	
		Assets HK\$'m	Liabilities HK\$'m
Exchange rate contracts			
Spot, forwards and futures	315,793	11,814	(8,082)
Swaps	1,556,697	10,849	(10,108)
Options	49,544	132	(100)
	1,922,034	22,795	(18,290)
Interest rate contracts			
Futures	2,318	2	(29)
Swaps	1,223,157	7,462	(12,002)
Options	3,114	–	–
	1,228,589	7,464	(12,031)
Commodity contracts	48,446	756	(2,576)
Equity contracts	1,317	12	(15)
Credit derivative contracts	389	–	(9)
	3,200,775	31,027	(32,921)

NOTES TO THE INTERIM FINANCIAL INFORMATION

23. Advances and other accounts

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Personal loans and advances	435,131	415,874
Corporate loans and advances	1,068,620	980,009
Advances to customers	1,503,751	1,395,883
Less: Impairment allowances		
– Stage 1	(5,390)	(4,563)
– Stage 2	(325)	(297)
– Stage 3	(2,341)	(2,175)
	1,495,695	1,388,848
Trade bills	13,267	20,727
Less: Impairment allowances		
– Stage 1	(1)	(1)
– Stage 2	–	–
– Stage 3	–	–
	13,266	20,726
Advances to banks and other financial institutions	1,403	3,387
Less: Impairment allowances		
– Stage 1	(1)	–
– Stage 2	–	–
– Stage 3	–	–
	1,402	3,387
	1,510,363	1,412,961

As at 30 June 2020, advances to customers included accrued interest of HK\$2,275 million (31 December 2019: HK\$2,751 million).

NOTES TO THE INTERIM FINANCIAL INFORMATION

24. Investment in securities

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Investment in securities at fair value through other comprehensive income		
– Treasury bills	243,715	234,284
– Certificates of deposit	47,496	51,167
– Other debt securities	410,774	399,251
	701,985	684,702
– Equity securities	6,177	5,968
	708,162	690,670
Investment in securities at amortised cost		
– Certificates of deposit	924	1,526
– Other debt securities	120,853	109,503
	121,777	111,029
– Impairment allowances		
Stage 1	(53)	(46)
Stage 2	–	–
Stage 3	–	–
	121,724	110,983
	829,886	801,653

NOTES TO THE INTERIM FINANCIAL INFORMATION

24. Investment in securities (continued)

Investment in securities is analysed by place of listing as follows:

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Investment in securities at fair value through other comprehensive income		
Debt securities and certificates of deposit		
– Listed in Hong Kong	82,318	69,523
– Listed outside Hong Kong	202,728	187,072
– Unlisted	416,939	428,107
	701,985	684,702
Equity securities		
– Listed in Hong Kong	3,037	3,207
– Listed outside Hong Kong	1,018	607
– Unlisted	2,122	2,154
	6,177	5,968
	708,162	690,670
Investment in securities at amortised cost		
Debt securities and certificates of deposit		
– Listed in Hong Kong	24,337	19,664
– Listed outside Hong Kong	58,825	55,151
– Unlisted	38,562	36,168
	121,724	110,983
	829,886	801,653
Market value of listed securities at amortised cost	87,552	77,394

Investment in securities is analysed by type of issuer as follows:

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Sovereigns	355,077	357,468
Public sector entities	42,027	46,790
Banks and other financial institutions	241,298	221,098
Corporate entities	191,484	176,297
	829,886	801,653

NOTES TO THE INTERIM FINANCIAL INFORMATION

25. Investment properties

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
At 1 January	20,110	19,684
Additions	4	35
Fair value (losses)/gains	(507)	282
Reclassification (to)/from properties, plant and equipment (Note 26)	(28)	109
At period/year end	19,579	20,110

26. Properties, plant and equipment

	Equipment, fixtures and Right-of-use			Total HK\$'m
	Premises HK\$'m	fittings HK\$'m	assets HK\$'m	
Net book value at 1 January 2020	46,342	3,331	1,929	51,602
Additions	8	431	244	683
Disposals	–	(9)	–	(9)
Revaluation	(547)	–	–	(547)
Depreciation for the period (Note 13)	(588)	(553)	(388)	(1,529)
Reclassification from investment properties (Note 25)	28	–	–	28
Exchange difference	(4)	(7)	(9)	(20)
Net book value at 30 June 2020	45,239	3,193	1,776	50,208
At 30 June 2020				
Cost or valuation	45,239	11,538	2,769	59,546
Accumulated depreciation and impairment	–	(8,345)	(993)	(9,338)
Net book value at 30 June 2020	45,239	3,193	1,776	50,208
The analysis of cost or valuation of the above assets is as follows:				
At 30 June 2020				
At cost	–	11,538	2,769	14,307
At valuation	45,239	–	–	45,239
	45,239	11,538	2,769	59,546

NOTES TO THE INTERIM FINANCIAL INFORMATION

26. Properties, plant and equipment (continued)

	Premises HK\$'m	Equipment, fixtures and fittings HK\$'m	Right-of-use assets HK\$'m	Total HK\$'m
Net book value at 1 January 2019	46,390	3,045	1,757	51,192
Additions	147	1,303	877	2,327
Disposals	–	(8)	–	(8)
Revaluation	1,070	–	–	1,070
Depreciation for the year	(1,157)	(1,013)	(711)	(2,881)
Reclassification to investment properties (Note 25)	(109)	–	–	(109)
Exchange difference	1	4	6	11
Net book value at 31 December 2019	46,342	3,331	1,929	51,602
At 31 December 2019				
Cost or valuation	46,342	11,487	2,640	60,469
Accumulated depreciation and impairment	–	(8,156)	(711)	(8,867)
Net book value at 31 December 2019	46,342	3,331	1,929	51,602
The analysis of cost or valuation of the above assets is as follows:				
At 31 December 2019				
At cost	–	11,487	2,640	14,127
At valuation	46,342	–	–	46,342
	46,342	11,487	2,640	60,469

27. Other assets

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Reposessed assets	18	7
Precious metals	7,642	9,261
Reinsurance assets	52,499	48,614
Accounts receivable and prepayments	67,585	33,148
	127,744	91,030

28. Financial liabilities at fair value through profit or loss

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Trading liabilities		
– Short positions in Exchange Fund Bills and Notes	10,658	19,206
– Others	200	–
	10,858	19,206

NOTES TO THE INTERIM FINANCIAL INFORMATION

29. Deposits from customers

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Demand deposits and current accounts		
– Corporate	217,117	138,646
– Personal	76,211	68,367
	293,328	207,013
Savings deposits		
– Corporate	447,133	400,903
– Personal	549,082	499,106
	996,215	900,009
Time, call and notice deposits		
– Corporate	497,104	517,080
– Personal	353,789	385,171
	850,893	902,251
	2,140,436	2,009,273

30. Debt securities and certificates of deposit in issue

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
At amortised cost		
– Certificates of deposit	–	116

31. Other accounts and provisions

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Dividend payable	10,488	–
Other accounts payable	112,329	78,197
Lease liabilities	1,731	1,850
Impairment allowances on loan commitments and financial guarantee contracts		
– Stage 1	477	535
– Stage 2	22	22
– Stage 3	19	20
	125,066	80,624

NOTES TO THE INTERIM FINANCIAL INFORMATION

32. Deferred taxation

Deferred tax is recognised in respect of the temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in this interim financial information and unused tax credits in accordance with HKAS 12 “Income Taxes”.

The major components of deferred tax (assets)/liabilities recorded in the balance sheet, and the movements during the first half of 2020 and the year ended 31 December 2019 are as follows:

	At 30 June 2020					
	Accelerated tax depreciation	Property revaluation	Losses	Impairment allowances	Others	Total
	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m
At 1 January 2020	756	6,997	–	(804)	(532)	6,417
(Credited)/charged to income statement (Note 16)	(6)	(55)	(8)	(190)	40	(219)
(Credited)/charged to other comprehensive income	–	(112)	–	–	267	155
Release upon disposal of equity instruments at fair value through other comprehensive income	–	–	–	–	22	22
Release upon redemption of financial liabilities designated at fair value through profit or loss	–	–	–	–	6	6
Exchange difference	–	–	–	–	1	1
At 30 June 2020	750	6,830	(8)	(994)	(196)	6,382

	At 31 December 2019					
	Accelerated tax depreciation	Property revaluation	Losses	Impairment allowances	Others	Total
	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m
At 1 January 2019	706	6,991	–	(724)	(1,478)	5,495
Charged/(credited) to income statement	50	(127)	–	(80)	12	(145)
Charged to other comprehensive income	–	133	–	–	927	1,060
Release upon disposal of equity instruments at fair value through other comprehensive income	–	–	–	–	7	7
At 31 December 2019	756	6,997	–	(804)	(532)	6,417

NOTES TO THE INTERIM FINANCIAL INFORMATION

32. Deferred taxation (continued)

Deferred tax assets and liabilities are offset on an individual entity basis when there is a legal right to set off current tax assets against current tax liabilities and when the deferred taxation relates to the same authority. The following amounts, determined after appropriate offsetting, are shown in the balance sheet:

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Deferred tax assets	(64)	(63)
Deferred tax liabilities	6,446	6,480
	6,382	6,417

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Deferred tax assets to be recovered after more than twelve months	(70)	(43)
Deferred tax liabilities to be settled after more than twelve months	6,633	6,971
	6,563	6,928

As at 30 June 2020, the Group has no unrecognised deferred tax assets in respect of tax losses (31 December 2019: the Group has not recognised deferred tax assets in respect of tax losses amounting to HK\$9 million). All of the amount for the Group has no expiry date under the current tax legislation in different countries/regions.

33. Insurance contract liabilities

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
At 1 January	117,269	104,723
Benefits paid	(7,094)	(15,373)
Claims incurred and movement in liabilities	15,563	27,919
At period/year end	125,738	117,269

The insurance contract liabilities that are covered by reinsurance arrangements amounted to HK\$42,569 million (31 December 2019: HK\$40,130 million) and the associated reinsurance assets of HK\$52,499 million (31 December 2019: HK\$48,614 million) are included in "Other assets" (Note 27).

NOTES TO THE INTERIM FINANCIAL INFORMATION

34. Subordinated liabilities

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Subordinated notes – designated at fair value through profit or loss	–	12,954

Listed subordinated notes with aggregate principal amount of USD1,623 million, interest rate at 5.55% per annum payable semi-annually, has been fully repaid in February 2020. Amounts qualified as Tier 2 capital instruments for regulatory purposes are shown in Note 3.5(B). The carrying amount of subordinated notes designated at fair value through profit or loss as at 31 December 2019 was more than the amount that the Group would be contractually required to pay at maturity to the holders by HK\$41 million.

35. Share capital

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Issued and fully paid: 10,572,780,266 ordinary shares	52,864	52,864

36. Other equity instruments

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Undated non-cumulative subordinated Additional Tier 1 capital securities	23,476	23,476

In September 2018, BOCHK issued USD3,000 million undated non-cumulative subordinated Additional Tier 1 capital securities. The capital securities are perpetual securities in respect of which there is no fixed redemption date and are not callable within the first 5 years. They have an initial rate of distribution of 5.90% per annum payable semi-annually which may be cancelled at the sole discretion of BOCHK. Dividend paid to other equity instrument holders in the first half of 2020 amounted to HK\$689 million.

NOTES TO THE INTERIM FINANCIAL INFORMATION

37. Notes to condensed consolidated cash flow statement

(a) Reconciliation of operating profit to operating cash inflow/(outflow) before taxation

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Operating profit	19,788	20,848
Depreciation	1,529	1,402
Net charge of impairment allowances	1,366	793
Unwind of discount on impairment allowances	(4)	–
Advances written off net of recoveries	(229)	(106)
Interest expense on lease liabilities	28	27
Change in subordinated liabilities	–	227
Change in balances and placements with banks and other financial institutions with original maturity over three months	(6,858)	(11,380)
Change in financial assets at fair value through profit or loss	28,839	(13,061)
Change in derivative financial instruments	6,916	8,449
Change in advances and other accounts	(98,424)	(87,902)
Change in investment in securities	(9,465)	(181,429)
Change in other assets	(36,728)	(13,900)
Change in deposits and balances from banks and other financial institutions	2,595	(133,642)
Change in financial liabilities at fair value through profit or loss	(8,348)	3,540
Change in deposits from customers	131,163	122,427
Change in debt securities and certificates of deposit in issue	(116)	(8,661)
Change in other accounts and provisions	34,132	13,527
Change in insurance contract liabilities	8,469	8,277
Effect of changes in exchange rates	2,799	(3,617)
Operating cash inflow/(outflow) before taxation	77,452	(274,181)
Cash flows from operating activities included		
– interest received	30,958	33,813
– interest paid	11,495	12,679
– dividend received	124	124

NOTES TO THE INTERIM FINANCIAL INFORMATION

37. Notes to condensed consolidated cash flow statement (continued)

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

	At 30 June 2020 HK\$'m	At 30 June 2019 HK\$'m
Cash and balances and placements with banks and other financial institutions with original maturity within three months	358,862	320,755
Treasury bills, certificates of deposit and other debt instruments with original maturity within three months		
– financial assets at fair value through profit or loss	8,248	3,307
– investment in securities	19,287	17,578
	386,397	341,640

38. Contingent liabilities and commitments

The following is a summary of the contractual amounts of each significant class of contingent liability and commitment and the aggregate credit risk-weighted amount and is prepared with reference to the completion instructions for the HKMA return of capital adequacy ratio.

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Direct credit substitutes	3,856	5,455
Transaction-related contingencies	30,392	29,080
Trade-related contingencies	25,899	27,865
Commitments that are unconditionally cancellable without prior notice	487,710	447,055
Other commitments with an original maturity of		
– up to one year	14,269	13,772
– over one year	153,841	160,575
	715,967	683,802
Credit risk-weighted amount	69,684	76,911

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

NOTES TO THE INTERIM FINANCIAL INFORMATION

39. Capital commitments

The Group has the following outstanding capital commitments not provided for in this interim financial information:

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Authorised and contracted for but not provided for	172	188
Authorised but not contracted for	232	72
	404	260

The above capital commitments mainly relate to commitments to purchase computer equipment and software, and to renovate the Group's premises.

40. Operating lease commitments

As lessor

The Group has contracted with tenants for the following future minimum lease receivables under non-cancellable operating leases:

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Properties and equipment		
– Not later than one year	530	552
– One to two years	349	389
– Two to three years	142	187
– Three to four years	21	33
– Four to five years	9	1
– Later than five years	6	–
	1,057	1,162

The Group leases its investment properties under operating lease arrangements, with leases typically for a period from one to three years. The terms of the leases generally require the tenants to pay security deposits and provide for rent adjustments according to the prevailing market conditions upon the lease renewal.

NOTES TO THE INTERIM FINANCIAL INFORMATION

41. Segmental reporting

The Group manages the business mainly from a business segment perspective and over 90% of the Group's revenues, profits before tax and assets are derived from Hong Kong. Currently, four operating segments are identified: Personal Banking, Corporate Banking, Treasury and Insurance. The classification of the Group's operating segments is based on customer segment and product type, which is aligned with the RPC (relationship, product and channel) management model of the Group.

Both Personal Banking and Corporate Banking provide general banking services including various deposit products, overdrafts, loans, credit cards, trade related products and other credit facilities, investment and insurance products, and foreign currency and derivative products. Personal Banking mainly serves retail customers and small enterprises, while Corporate Banking mainly deals with corporate customers. Treasury manages the funding and liquidity, and the interest rate and foreign exchange positions of the Group in addition to proprietary trades. The Insurance segment represents business mainly relating to life insurance products, including individual life insurance and group life insurance products. "Others" mainly represents the Group's holdings of premises, investment properties, equity investments, certain interests in associates and joint ventures and the businesses of the Southeast Asian entities.

Measurement of segment assets, liabilities, income, expenses, results and capital expenditure is based on the Group's accounting policies. The segment information includes items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Inter-segment funding is charged according to the internal funds transfer pricing mechanism of the Group, which is primarily based on market rates with the consideration of specific features of the product.

As the Group derives a majority of revenue from interest and the senior management relies primarily on net interest income in managing the business, interest income and expense for all reportable segments are presented on a net basis. Under the same consideration, insurance premium income and insurance benefits and claims are also presented on a net basis.

NOTES TO THE INTERIM FINANCIAL INFORMATION

41. Segmental reporting (continued)

	Personal Banking HK\$'m	Corporate Banking HK\$'m	Treasury HK\$'m	Insurance HK\$'m	Others HK\$'m	Subtotal HK\$'m	Eliminations HK\$'m	Consolidated HK\$'m
Half-year ended 30 June 2020								
Net interest income/(expense)								
– External	373	8,363	7,205	1,701	994	18,636	–	18,636
– Inter-segment	5,375	(1,755)	(3,045)	(8)	(567)	–	–	–
	5,748	6,608	4,160	1,693	427	18,636	–	18,636
Net fee and commission income/(expense)	3,339	1,960	115	(308)	528	5,634	(199)	5,435
Net insurance premium income	–	–	–	7,927	–	7,927	(11)	7,916
Net trading gain/(loss)	465	721	916	(26)	219	2,295	35	2,330
Net gain/(loss) on other financial instruments at fair value through profit or loss	–	–	151	49	(3)	197	5	202
Net gain on other financial assets	–	10	2,496	65	–	2,571	–	2,571
Other operating income	16	4	23	73	1,040	1,156	(692)	464
Total operating income	9,568	9,303	7,861	9,473	2,211	38,416	(862)	37,554
Net insurance benefits and claims and movement in liabilities	–	–	–	(8,811)	–	(8,811)	–	(8,811)
Net operating income before impairment allowances	9,568	9,303	7,861	662	2,211	29,605	(862)	28,743
Net charge of impairment allowances	(630)	(561)	(84)	(23)	(68)	(1,366)	–	(1,366)
Net operating income	8,938	8,742	7,777	639	2,143	28,239	(862)	27,377
Operating expenses	(4,609)	(1,584)	(562)	(247)	(1,449)	(8,451)	862	(7,589)
Operating profit	4,329	7,158	7,215	392	694	19,788	–	19,788
Net loss from disposal of/fair value adjustments on investment properties	–	–	–	–	(507)	(507)	–	(507)
Net loss from disposal/revaluation of properties, plant and equipment	(2)	–	–	–	(1)	(3)	–	(3)
Share of profits less losses after tax of associates and joint ventures	25	–	2	–	(81)	(54)	–	(54)
Profit before taxation	4,352	7,158	7,217	392	105	19,224	–	19,224
At 30 June 2020								
ASSETS								
Segment assets	460,942	1,025,662	1,446,472	164,982	163,478	3,261,536	(36,388)	3,225,148
Interests in associates and joint ventures	584	–	3	–	991	1,578	–	1,578
	461,526	1,025,662	1,446,475	164,982	164,469	3,263,114	(36,388)	3,226,726
LIABILITIES								
Segment liabilities	1,115,488	1,004,391	565,593	154,409	110,229	2,950,110	(36,388)	2,913,722
Half-year ended 30 June 2020								
Other information								
Capital expenditure	3	1	–	36	647	687	–	687
Depreciation	651	137	54	31	674	1,547	(18)	1,529
Amortisation of securities	–	–	112	177	31	320	–	320

NOTES TO THE INTERIM FINANCIAL INFORMATION

41. Segmental reporting (continued)

	Personal Banking HK\$'m	Corporate Banking HK\$'m	Treasury HK\$'m	Insurance HK\$'m	Others HK\$'m	Subtotal HK\$'m	Eliminations HK\$'m	Consolidated HK\$'m
Half-year ended 30 June 2019								
Net interest income/(expense)								
– External	4	7,564	9,547	1,580	1,208	19,903	–	19,903
– Inter-segment	6,881	(226)	(5,943)	(8)	(704)	–	–	–
	6,885	7,338	3,604	1,572	504	19,903	–	19,903
Net fee and commission income/(expense)	3,620	2,247	228	(440)	583	6,238	(192)	6,046
Net insurance premium income	–	–	–	9,406	–	9,406	(10)	9,396
Net trading gain/(loss)	386	713	979	(438)	162	1,802	27	1,829
Net (loss)/gain on other financial instruments at fair value through profit or loss	(1)	–	136	2,075	1	2,211	4	2,215
Net (loss)/gain on other financial assets	–	(2)	729	(11)	–	716	–	716
Other operating income	28	–	11	65	1,068	1,172	(671)	501
Total operating income	10,918	10,296	5,687	12,229	2,318	41,448	(842)	40,606
Net insurance benefits and claims and movement in liabilities	–	–	–	(11,437)	–	(11,437)	–	(11,437)
Net operating income before impairment allowances	10,918	10,296	5,687	792	2,318	30,011	(842)	29,169
Net (charge)/reversal of impairment allowances	(88)	(675)	(44)	(2)	16	(793)	–	(793)
Net operating income	10,830	9,621	5,643	790	2,334	29,218	(842)	28,376
Operating expenses	(4,430)	(1,556)	(570)	(239)	(1,575)	(8,370)	842	(7,528)
Operating profit	6,400	8,065	5,073	551	759	20,848	–	20,848
Net gain from disposal of/fair value adjustments on investment properties	–	–	–	–	657	657	–	657
Net gain from disposal/revaluation of properties, plant and equipment	–	–	–	–	1	1	–	1
Share of profits less losses after tax of associates and joint ventures	54	–	1	–	(9)	46	–	46
Profit before taxation	6,454	8,065	5,074	551	1,408	21,552	–	21,552
At 31 December 2019								
ASSETS								
Segment assets	442,694	947,164	1,354,356	153,116	155,953	3,053,283	(28,859)	3,024,424
Interests in associates and joint ventures	559	–	1	–	1,072	1,632	–	1,632
	443,253	947,164	1,354,357	153,116	157,025	3,054,915	(28,859)	3,026,056
LIABILITIES								
Segment liabilities	1,079,821	907,381	521,210	143,011	96,000	2,747,423	(28,859)	2,718,564
Half-year ended 30 June 2019								
Other information								
Capital expenditure	35	1	1	21	1,139	1,197	–	1,197
Depreciation	561	110	50	27	654	1,402	–	1,402
Amortisation of securities	–	–	925	30	(34)	921	–	921

NOTES TO THE INTERIM FINANCIAL INFORMATION

42. Assets pledged as security

As at 30 June 2020, the liabilities of the Group amounting to HK\$8,915 million (31 December 2019: HK\$15,862 million) were secured by assets deposited with central depositories to facilitate settlement operations. In addition, the liabilities of the Group amounting to HK\$75,190 million (31 December 2019: HK\$60,562 million) were secured by debt securities related to sale and repurchase arrangements. The amount of assets pledged by the Group to secure these liabilities was HK\$85,146 million (31 December 2019: HK\$76,656 million) mainly included in “Financial assets at fair value through profit or loss” and “Investment in securities”.

43. Significant related party transactions

The Group is subject to the control of the State Council of the PRC Government through China Investment Corporation (“CIC”), its wholly-owned subsidiary Central Huijin Investment Ltd. (“Central Huijin”), and BOC in which Central Huijin has controlling equity interests.

(a) Transactions with the parent companies and the other companies controlled by the parent companies

General information of the parent companies:

The Group is controlled by BOC. Central Huijin is the controlling entity of BOC, and it is a wholly-owned subsidiary of CIC which is a wholly state-owned company engaging in foreign currency investment management.

Central Huijin has controlling equity interests in certain other entities in the PRC.

The Group enters into banking and other transactions with these entities in the normal course of business which include loans, investment securities, money market and reinsurance transactions.

The majority of transactions with BOC arise from money market activities. As at 30 June 2020, the related aggregate amounts due from and to BOC of the Group were HK\$85,773 million (31 December 2019: HK\$98,066 million) and HK\$63,711 million (31 December 2019: HK\$56,995 million) respectively. The aggregate amounts of income and expenses of the Group arising from these transactions with BOC for the first half of 2020 were HK\$493 million (first half of 2019: HK\$1,160 million) and HK\$119 million (first half of 2019: HK\$347 million) respectively.

Transactions with other companies controlled by BOC are not considered material.

(b) Transactions with government authorities, agencies, affiliates and other state controlled entities

The Group is subject to the control of the State Council of the PRC Government through CIC and Central Huijin, which also directly or indirectly controls a significant number of entities through its government authorities, agencies, affiliates and other state controlled entities. The Group enters into banking transactions with government authorities, agencies, affiliates and other state controlled entities in the normal course of business at commercial terms.

NOTES TO THE INTERIM FINANCIAL INFORMATION

43. Significant related party transactions (continued)

(b) Transactions with government authorities, agencies, affiliates and other state controlled entities (continued)

These transactions include, but are not limited to, the following:

- lending, provision of credits and guarantees, and deposit taking;
- inter-bank balance taking and placing;
- sales, purchases, underwriting and redemption of bonds issued by other state controlled entities;
- rendering of foreign exchange, remittance and investment related services;
- provision of fiduciary activities; and
- purchase of utilities, transport, telecommunication and postage services.

(c) Summary of transactions entered into during the ordinary course of business with associates, joint ventures and other related parties

The aggregate income/expenses and balances arising from related party transactions with associates, joint ventures and other related parties of the Group are summarised as follows:

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Income statement items		
Associates and joint ventures		
– Fee and commission income	20	–
– Interest expenses	–	2
– Fee and commission expenses	–	4
– Other operating expenses	40	41
Other related parties		
– Fee and commission income	6	5

	At 30 June 2020 HK\$'m	At 31 December 2019 HK\$'m
Balance sheet items		
Associates and joint ventures		
– Other assets	6	–
– Deposits and balances from banks and other financial institutions	75	96
– Deposits from customers	139	–
– Other accounts and provisions	–	1

NOTES TO THE INTERIM FINANCIAL INFORMATION

43. Significant related party transactions (continued)

(d) Key management personnel

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, including directors and senior management. The Group accepts deposits from and grants loans and credit facilities to key management personnel in the ordinary course of business. During both the current and prior periods, no material transaction was conducted with key management personnel of the Company and its holding companies, as well as parties related to them.

The compensation of key management personnel is detailed as follows:

	Half-year ended 30 June 2020 HK\$'m	Half-year ended 30 June 2019 HK\$'m
Salaries and other short-term employee benefits	20	18

44. International claims

The below analysis is prepared with reference to the completion instructions for the HKMA return of international banking statistics. International claims are exposures to counterparties on which the ultimate risk lies based on the locations of the counterparties after taking into account the transfer of risk, and represent the sum of cross-border claims in all currencies and local claims in foreign currencies. For a claim guaranteed by a party situated in a location different from the counterparty, the risk will be transferred to the location of the guarantor. For a claim on an overseas branch of a bank whose head office is located in another location, the risk will be transferred to the location where its head office is located.

Claims on individual countries/regions, after risk transfer, amounting to 10% or more of the aggregate international claims of the Group are shown as follows:

	At 30 June 2020				
	Banks HK\$'m	Official sector HK\$'m	Non-bank private sector		Total HK\$'m
			Non-bank financial institutions HK\$'m	Non-financial private sector HK\$'m	
Chinese Mainland	294,850	119,690	20,400	157,188	592,128
Hong Kong	10,015	82	47,530	404,733	462,360
United States	13,024	93,834	24,001	22,452	153,311

	At 31 December 2019				
	Banks HK\$'m	Official sector HK\$'m	Non-bank private sector		Total HK\$'m
			Non-bank financial institutions HK\$'m	Non-financial private sector HK\$'m	
Chinese Mainland	290,330	110,229	21,988	154,714	577,261
Hong Kong	6,842	96	44,230	362,148	413,316
United States	17,219	106,473	22,908	22,146	168,746

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45. Non-bank Mainland exposures

The analysis of non-bank Mainland exposures is based on the categories of non-bank counterparties and the types of direct exposures with reference to the completion instructions for the HKMA return of Mainland activities, which includes the Mainland exposures extended by BOCHK's Hong Kong office only.

	Items in the HKMA return	At 30 June 2020		
		On-balance sheet exposure HK\$'m	Off-balance sheet exposure HK\$'m	Total exposure HK\$'m
Central government, central government-owned entities and their subsidiaries and joint ventures	1	351,918	34,077	385,995
Local governments, local government-owned entities and their subsidiaries and joint ventures	2	66,085	10,225	76,310
PRC nationals residing in Mainland or other entities incorporated in Mainland and their subsidiaries and joint ventures	3	109,558	22,585	132,143
Other entities of central government not reported in item 1 above	4	32,198	4,777	36,975
Other entities of local governments not reported in item 2 above	5	578	–	578
PRC nationals residing outside Mainland or entities incorporated outside Mainland where the credit is granted for use in Mainland	6	89,016	7,940	96,956
Other counterparties where the exposures are considered to be non-bank Mainland exposures	7	1,811	–	1,811
Total	8	651,164	79,604	730,768
Total assets after provision	9	2,994,168		
On-balance sheet exposures as percentage of total assets	10	21.75%		

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45. Non-bank Mainland exposures (continued)

	Items in the HKMA return	At 31 December 2019		
		On-balance sheet exposure HK\$'m	Off-balance sheet exposure HK\$'m	Total exposure HK\$'m
Central government, central government-owned entities and their subsidiaries and joint ventures	1	310,795	43,519	354,314
Local governments, local government-owned entities and their subsidiaries and joint ventures	2	65,697	13,247	78,944
PRC nationals residing in Mainland or other entities incorporated in Mainland and their subsidiaries and joint ventures	3	102,300	21,580	123,880
Other entities of central government not reported in item 1 above	4	32,086	3,735	35,821
Other entities of local governments not reported in item 2 above	5	500	2	502
PRC nationals residing outside Mainland or entities incorporated outside Mainland where the credit is granted for use in Mainland	6	80,635	13,988	94,623
Other counterparties where the exposures are considered to be non-bank Mainland exposures	7	1,770	–	1,770
Total	8	593,783	96,071	689,854
Total assets after provision	9	<u>2,800,915</u>		
On-balance sheet exposures as percentage of total assets	10	<u>21.20%</u>		

NOTES TO THE INTERIM FINANCIAL INFORMATION

46. Compliance with HKAS 34

The unaudited interim financial information for the first half of 2020 complies with HKAS 34 “Interim Financial Reporting” issued by the HKICPA.

47. Statutory accounts

The financial information relating to the year ended 31 December 2019 that is included in this Interim Report as comparative information does not constitute the Company’s statutory annual consolidated financial statements for that year but is derived from those financial statements. Further information relating to these statutory financial statements required to be disclosed in accordance with section 436 of the Hong Kong Companies Ordinance is as follows:

The Company has delivered the financial statements for the year ended 31 December 2019 to the Registrar of Companies as required by section 662(3) of, and Part 3 of Schedule 6 to, the Hong Kong Companies Ordinance.

The Company’s auditor has reported on those financial statements. The auditor’s report was unqualified; did not include a reference to any matters to which the auditor drew attention by way of emphasis without qualifying its report; and did not contain a statement under sections 406(2), 407(2) or (3) of the Hong Kong Companies Ordinance.