

The Hongkong and Shanghai Banking Corporation Limited
New Zealand Banking Group

Disclosure Statement

31 December 2014

HSBC 

Disclosure Statement For the Year Ended 31 December 2014

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General Disclosures

Registered Bank

The Hongkong and Shanghai Banking Corporation Limited (“HBAP”)
1 Queen's Road Central
Hong Kong SAR

HBAP was incorporated in Hong Kong in 1866 under the Laws of Hong Kong.

New Zealand Branch

The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch (“Branch”) is defined as the New Zealand business of HBAP (overseas incorporated bank).

New Zealand Head Office:

1 Queen Street
Auckland
New Zealand

New Zealand Banking Group

The New Zealand Banking Group (“Banking Group”) is the New Zealand operations of HBAP and all New Zealand incorporated subsidiaries of HBAP and controlled structured entities. The entities that have been considered for aggregation to form the Banking Group are detailed in the Statement of Accounting Policies.

Overseas Banking Group

The Overseas Banking Group (“HBAP Group”) includes all entities consolidated for the purposes of public reporting of Group financial statements in Hong Kong including HBAP and its subsidiaries and associated companies.

Ultimate Holding Company

The ultimate holding company of HBAP is:

HSBC Holdings plc
8 Canada Square
London E14 5HQ
United Kingdom

Access to parental disclosures

The most recent publicly available financial statements of HBAP Group and HSBC Holdings plc can be found at HSBC Holdings plc’s website, www.hsbc.com under Investor Relations, Financial and regulatory reports.

Ranking of Local Creditors in a Winding-up

Under Section 265(1) (db) of the Companies Ordinance of the Hong Kong SAR which HBAP is subject to, in the event of a winding up of HBAP, there shall be paid in priority to all other unsecured debts the aggregate amount held on deposit, up to a maximum of HKD 500,000, to each depositor and that this Section has no geographic limitation. Save as aforesaid, the Directors believe that no other material legislative or regulatory restrictions exist which subordinate the claims of any class of the Banking Group’s unsecured creditors on the global assets of HBAP to those of any other class of unsecured creditors of HBAP, in a winding up of HBAP.

Guarantee Arrangements

No material obligations of HBAP that relate to the Branch are guaranteed as at the date of signing this Disclosure Statement.

Government Guarantee

No obligations of HBAP that relate to the Branch are guaranteed under a government guarantee as at the date of signing this Disclosure Statement.

General Disclosures *(continued)*

Other Material Matters

There are no material matters that, if disclosed, would adversely affect the decision of a person to subscribe for Debt Securities of which HBAP and the Banking Group is the issuer.

Pending Proceedings and Arbitration

HBAP is named in and is defending legal actions in various jurisdictions arising from its normal business.

Auditor

New Zealand Banking Group

KPMG
KPMG Centre
18 Viaduct Harbour Avenue
Auckland
New Zealand

Overseas Banking Group

KPMG
8th Floor
Prince's Building
10 Chater Road
Hong Kong SAR

New Zealand Chief Executive Officer/Responsible Person

The New Zealand Chief Executive Officer, Noel Gerard McNamara, has been authorised in writing by each Director named below, in accordance with section 82 of the Reserve Bank of New Zealand Act 1989, to sign this Disclosure Statement on the Directors' behalf. Accordingly, Noel Gerard McNamara is a Responsible Person under the Registered Bank Disclosure Statements (Overseas Incorporated Registered Banks) Order 2014 (as amended).

Noel Gerard McNamara

Chief Executive Officer New Zealand Branch. Joined the HSBC Group in 1995 and resides in New Zealand. He has a Post Graduate Diploma in International Management from the Institute of Management Adelaide South Australia.

Communications addressed to the responsible person may be sent to:
c/o The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch
PO Box 5947
Wellesley Street
Auckland 1141
New Zealand

Dealings with Responsible Person

No dealings with any responsible person or director, the immediate relative or professional associate of a responsible person or director, have been entered into by HBAP and the Banking Group other than those given in the ordinary course of business.

Board of Directors of HBAP

The Directors of HBAP at the time this Disclosure Statement was signed are:

Stuart Thomson Gulliver (Chairman)

Masters Degree in Jurisprudence, Worcester College, Oxford University, 1980
Executive Director and Group Chief Executive, HSBC Holdings plc

Peter Wong Tung Shun (Deputy Chairman and Chief Executive)

Bachelor of Arts, Indiana University, 1974; Master of Business Administration, Indiana University, 1976
Master of Science, Indiana University, 1978

Laura Cha May Lung, GBS (Deputy Chairman)

B.A., University of Wisconsin-Madison, 1972; Juris Doctor, University of Santa Clara Law School, 1982; and admitted to practice in the State of California and in Federal Courts, 1983
Company Director

General Disclosures *(continued)*

Board of Directors of HBAP *(continued)*

* Zia Mody (Deputy Chairman)

Master of Laws, Harvard University, 1979; Bachelor of Arts (Law), Cambridge University, 1978
Partner, AZB & Partners

* Graham John Bradley

BA, LLB (Hons I) from Sydney University, 1971
LLM, Harvard University, 1973
Company Director

Dr Christopher Cheng Wai Chee, GBS, OBE

Bachelor of Business Administration, University of Notre Dame, 1969; Master of Business Administration, Columbia University, 1979; Doctorate in Social Sciences honoris causa, The University of Hong Kong, 2011
Chairman, Wing Tai Properties Limited

Dr Raymond Ch'ien Kuo Fung, GBS, CBE

B.A., Rockford College, 1973; Master of Arts and Doctor of Philosophy (Economics), University of Pennsylvania, 1976 and 1978
Non-Executive Chairman, MTR Corporation Limited and Independent Non-executive Chairman, Hang Seng Bank Limited

*** Naina Lal Kidwai**

Bachelor of Arts degree (Honours Course) in Economics, Delhi University, examined in 1977, certificate awarded 4 March 1978; Masters in Business Administration, Harvard University, 1982
Group General Manager, Chairman India and Director HSBC Asia Pacific

Irene Lee Yun-lien

Bachelor of Arts (Distinction) in History of Art from Smith College, Northampton, Massachusetts, USA, 1974
Member of Honourable Society of Gray's Inn, UK, 1977
Barrister-at-Law in England and Wales, 1977
Chairman, Hysan Development Company Limited

Rose Lee Wai Mun

Bachelor of Business Administration, University of Hawaii, 1977
Vice-Chairman and Chief Executive, Hang Seng Bank Limited

^ Victor Li Tzar Kuoi

B.Sc. and M.Sc., Stanford University, 1986
Managing Director and Deputy Chairman, Cheung Kong (Holdings) Limited

Peter James Holland Riley

BA Hons in Geography from University College, Durham University, 1982; ACA, The Institute of Chartered Accountants in England and Wales (Qualified 1985); and FCPA, The Hong Kong Society of Accountants, 2003
Group Finance Director, Jardine Matheson Holdings Limited

John Robert Slosar

Bachelor degree in Economics from Columbia University, 1978
Bachelor degree in Economics, subsequently M.A. from University of Cambridge, 1980
Chairman, John Swire & Sons (H.K.) Limited

Kevin Anthony Westley

Bachelor of Arts, University of London, 1970; Chartered Accountant, Institute of Chartered Accountants in England and Wales, 1973
Company Director

Dr Rosanna Wong Yick-Ming, DBE

B.Soc.Sc, University of Hong Kong 1975; MSW, University of Toronto 1979; M.Sc. in Social Policy and Planning, London School of Economics and Political Science, University of London 1983; Diploma in Executive Management, Chinese University of Hong Kong 1985; M.A. and Doctor Degree in Sociology, University of California, Davis 1993 and 1997 Executive Director, The Hong Kong Federation of Youth Groups

General Disclosures *(continued)*

Board of Directors of HBAP *(continued)*

Marjorie Yang Mun Tak, GBS

B.Sc. in Mathematics, Massachusetts Institute of Technology, 1974; and Master of Business Administration, Harvard Business School, 1976

Chairman, Esquel Holdings Inc.

#* Tan Sri Dr Francis Yeoh Sock Ping, CBE

Bachelor of Science (Hons.) in Civil Engineering, University of Kingston, UK, 1978; Honorary Doctorate of Engineering from University of Kingston, 2004

Managing Director, YTL Corporation Berhad

#* Xinzhe Li Jennifer

Master of Business Administration, The University of British Columbia, Vancouver, Canada, 1994

Bachelor of Arts, Tsinghua University, Beijing, China, 1990

Chief Financial Officer, Baidu, Inc.

[#] independent non-executive Director

[^] non-executive Director

Country of Residence

With the exception of those denoted with an *, all directors reside in Hong Kong. Zia Mody and Naina Lal Kidwai reside in India, Graham John Bradley resides in Australia, Tan Sri Dr Francis Yeoh Sock Ping resides in Malaysia and Xinzhe Li Jennifer resides in China.

Communications addressed to the Directors may be sent to:

c/o The Hongkong and Shanghai Banking Corporation Limited

GPO Box 64

Hong Kong

Change in Board of Directors for HBAP

The composition of the Board of Directors has changed since 31 December 2013.

Christopher Dale Pratt and Andreas Sohmen-Pao resigned as non-executive directors of HBAP with effect from 14 March 2014 and 19 May 2014 respectively.

John Robert Slosar and Xinzhe Li Jennifer were appointed as non-executive directors of HBAP with effect from 12 May 2014 and 22 September 2014 respectively.

Directors' Policy on Conflicts of Interests

Regulation 99(h) of HBAP's Articles of Association states:

“The office of a director shall ipso facto be vacated if he or his firm or any partner therein or representative thereof acts (otherwise than with the consent of the Board) either directly or indirectly as a director, managing director, manager or partner of any corporation, company, partnership or body of persons other than a subsidiary of the Company (or of the holding company of the Company or any of its subsidiaries) carrying on business which competes with that carried on by the Company, such consent must be evidenced by writing signed by the Chairman pursuant to a resolution of the Board and may be at any time withdrawn by the Board without previous notice.”

Directors' Interests in Contracts

No contracts of significance to which HBAP, its ultimate holding company, its subsidiary companies or any fellow subsidiary company was a party to and in which a Director had a material interest existed at 31 December 2014 or at any time during the period.

General Disclosures *(continued)*

Audit Committee

The Banking Group does not have an Audit Committee. The Audit Committee of HBAP, comprising four independent Directors, meets regularly with the Group's senior management and the external auditors to consider and review the Group's financial statements, the nature and scope of audit reviews and the effectiveness of the systems of internal control and compliance. The members of the Audit Committee are Peter James Holland Riley (Chairman of the Committee), Graham John Bradley, Kevin Anthony Westley and Irene Lee Yun-lien.

Credit Rating

HBAP has the following long term debt ratings for non-HK\$ long-term senior unsecured obligations which are payable in New Zealand in New Zealand dollars:

	Current Rating	Previous Rating (if changed in the previous two years)	Date of Change
Moody's Investor Service Inc.	Aa2 (stable outlook)	Not changed	-
Standard & Poor's Corporation	AA- (stable outlook)	Not changed	-
Fitch IBCA Inc.	AA- (stable outlook)	Not changed	-

Rating scales are:

Credit Ratings	Moody's (a)	S&P (b)	Fitch (b)
Highest quality/Extremely strong capacity to pay interest and principal	Aaa	AAA	AAA
High quality/Very strong	Aa	AA	AA
Upper medium grade/Strong	A	A	A
Medium grade (lowest investment grade)/Adequate	Baa	BBB	BBB
Predominantly speculative/Less near term vulnerability to default	Ba	BB	BB
Speculative, low grade/Great vulnerability	B	B	B
Poor to default/identifiable vulnerability	Caa	CCC	CCC
Highest speculations	Ca	CC	CC
Lowest quality, no interest	C	C	C
Defaulted on obligations		D	D

(a) Moody's - A numeric modifier is applied to each generic rating category from Aa to B, indicating that the counterparty is (1) in the higher end of its letter-rating category, (2) in mid-range, (3) in lower end.

(b) Standard & Poor's and Fitch – Ratings are modified by the addition of a plus (+) or minus (-) sign to show relative standing within the major rating categories.

Conditions of Registration

Conditions of registration for The Hongkong and Shanghai Banking Corporation Limited in New Zealand

These conditions of registration apply on and after 1 November 2014.

The registration of The Hongkong and Shanghai Banking Corporation Limited (“the registered bank”) in New Zealand is subject to the following conditions:

1. That the banking group does not conduct any non-financial activities that in aggregate are material relative to its total activities.

In this condition of registration, the meaning of “material” is based on generally accepted accounting practice.

2. That the banking group’s insurance business is not greater than 1% of its total consolidated assets.

For the purposes of this condition of registration, the banking group’s insurance business is the sum of the following amounts for entities in the banking group:

- (a) if the business of an entity predominantly consists of insurance business and the entity is not a subsidiary of another entity in the banking group whose business predominantly consists of insurance business, the amount of the insurance business to sum is the total consolidated assets of the group headed by the entity; and
- (b) if the entity conducts insurance business and its business does not predominantly consist of insurance business and the entity is not a subsidiary of another entity in the banking group whose business predominantly consists of insurance business, the amount of the insurance business to sum is the total liabilities relating to the entity’s insurance business plus the equity retained by the entity to meet the solvency or financial soundness needs of its insurance business.

In determining the total amount of the banking group’s insurance business –

- (a) all amounts must relate to on balance sheet items only, and must comply with generally accepted accounting practice; and
- (b) if products or assets of which an insurance business is comprised also contain a non-insurance component, the whole of such products or assets must be considered part of the insurance business.

For the purposes of this condition of registration, –

“insurance business” means the undertaking or assumption of liability as an insurer under a contract of insurance:

“insurer” and “contract of insurance” have the same meaning as provided in sections 6 and 7 of the Insurance (Prudential Supervision) Act 2010.

3. That the business of the registered bank in New Zealand does not constitute a predominant proportion of the total business of the registered bank.
4. That no appointment to the position of the New Zealand chief executive officer of the registered bank shall be made unless:
 - (i) the Reserve Bank has been supplied with a copy of the curriculum vitae of the proposed appointee; and
 - (ii) the Reserve Bank has advised that it has no objection to that appointment.

Conditions of Registration *(continued)*

5. That The Hongkong and Shanghai Banking Corporation Limited complies with the requirements imposed on it by the Hong Kong Monetary Authority.
6. That, with reference to the following table, each capital adequacy ratio of The Hongkong and Shanghai Banking Corporation Limited must be equal to or greater than the applicable minimum requirement.

Capital adequacy ratio	Minimum requirement		
	1 January 2013 to 31 December 2013	1 January 2014 to 31 December 2014	On and after 1 January 2015
Common Equity Tier 1 capital	3.5 %	4 %	4.5 %
Tier 1 capital	4.5 %	5.5 %	6 %
Total capital	8 %	8 %	8 %

For the purposes of this condition of registration, the capital adequacy ratios –

- (a) must be calculated as a percentage of the registered bank's risk weighted assets; and
- (b) are otherwise as administered by the Hong Kong Monetary Authority.
7. That liabilities of the registered bank in New Zealand, net of amounts due to related parties (including amounts due to a subsidiary or affiliate of the registered bank), do not exceed NZ\$15 billion.
8. That, for a loan-to-valuation measurement period, the total of the business of the registered bank in New Zealand's qualifying new mortgage lending amounts must not for residential properties with a loan-to-valuation ratio of more than 80%, exceed 10% of the total of the qualifying new mortgage lending amounts arising in the loan-to-valuation measurement period.
9. That the business of the registered bank in New Zealand must not make a residential mortgage loan unless the terms and conditions of the loan contract or the terms and conditions for an associated mortgage require that a borrower obtain the registered bank's agreement before the borrower can grant to another person a charge over the residential property used as security for the loan.
10. That the business of the registered bank in New Zealand must not permit a borrower to grant a charge in favour of another person over a residential property used as security for a residential mortgage loan unless the sum of the lending secured by the charge and the loan value for the residential mortgage loan would not exceed 80% of the property value of the residential property when the lending secured by the charge is drawn down.
11. That the business of the registered bank in New Zealand must not provide a residential mortgage loan if the residential property to be mortgaged to the registered bank as security for the residential mortgage loan is subject to a charge in favour of another person unless the total amount of credit secured by the residential property would not exceed 80% of the property value when the residential mortgage loan is drawn down.
12. That the business of the registered bank in New Zealand must not—
- (a) act as broker or arrange a residential mortgage loan for the business of the registered bank outside New Zealand or for an associated person of the registered bank outside New Zealand; or
- (b) facilitate the drawdown of a residential mortgage loan the registered bank originated as part of its business outside New Zealand or by an associated person of the registered bank outside New Zealand without notifying the Reserve Bank of this activity in the manner and form specified by the Reserve Bank.

Conditions of Registration *(continued)*

In these conditions of registration, –

“banking group” –

- (a) means the New Zealand business of the registered bank and its subsidiaries as required to be reported in group financial statements for the group’s New Zealand business under section 461B(2) of the Financial Markets Conduct Act 2013 (unless paragraph (b) applies); or
- (b) if the Financial Reporting Act 1993 applies to the registered bank, means the New Zealand business of the registered bank and its subsidiaries as required to be reported in group financial statements for the group’s New Zealand business under section 9(2) of the Financial Reporting Act 1993:

“business of the registered bank in New Zealand” –

- (a) means the New Zealand business of the registered bank as defined in the requirement for financial statements for New Zealand business in section 461B(1) of the Financial Markets Conduct Act 2013 (unless paragraph (b) applies); or
- (b) if the Financial Reporting Act 1993 applies to the registered bank, means the New Zealand business of the registered bank as required to be reported in financial statements under section 8(2) of the Financial Reporting Act 1993:

“generally accepted accounting practice” –

- (a) has the same meaning as in section 8 of the Financial Reporting Act 2013 (unless paragraph (b) applies); or
- (b) means generally accepted accounting practice within the meaning of section 3 of the Financial Reporting Act 1993 if the registered bank is required to prepare financial statements in accordance with that practice:

“liabilities of the registered bank in New Zealand” –

- (a) means the liabilities that the registered bank would be required to report in financial statements for its New Zealand business if section 461B(1) of the Financial Markets Conduct Act 2013 applied (unless paragraph (b) applies); or
- (b) if the Financial Reporting Act 1993 applies to the registered bank, means the liabilities of the registered bank as required to be reported in financial statements under section 8(2) of the Financial Reporting Act 1993.

In conditions of registration 8 to 12,—

“loan-to-valuation ratio”, “loan value”, “property value”, “qualifying new mortgage lending amount” and “residential mortgage loan” have the same meaning as in the Reserve Bank of New Zealand document entitled “Framework for Restrictions on High-LVR Residential Mortgage Lending” (BS19) dated October 2014.

“loan-to-valuation measurement period” means a period of six calendar months ending on the last day of the sixth calendar month, the first of which ends on the last day of March 2014.

Changes to Conditions of Registration since the 30 September 2014 Disclosure Statement

The “Framework for Restrictions on High-LVR Residential Mortgage Lending” (BS19) dated October 2014 referred to above was previously “Framework for Restrictions on High-LVR Residential Mortgage Lending” (BS19) dated July 2014.

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HISTORICAL SUMMARY OF FINANCIAL STATEMENTS

FIVE YEAR COMPARISON

<i>Dollars in Thousands</i>	<i>Banking Group</i>					
	Audited Year ended 31 December					
	2014	2013	2012	2011	2010	2009
Summary of Financial Results						
Interest income	206,493	188,494	203,549	201,411	214,285	266,178
Interest expense	(116,554)	(109,506)	(115,302)	(118,816)	(124,794)	(168,803)
Net interest income	89,939	78,988	88,247	82,595	89,491	97,375
Net trading income	8,650	17,912	9,140	14,929	12,459	13,896
Other net operating income	34,725	39,239	35,419	45,647	47,857	25,104
Operating income	133,314	136,139	132,806	143,171	149,807	136,375
Operating expenses	(58,926)	(58,483)	(58,628)	(63,726)	(57,496)	(57,287)
Operating profit before provisions and tax	74,388	77,656	74,178	79,445	92,311	79,088
Release / (provisions) for loan impairment	18,046	(42,690)	(17,596)	(24,522)	(11,111)	(6,488)
Operating profit before tax	92,434	34,966	56,582	54,923	81,200	72,600
Income tax expense	(25,978)	(9,899)	(15,983)	(15,526)	(25,011)	(21,869)
Profit after tax	66,456	25,067	40,599	39,397	56,189	50,731
Head Office Account brought forward	(3,691)	13,503	15,392	28,184	24,607	19,777
Retained profit repatriated	(21,026)	(42,261)	(42,488)	(52,189)	(52,612)	(45,901)
Head Office Account carried forward	41,739	(3,691)	13,503	15,392	28,184	24,607
Statement of Financial Position						
Individually impaired assets	121,913	141,964	65,217	75,325	71,781	43,900
Total assets	5,308,720	5,155,681	5,045,975	4,939,706	5,020,899	4,770,370
Liabilities	5,264,771	5,155,380	5,030,627	4,922,561	4,992,990	4,743,689
Equity	43,949	301	15,348	17,145	27,909	26,681
Total liabilities and equity	5,308,720	5,155,681	5,045,975	4,939,706	5,020,899	4,770,370

The amounts included in this summary have been taken from the audited financial statements of the Banking Group.

STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2014

		<i>Banking Group and Branch</i>	
		Audited	
		12 months ended	
<i>Dollars in Thousands</i>	Note	31.12.14	31.12.13
Interest income	3	206,493	188,494
Interest expense	3	(116,554)	(109,506)
Net interest income		89,939	78,988
Net trading income	3	8,650	17,912
Other net operating income	3	34,725	39,239
Operating income		133,314	136,139
Operating expenses	4	(58,926)	(58,483)
Operating profit before provisions and tax		74,388	77,656
Release / (provisions) for loan impairment	15	18,046	(42,690)
Operating profit before tax		92,434	34,966
Income tax expense	6	(25,978)	(9,899)
Profit after tax		66,456	25,067
Other comprehensive income / (expense)			
Items that may be reclassified subsequently to profit or loss:			
Cashflow hedges		(3,090)	2,763
Income tax expense on cashflow hedge		866	(810)
Available-for-sale financial assets		614	318
Income tax expense on available-for-sale financial assets		(171)	(89)
Other comprehensive income / (expense) for the period		(1,781)	2,182
Total comprehensive income for the period		64,675	27,249

The accompanying notes form part of and should be read in conjunction with these financial statements.

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2014

	<i>Banking Group and Branch</i>	
	Audited	
	12 months ended	
<i>Dollars in Thousands</i>	31.12.14	31.12.13
Head Office Account *		
At beginning of period	(3,691)	13,503
Repatriation to Head Office	(21,026)	(42,261)
Profit after tax	<u>66,456</u>	<u>25,067</u>
At end of period	<u><u>41,739</u></u>	<u><u>(3,691)</u></u>
Cashflow Hedging Reserve		
At beginning of period	2,327	374
Movement in the fair value of derivatives	(3,090)	2,763
Tax on movements and transfers	<u>866</u>	<u>(810)</u>
At end of period	<u><u>103</u></u>	<u><u>2,327</u></u>
Available for Sale Reserve		
At beginning of period	42	(187)
Movement in the fair value of debt and equity securities	614	318
Tax on movements and transfers	<u>(171)</u>	<u>(89)</u>
At end of period	<u><u>485</u></u>	<u><u>42</u></u>
Other Reserve		
At beginning of period	1,623	1,658
Amortisation of share options granted	228	285
Movement in respect of share-based payment arrangements	<u>(229)</u>	<u>(320)</u>
At end of period	<u><u>1,622</u></u>	<u><u>1,623</u></u>
Equity at end of period	<u><u>43,949</u></u>	<u><u>301</u></u>
Represented by:		
Profit after tax	66,456	25,067
Other comprehensive income	<u>(1,781)</u>	<u>2,182</u>
Total comprehensive income for the period	<u>64,675</u>	<u>27,249</u>
Repatriation to Head Office	(21,026)	(42,261)
Movement in other reserve	<u>(1)</u>	<u>(35)</u>
Equity at beginning of period	<u>301</u>	<u>15,348</u>
	<u><u>43,949</u></u>	<u><u>301</u></u>

* The Head Office account is interest free, repayable at the discretion of the Branch and subordinate to all other debts.

The accompanying notes form part of and should be read in conjunction with these financial statements.

STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2014

		<i>Banking Group and Branch</i>	
<i>Dollars in Thousands</i>	Note	Audited 31.12.14	Audited 31.12.13
ASSETS			
Cash and demand balances with central banks		411,548	763,286
Advances to banks	7, 8	14,871	15,179
Debt and equity securities	9	494,580	399,585
Derivative financial instruments	10	196,182	248,167
Advances to customers	11	3,774,940	3,372,765
Amounts due from related parties	21	367,519	308,868
Other assets	12	22,921	16,944
Current taxation		-	593
Deferred taxation	6	7,086	9,130
Intangible assets	13	18,101	19,847
Fixed assets	14	972	1,317
Total Assets		5,308,720	5,155,681
LIABILITIES			
Deposits by banks	16	182,194	157,678
Derivative financial instruments	17	186,914	223,174
Customer deposits	18	3,180,934	3,135,950
Debt securities	19	739,746	792,482
Amounts due to related parties	21	925,126	808,696
Other liabilities	20	42,710	37,400
Current taxation		7,147	-
Total Liabilities		5,264,771	5,155,380
Net Assets		43,949	301
EQUITY			
Head Office Account		41,739	(3,691)
Cashflow Hedging Reserve		103	2,327
Available for Sale Reserve		485	42
Other Reserve		1,622	1,623
Total Equity		43,949	301

The accompanying notes form part of and should be read in conjunction with these financial statements.



Director: Peter T S Wong
Date: 26 March 2015



Director: Rose W M Lee
Date: 26 March 2015

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2014

	<i>Banking Group and Branch</i>	
	Audited	
	12 months ended	
<i>Dollars in Thousands</i>	31.12.14	31.12.13
<i>Cash flows from / (to) operating activities</i>		
Interest received	194,476	194,962
Fees and commissions	34,315	38,795
Realised trading gain	31,848	1,917
Interest paid	(100,795)	(101,349)
Operating expenses	(55,744)	(54,441)
Taxation paid	(15,500)	(7,750)
Net cash flows from operating activities before changes in operating assets and liabilities	88,600	72,134
Changes in operating assets and liabilities arising from cash flow movements		
Cash was provided net from / applied net (to):		
Debt and equity securities matured / (purchased)	(93,262)	392,483
Advances to customers	(318,392)	(50,840)
Amounts due from related parties	(99,661)	7,354
Other assets	1,267	(464)
Other liabilities	2,849	(3,176)
Debt securities issued	(63,771)	395,027
Deposits by banks	(4,156)	(1,287)
Customer deposits	(117,483)	(326,191)
Amounts due to related parties	164,413	(81,187)
Net change in operating assets and liabilities	(528,196)	331,719
Net cash flows from / (to) operating activities	(439,596)	403,853
<i>Cash flows from / (to) investing activities</i>		
Proceeds from fixed assets	-	8
Acquisition of fixed assets	(217)	(441)
Acquisition of intangible assets	-	(148)
Net cash flows to investing activities	(217)	(581)
<i>Cash flows to financing activities</i>		
Repatriation to head office	(21,026)	(42,261)
Net cash flows to financing activities	(21,026)	(42,261)
Net increase / (decrease) in cash and cash equivalents	(460,839)	361,011
Effect of exchange rate fluctuations on cash held	(12,526)	7,397
Cash and cash equivalents at beginning of period	(980,300)	(1,348,708)
Cash and cash equivalents at end of period	(1,453,665)	(980,300)

The accompanying notes form part of and should be read in conjunction with these financial statements.

STATEMENT OF CASH FLOWS *(continued)*

FOR THE YEAR ENDED 31 DECEMBER 2014

	<i>Banking Group and Branch</i>	
	Audited	
	12 months ended	
<i>Dollars in Thousands</i>	31.12.14	31.12.13
<i>Analysis of cash and cash equivalents</i>		
Cash and demand balances with central banks	411,548	763,286
Advances to banks – demand	14,871	15,179
Advances to customers – demand	255,253	195,554
Balance due from related parties – demand	10,965	51,965
Balance due to related parties – demand	(68,733)	(119,854)
Deposits by banks – demand	(182,194)	(153,521)
Deposits by customers - demand	(1,895,375)	(1,732,909)
	<u>(1,453,665)</u>	<u>(980,300)</u>
<i>Reconciliation of profit after tax to net cash flows from operating activities</i>		
Profit after tax	66,456	25,067
<i>Adjustments to reconcile profit after tax to net cash flow from operating activities:</i>		
Change in interest accruals	(2,921)	5,178
Change in mark to market accruals	22,788	(16,439)
Depreciation	562	759
Amortisation of intangible asset	1,746	1,718
Amortisation of premium and discounts	12,289	10,037
Change in deferred income and accrued expense	646	1,287
Amortisation of share options granted	228	285
Impairment charge on loans and advances	(18,046)	42,690
Discount unwinding on impaired loans and advances	(5,626)	(590)
(Gain) / loss on disposal of fixed assets	-	(8)
Change in current and deferred taxation	10,478	2,149
Adjust operating cash flows not included in profit after tax:		
Net change in operating assets and liabilities	<u>(528,196)</u>	<u>331,720</u>
Net cash flows from operating activities	<u>(439,596)</u>	<u>403,853</u>

The accompanying notes form part of and should be read in conjunction with these financial statements.

Notes to and forming part of the Financial Statements

1. Statement of Accounting Policies

GENERAL ACCOUNTING POLICIES

Reporting Entity

These financial statements are for the New Zealand Banking Group (“Banking Group”). As the Branch and Banking Group’s financial performance and position are the same in all material aspects, a single set of Banking Group numbers are presented.

The following entities have been aggregated to form the Banking Group:

The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch

HSBC Nominees (New Zealand) Limited

This New Zealand incorporated entity is the Branch’s nominee company which provides custodian services. HSBC Nominees (New Zealand) Limited is wholly owned by HBAP. Income and expenses of the custodian services business are included in the Branch’s financial statements.

HSBC Investments New Zealand Limited

This New Zealand incorporated entity provides fund management services to customers and commenced trading operations in June 2008. HSBC Investments New Zealand Limited is wholly owned by HSBC Asia Pacific Holdings (UK) Limited which is wholly owned by HBAP. The Unit Trusts for which the Company has acted as Manager were closed on 31 October 2014. As a result, the Company is ceasing to trade and no longer continues as a going concern. The individual accounts of HINZ have not been prepared on a going concern basis to reflect the likely discontinuation of operations. This has had no impact on the Banking Group financial statements.

HSBC Cash Fund

The HSBC Cash Fund was a Unit Trust set up in June 2008 following the introduction by the New Zealand Inland Revenue of the Portfolio Investment Entity (“PIE”) regime. The HSBC Cash Fund was managed by HSBC Investments New Zealand Limited with an independent trustee (New Zealand Guardian Trust) responsible for ensuring that the HSBC Cash Fund was administered in accordance with the trust deed. All funds received into the HSBC Cash Fund were placed with the Branch and were included in the Banking Group’s financial results as Customer Deposits. The HSBC Cash Fund was closed in July 2013.

HSBC Term Fund

The HSBC Term Fund was a Unit Trust, set up in April 2009, following the introduction by the New Zealand Inland Revenue of the Portfolio Investment Entity (“PIE”) regime. The HSBC Term Fund was managed by HSBC Investments New Zealand Limited with an independent trustee (New Zealand Guardian Trust) responsible for ensuring that the HSBC Term Fund was administered in accordance with the trust deed. All funds received into the HSBC Term Fund were placed with the Branch and were included in the Banking Group’s financial results as Customer Deposits. The HSBC Term Fund was closed in May 2013.

Non-Banking Group Entities

The following New Zealand incorporated entities do not form part of the Banking Group as defined in the Conditions of Registration. They are ultimately wholly owned by HSBC Holdings plc and HBAP is not their parent entity.

HSBC International Trustee (New Zealand) Limited and *HSBC International Trustee Limited, New Zealand Branch* provide trustee services to an international client base. HSBC International Trustee (New Zealand) Limited is a wholly owned subsidiary of Bermuda Asia Pacific Holdings Limited, incorporated in the Cook Islands. HSBC International Trustee Limited is a body corporate incorporated in British Virgin Islands. The respective directors are winding down the company and branch, accordingly, they no longer continue on a going concern basis.

Non-controlled Structured Entities

The following New Zealand incorporated entities do not form part of the Banking Group as defined in the Conditions of Registration. The Banking Group does not control the structured entities.

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

Non-controlled Structured Entities *(continued)*

HSBC Global Unit Trusts

The HSBC Global Unit Trusts were set up in August 2009 to support the local launch of HSBC Group Investment Funds under the Portfolio Investment Entity (“PIE”) structure and branded locally as HSBC Investments New Zealand Limited Global Unit Trusts.

The HSBC Global Unit Trusts were managed by HSBC Investments New Zealand Limited with an independent trustee (New Zealand Guardian Trust) responsible for ensuring that the HSBC Global Unit Trusts were administered in accordance with the trust deed. Funds received into the HSBC Global Unit Trusts were primarily invested in shares of a sub-fund of HSBC Global Investment Funds, an investment company incorporated in the Grand Duchy of Luxembourg. HSBC Investment Funds (Luxembourg) S.A., the manager of the Sub-funds is part of HSBC Global Asset Management. There were four funds; HSBC China Fund, HSBC BRIC Fund, HSBC India Fund and HSBC Asia ex Japan Fund. The HSBC Global Unit Trusts were closed on 31 October 2014.

HSBC World Selection Funds

The HSBC World Selection Funds were established on 18 January 2010 to support the local launch of HSBC Portfolios under the Portfolio Investment Entity (“PIE”) structure.

The HSBC World Selection Funds were managed by HSBC Investments New Zealand Limited with an independent trustee (New Zealand Guardian Trust) responsible for ensuring that the HSBC World Selection Funds were administered in accordance with the trust deed. Funds received into the HSBC World Selection Funds were invested primarily in shares of a sub-fund of HSBC Portfolios, an investment company incorporated in the Grand Duchy of Luxembourg. HSBC Investment Funds (Luxembourg) S.A. is the manager of the HSBC Portfolios and HSBC Global Asset Management (UK) Limited is the investment adviser. Both the manager and investment adviser are part of HSBC Global Asset Management. There were three funds offered; HSBC World Selection – Foundation Fund, HSBC World Selection – Frontier Fund, and HSBC World Selection – Horizon Fund. The HSBC World Selection Funds were closed on 31 October 2014.

Other

The Banking Group enters into transactions with unconsolidated structured entities in the normal course of business to facilitate customer transactions and for specific investment opportunities to earn income in the form of interest and fees. The Banking Group’s arrangements that involve structured entities are authorised centrally prior to being established to ensure appropriate purpose and governance. The Banking Group has interests in an unconsolidated securitisation vehicle providing funding through the subscription of notes issued by the structured entity. The primary source of debt service and security is derived from the underlying assets of the structured entity. All lending is subject to the Banking Group’s credit approval process. The total assets of the unconsolidated structure entity at reporting date was \$287m. The total assets and commitments of the Banking Group in the unconsolidated structured entity at reporting date was \$57m and \$10m respectively (December 2013: Nil). This reflects the maximum exposure to loss in relation to those interests regardless of the probability of the loss being incurred. This is stated gross of the effects of any collateral arrangements entered into to mitigate the Banking Groups exposure to loss. On balance sheet amounts are included in ‘advances to customers’. The Banking Group has no provisions for amounts held in structured entities, nor does the Banking Group provide or anticipate providing in the future any non-contractual financial support.

Basis of consolidation

Structured entities

The Banking Group had established the following structured entities (“SEs”): the HSBC Cash Fund, the HSBC Term Fund, the HSBC Global Unit Trusts and the HSBC World Selection Funds.

The Banking Group does not have any direct or indirect unit holding in these entities. An SE is consolidated when the Banking Group is exposed, or has rights, to variable returns from its involvement with the SE and has the power to affect those returns. The SEs controlled by the Banking Group are established under terms that impose strict limitations on the decision making powers of the SEs’ management and operates in a predetermined way such that virtually all rights, obligations and aspects of their activities are controlled through these terms.

Transactions eliminated on consolidation

Intra-group balances are eliminated in preparing the Banking Group’s financial statements.

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

Basis of Reporting

These financial statements are prepared and presented in accordance with the Financial Reporting Act 1993, the Registered Bank Disclosure Statements (Overseas Incorporated Registered Banks) Order 2014 (as amended), the Reserve Bank of New Zealand Act 1989, and all applicable financial reporting standards and other generally accepted accounting practices in New Zealand.

Measurement Base

These financial statements are based on the general principles of historical cost accounting, as modified by the revaluation of certain assets and liabilities. They are prepared on a going concern basis. All amounts are expressed in New Zealand currency, the presentation currency and functional currency, and all references to “\$” is to New Zealand dollars unless otherwise stated.

Particular Accounting Policies

These financial statements have been prepared in accordance with NZGAAP. They comply with New Zealand Equivalents to International Financial Reporting Standards (“NZ IFRS”), and other applicable Financial Reporting Standards, as appropriate for profit oriented entities.

The External Reporting Board has released a number of standards and amendments which are effective for annual periods beginning after 1 January 2015. These standards and amendments have not been adopted early and are excluded from application to these financial statements. Those which may be relevant to the Group are set out below.

- NZ IFRS 9 (2014)

These standards introduce new requirements for the classification and measurement of financial assets and financial liabilities. On the adoption of NZ IFRS 9 the Banking Group would have the option of classifying its financial assets as subsequently measured at either amortised cost or fair value through other comprehensive income or fair value through profit or loss, depending on the business model for managing those financial assets and the assets’ contractual cash flow characteristics when the standard is effective. This would be the result of a change in accounting policy on the adoption of NZ IFRS 9 if the Banking Group selected to do so. The classification of financial liabilities is essentially unchanged, except that, for certain liabilities designated at fair value through profit and loss, gains or losses relating to changes in the entity’s own credit risk are to be included in other comprehensive income (if any).

In addition the standard introduces a new expected loss impairment model. The impairment requirements apply to financial assets measured at amortised cost and fair value through other comprehensive income, and lease receivables and certain loan commitments and financial guarantee contracts. At initial recognition, allowance (or provision in the case of commitments and guarantees) is required for expected credit losses (“ECL”) resulting from default events that are possible within the next 12 months (“12 month ECL”). In the event of a significant increase in credit risk, allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument (“lifetime ECL”).

The assessment of whether credit risk has increased significantly since initial recognition is performed for each reporting period by considering the change in the risk of default occurring over the remaining life of the financial instrument, rather than by considering an increase in ECL. The assessment of credit risk, and the estimation of ECL, are required to be unbiased and probability-weighted, and should incorporate all available information which is relevant to the assessment, including information about past events, current conditions and reasonable and supportable forecasts of future events and economic conditions at the reporting date. In addition, the estimation of ECL should take into account the time value of money.

As a result, the recognition and measurement of impairment is intended to be more forward-looking than under NZ IAS 39 and the resulting impairment charge will tend to be more volatile. It will also tend to result in an increase in the total level of impairment allowances, since all financial assets will be assessed for at least 12 month ECL and the population of financial assets to which lifetime ECL applies is likely to be larger than the population for which there is objective evidence of impairment in accordance with NZ IAS 39.

The general hedge accounting requirements in this standard aim to simplify hedge accounting, creating a stronger link with risk management strategy and permitting hedge accounting to be applied to a greater variety of hedging instruments and risks.

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

Particular Accounting Policies *(continued)*

The standard is effective for annual accounting periods beginning on or after 1 January 2018 with early adoption permitted. NZ IFRS 9 is required to be applied retrospectively but prior periods need not be restated. The Banking Group will adopt the standard in line with HBAP's adoption of IFRS 9.

The Banking Group is assessing the potential impact on the consolidated financial statements resulting from application of NZ IFRS 9.

- NZ IFRS 15 Revenue from contracts with Customers

This standard provides a single, comprehensive principles-based model to be applied to all contracts from customers. The standard is effective for annual accounting periods beginning on or after 1 January 2017. The standard should be applied retrospectively. HSBC is currently assessing the impact of this standard but it is not practicable to quantify the effect as at the date of the publication of these financial statements.

The Banking Group has also considered all other standards issued but not yet effective and determined that they will have no material impact on the financial statements.

Changes in Accounting Policies

There were no new standards applied during the year ended 31 December 2014. On 1 January 2014, the Banking Group applied 'Offsetting Financial Assets and Financial Liabilities (Amendments to NZ IAS 32)', which clarified the requirements for offsetting financial instruments. The amendments were applied retrospectively and did not have a material effect on the Banking Group financial statements.

All other interpretations and amendments to standards had an insignificant effect on the Banking Group financial statements.

All other accounting policies have not changed and are the same as those applied by the Banking Group in the Disclosure Statement for the year ended 31 December 2013.

Comparative Figures

These financial statements include comparative information as required by NZ IAS 1 and the Registered Bank Disclosure Statements (Overseas Incorporated Registered Banks) Order 2014 (as amended).

There have been no material changes to the comparative figures.

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

PRINCIPAL ACCOUNTING POLICIES

The preparation of financial information requires the use of estimates and assumptions about future conditions. Use of available information and application of judgement are inherent in the formation of estimates. Actual results in the future may differ from those reported. In this connection, management believes that the critical accounting policies where management judgement is necessarily applied are those in relation to provisions for impairment on loans and advances, impairment of goodwill and the valuation of financial instruments.

In the opinion of management, all normal and recurring adjustments considered necessary for a fair presentation of the Banking Group's net income, financial position and cash flows have been made.

Acceptances & Endorsements

Acceptances and endorsements of bills of exchange are financial instruments used to facilitate trade settlements on behalf of clients. The Banking Group is effectively providing a payment guarantee to a third party.

Acceptances and endorsements of bills of exchange are recognised in the Statement of Financial Position as both assets and liabilities. Both asset and liability are recorded at face value since settlement is within 6 months.

There is no asset impairment test required since clients are required to hold sufficient cash funds to support the underlying transaction.

Accounting for Business Combinations

All business combinations are accounted for by applying the acquisition method.

When an entity becomes or ceases to be part of the Banking Group during the period the results of the entity are included in the results from the date that control or significant influence commenced or until the date that control or significant influence ceased. When an entity is acquired all identifiable assets and liabilities are recognised at their fair value at acquisition date. The fair value does not take into consideration any future intentions of the Banking Group. Where an entity that is part of the Banking Group is disposed of, the gain or loss recognised in profit or loss is calculated as the difference between the sale price and the carrying amount of the entity.

Advances to Banks, Customers & Related Parties

Advances to banks, customers, and related parties include loans and advances originated by the Banking Group, which are not intended to be sold in the short term and have not been classified either as held for trading or designated at fair value. Loans and advances are recognised when cash is advanced to borrowers. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method, less impairment losses.

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

Asset Impairment

Provisions for impaired financial assets are made when objective evidence of impairment exists and on a consistent basis. Objective evidence that financial assets are impaired can include default or delinquency by a borrower, restructuring of a loan or advance by the Banking Group on terms that the Banking Group would not otherwise consider, indication that the borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group.

Impairment provisions represent the quantification of incurred losses from homogeneous portfolios of assets and individually identified accounts. Impairment provisions are deducted from loans and advances in the Statement of Financial Position. There are two basic methods of calculating impairment losses, those calculated on individual loans and those losses assessed on a collective basis. Losses expected as a result of future events, no matter how likely, are not recognised.

Individually assessed accounts

Specific impairment provisions on individually assessed accounts are determined by an evaluation of the discounted future cash flows on a case-by-case basis. This procedure is applied to all accounts that are not subject to a portfolio-based approach. In estimating future cash flows on individually assessed accounts, the following factors are considered:

- The Banking Group's exposure to the customer (including contingent liabilities);
- The likely dividend available on liquidation or bankruptcy;
- The viability of the customer's business model and the capability of management to trade successfully out of financial difficulties and generate sufficient cash flow to service their debt obligations;
- The extent of other creditors' commitments ranking ahead of, or pari passu with, the Banking Group and the likelihood of other creditors continuing to support the company;
- The complexity of determining the aggregate amount and ranking of all creditor claims and the extent to which legal and insurance uncertainties are evident;
- The amount and timing of expected receipts and recoveries;
- The realisable value of security (or other credit mitigants) and likelihood of successful repossession;
- The likely deduction of any costs involved in recovery of amounts outstanding; and
- The ability of the borrower to obtain the relevant foreign currency if loans are not in local currency.

Releases on individually calculated specific provisions are recognised whenever the Banking Group has reasonable evidence that the established estimate of loss has been reduced.

Impairment loss is calculated by comparing the present value of the expected future cash flows, discounted at the original effective interest rate of the loan, with its current carrying value and the amount of any loss is charged in profit or loss. The carrying amount of impaired loans is reduced through the use of a specific provision account.

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

Asset Impairment *(continued)*

Collectively assessed loans and advances

For the calculation of impairment on a portfolio basis, loans and advances are grouped on the basis of similar credit risk characteristics.

Future expected cash flows are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group, adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future expected cash flows reflect and are directionally consistent with changes in related observable data from period to period. The methodologies and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Write-offs of loans and advances

Loans and advances (and the related impairment provisions) are normally written off, either partially or in full, when there is no realistic prospect of recovery of these amounts and when the proceeds from the realisation of security have been received.

Reversals of impairment

If, in a subsequent period, the amount of an impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed to the extent it is now excessive by reducing the provision account. The amount of any reversal is recognised in profit or loss.

Past due assets/90 days past due assets

Past due assets are defined as assets where a counterparty has failed to make a payment when contractually due. They are still accruing interest but are in the process of collection and are well-secured by collateral of realisable value equal to or greater than the asset. 90 days past due assets are assets that have been in this state for 90 days or more.

Renegotiated Loans

Loans with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the Banking Group has made concessions that it would not otherwise consider. Once the loan is restructured, it remains in this category independent of satisfactory performance after restructuring. Renegotiated loans do not include loans which are past due or impaired.

Assets & Liabilities – Derecognition

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

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

Debt & Equity Securities

Treasury bills, debt securities and equity shares intended to be held on a continuing basis are classified as available-for-sale securities and are measured at fair value. Available-for-sale securities are initially measured at fair value plus direct and incremental transaction costs on the trade date, the date on which the Banking Group commits to purchase or sell the asset. They are subsequently remeasured at fair value. Unless they are in a fair value hedge relationship, changes in fair value are recognised in equity in the available-for-sale reserve, through other comprehensive income, until the securities are either sold or impaired. Where the debt securities are in a fair value hedge relationship, the revaluation gain or loss attributable to the hedged risk is recognised in profit or loss.

On the sale of available-for-sale securities, cumulative gains or losses held within equity are recognised through profit or loss in 'Other net operating income'. Interest income is recognised on such securities using the effective interest rate method, calculated over the asset's expected life. Where dated debt securities have been purchased at a premium or discount, these premiums and discounts are recognised as an adjustment to the effective interest rate.

An assessment is made at the end of each reporting period as to whether there is any objective evidence of impairment, being circumstances where an adverse impact on estimated future cash flows of the financial asset or group of assets can be reliably estimated.

Impairment losses recognised in profit or loss for an equity instrument shall not be reversed through profit or loss.

If an available-for-sale financial asset is determined to be impaired, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in profit or loss.

If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through profit or loss.

Debt securities in issue are initially measured at fair value, which is the consideration received, net of directly attributable transaction costs incurred. Subsequent measurement is at amortised cost, using the effective interest rate method to amortise the difference between proceeds net of directly attributable transaction costs and the redemption amount over the expected life of the debt, unless the securities are designated at fair value.

Deposits by Banks, Customers & Related Parties

Deposits by banks, customers, and related parties are recognised when the Banking Group enters into the contractual provisions of the arrangements with counterparties, which is generally on trade date, and initially measured at fair value, which is normally the consideration net of directly attributable transaction costs incurred. Subsequent measurement is at amortised cost, using the effective interest rate method to amortise the difference between proceeds net of directly attributable transaction costs and the redemption amount over the expected life of the deposit.

Derivative Financial Instruments

Derivatives are bilateral contracts or payment exchange agreements whose value derives from the value of an underlying asset, reference rate or index. Derivative financial instruments include foreign exchange and interest rate forwards, forward purchase and sale agreements, futures, options, interest rate and currency swaps.

Derivatives are initially recognised at fair value from the date a derivative contract is entered into and subsequently remeasured at their fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and valuation techniques. The fair values represent the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Changes in the fair value, together with related interest income and expense, are recognised immediately in profit or loss as 'Net trading income'.

Valuation techniques include discounted cash flow models and option pricing models as appropriate. All derivatives are classified as assets when their fair value is positive and as liabilities when their fair value is negative.

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

Derivative Financial Instruments *(continued)*

In the normal course of business, the fair value of a derivative at initial recognition is considered to be the transaction price (i.e. the fair value of the consideration given or received). However, in certain circumstances the fair value of an instrument will be evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When such evidence exists, the Banking Group recognises trading profits on inception of the derivative.

If observable market data is not available, the initial increase in fair value indicated by the valuation model, but based on unobservable inputs, is not recognised immediately in profit or loss but is recognised over the life of the transaction on an appropriate basis, or recognised in profit or loss when the inputs become observable, or when the transaction matures or is closed out.

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

Derivative Financial Instruments – Hedge Accounting

The method of recognising the resulting fair value gain or loss depends on whether the derivative is held for trading, or designated as a hedging instrument, and if so, the nature of the item being hedged. All gains and losses from changes in the fair value of derivatives held for trading are recognised in profit or loss. Where derivatives are designated as hedges, the Banking Group classifies them as either:

- hedges of the fair value of recognised assets or liabilities or firm commitments (fair value hedge); or
- hedges of highly probable future cash flows attributable to a recognised asset or liability, or a forecasted transaction (cash flow hedge).

It is the Banking Group's policy to document, at the inception of the transaction, the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. Such policies also require documentation of the assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. Interest on designated qualifying hedges is included in "net interest income".

Fair value hedge

Fair value hedges in place principally consisted of interest rate swaps that are used to protect against changes in the fair value of fixed-rate long-term financial instruments due to movements in market interest rates.

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in profit or loss, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

If a hedging relationship no longer meets the criteria for hedge accounting, the cumulative adjustment to the carrying amount of the hedged item is amortised to profit or loss based on a recalculated effective interest rate over the residual period to maturity, unless the hedged item is derecognised, in which case, it is released to the profit or loss immediately.

If the hedged item is an available-for-sale asset, hedge accounting will discontinue prospectively and the effect of previous hedge accounting will not be reversed.

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

Derivative Financial Instruments – Hedge Accounting *(continued)*

Cash flow hedge

Cash flow hedges in place represent hedges via interest rate swaps of interest rate risk associated with certificates of deposit issued, medium term notes issued, and assets such as certificates of deposit purchased.

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in equity in the cash flow hedge reserve and other comprehensive income. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss.

Amounts accumulated in equity are recycled to profit or loss in the periods in which the hedged item will affect profit or loss (for example, when the forecast sale that is hedged takes place). However, when the forecast transaction that is hedged results in the recognition of a non-financial asset or a liability, the gains and losses previously recognised in equity are transferred from equity and included in the initial measurement of the cost of the asset or liability.

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

Derivatives that do not qualify for hedge accounting

Certain derivative instruments, used for risk management purposes, do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting, together with related interest income and expense, are recognised immediately in profit or loss as 'Other net operating income'.

Hedge effectiveness testing

To qualify for hedge accounting, NZ IAS 39 requires that at the inception of the hedge and throughout its life, each hedge must be expected to be highly effective (prospective effectiveness). Actual effectiveness (retrospective effectiveness) must also be demonstrated on an on-going basis.

The documentation of each hedging relationship sets out how the effectiveness of the hedge is assessed. The method the Banking Group adopts for assessing hedge effectiveness will depend on its risk management strategy.

For fair value hedge relationships, the Banking Group uses the cumulative dollar offset method or regression analysis as effectiveness testing methodologies. For cash flow hedge relationships, the Banking Group uses the change in variable cash flow method or the cumulative dollar offset method using the hypothetical derivative approach.

For prospective effectiveness, the hedging instrument must be expected to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated. For actual effectiveness, the changes in the fair value or cash flows must offset each other in the range of 80%-125% for the hedge to be deemed effective.

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

Employee Benefits

Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in profit or loss as incurred.

Share-based payments

HSBC enters into equity-settled share-based payment arrangements with its employees as compensation for services provided by employees. Equity-settled share-based payment arrangements entitle employees to receive equity instruments of HSBC.

The cost of equity-settled share-based payment arrangements with employees is measured by reference to the fair value of equity instruments on the date they are granted and recognised as an expense on a straight-line basis from the start of the period to which the service relates to the end of the vesting period.

A cancellation that occurs during the vesting period is treated as an acceleration of vesting, and recognised immediately for the amount that would otherwise have been recognised for services over the vesting period.

Other Reserve

The other reserve comprises the share-based payment reserve accounts. These accounts are used to record the corresponding amount relating to share options granted to employees of the Banking Group directly by HSBC Holdings plc.

Financial Instruments Designated as at Fair Value Through Profit or Loss

A financial instrument, other than one held for trading, is classified in this category if it meets the criteria set out below, and is so designated by management:

- eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring financial assets or financial liabilities or recognising the gains and losses on them on different bases; or
- applies to a group of financial assets, financial liabilities or both that is managed and its performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and where information about that group of financial instruments is provided internally on that basis to key management personnel; or
- relates to financial instruments containing one or more embedded derivatives that significantly modify the cash flows resulting from those financial instruments.

The Banking Group may designate certain financial instruments as at fair value through profit or loss to remove or reduce accounting mismatches in measurement or recognition.

Financial assets and financial liabilities so designated are recognised initially at fair value, with transaction costs taken directly to profit or loss, and are subsequently measured at fair value. Financial assets and financial liabilities are recognised using trade date accounting.

Gains and losses from changes in the fair value of such assets and liabilities are recognised in profit or loss as they arise.

Gains and losses arising from the changes in the fair value of derivatives that are managed in conjunction with financial assets and financial liabilities designated at fair value are included in profit or loss.

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

Financial Instruments – Right to Offset

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

Fixed Assets

Leasehold improvements are stated at cost less accumulated depreciation and impairment losses. Depreciation is calculated on a straight-line basis to write off the assets over the unexpired term of the lease, which is generally 5 years.

Equipment, fixtures and fittings are stated at cost less accumulated depreciation and impairment losses. Depreciation is calculated on the straight-line basis to write off the assets over their estimated useful lives, which are generally between 3 and 5 years. Where material parts of an asset have different useful lives, they are accounted for as separate assets.

Foreign Currencies

Transactions in foreign currencies are recorded in the functional currency at the rate of exchange ruling on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rate of exchange ruling at the end of the reporting period. Any resulting exchange differences are included in profit or loss. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated into the functional currency using the rate of exchange at the date of the initial transaction. Non-monetary assets and liabilities measured at fair value in a foreign currency are translated into the functional currency using the rate of exchange at the date the fair value was determined.

Funds Management Activities

HSBC Investments New Zealand Limited previously acted as manager for the HSBC Cash Fund, the HSBC Term Fund, the HSBC Global Unit Trusts, and the HSBC World Selection Funds. The Unit Trusts have now closed.

Intangible Assets

Goodwill

Goodwill represents the difference between the cost of an acquisition and the fair value of the net identifiable assets acquired. Acquisition expenses such as professional fees and legal fees directly attributable to an acquisition are expensed.

Goodwill is stated at cost less any accumulated impairment losses.

Goodwill is assessed at each reporting date to determine whether there is an indication of impairment. If any such indication exists, goodwill is tested for impairment. Goodwill is tested for impairment at least annually by comparing the present value of the expected future cash flows from a business with the carrying value of its net assets, including attributable goodwill. Goodwill is allocated to cash-generating units for the purposes of impairment testing. Goodwill is tested for impairment at the lowest level at which it is monitored for internal management purposes. Any impairment loss in respect of goodwill would not be reversed.

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

Intangible Assets *(continued)*

Other Intangible Assets

Intangible assets include internally generated computer software and customer relationships purchased. Intangible assets that are not yet ready for use are tested at least annually for impairment or at each reporting date where there is an indicator of impairment.

Intangible assets that have a finite useful life are stated at cost less amortisation and accumulated impairment losses and are amortised on a straight line basis over their useful lives as follows:

- Customer relationships – between 3 and 12 years
- Software – between 3 and 5 years.

Intangible assets are subject to impairment review at each reporting date to determine if there are events or changes in circumstances that indicate that the carrying amount may not be recoverable.

Interest Income & Expense

Interest income and expense for financial assets and financial liabilities that are not measured at fair value are recognised in profit or loss using the effective interest rates of the financial assets or financial liabilities to which they relate.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability or, where appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. Interest on impaired financial assets is recognised at the original effective interest rate of the financial asset applied to the impaired carrying amount.

Income – Net Fees

The Banking Group earns fee and commission income from a diverse range of services it provides to its customers including fiduciary activities. Fee and commission income is accounted for as follows:

- If the income is earned on the execution of a significant act, it is recognised as revenue when the significant act has been completed (for example, commission and fees arising from negotiating, or participating in the negotiation of, a transaction for a third party, such as the arrangement for the acquisition of shares or other securities);
- If the income is earned as services are provided, it is recognised as revenue as the services are provided (for example, asset management, portfolio and other management advisory and service fees); and
- If the income is an integral part of the effective interest rate of a financial instrument, it is recognised as an adjustment to the effective interest rate (for example, loan establishment fees).

Leases

Leases where substantially all the risks and rewards associated with ownership remain with the lessor, are classified as operating leases. Assets leased under operating leases are not recognised in the Statement of Financial Position. Payments made under operating leases are recognised in profit or loss on a straight line basis over the term of the lease. Lease incentives received are recognised in profit or loss over the lease term as an integral part of the total lease expense.

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

Sale & Repurchase Agreements

When securities are sold subject to a commitment to repurchase them at a predetermined price (“repos”) they remain on the Statement of Financial Position and a liability is recorded in respect of the consideration received. The Banking Group does not purchase securities under commitment to sell (“reverse repos”).

The difference between the sale and repurchase price is treated as interest and recognised over the life of the agreement.

The Banking Group does not engage in securities borrowing transactions. Securities lending transactions are generally entered into on a collateralised basis, with securities or cash received as collateral. The transfer of the securities to counterparties is not normally reflected on the Statement of Financial Position.

If cash collateral is received, a liability is recorded at the amount of cash collateral received.

Statement of Cash Flows

The Statement of Cash Flows has been prepared using the direct approach modified by the netting of certain items as appropriate.

Cash and cash equivalents reflect the balance of cash and liquid assets used in the day-to-day cash management of the Banking Group, which are unconditionally convertible into cash within no more than two working days. For the purpose of the cash flow statement, cash and cash equivalents include highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value. Certain cash flows have been netted in order to provide more meaningful disclosure in compliance with the standards.

Taxation

Income tax on the profit or loss for the period comprises current tax and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to items recognised directly in other comprehensive income or equity, in which case it is recognised in other comprehensive income.

Current tax is the expected tax payable on the taxable income for the period, calculated using tax rates enacted or substantially enacted by the end of the reporting period, and any adjustment to tax payable in respect of previous years. Current tax assets and liabilities offset when a legal right to offset exists and the assets and liabilities relate to income taxes levied by the same taxation authority.

Deferred tax is recognised on temporary differences between the carrying amount of assets and liabilities in the Statement of Financial Position and the amount attributed to such assets and liabilities for tax purposes. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent it is probable that future taxable profits will be available against which deductible temporary differences can be utilised.

Deferred tax is calculated using the tax rates expected to apply in the periods in which the assets will be realised or the liabilities settled. Deferred tax assets and liabilities are offset when a legal right to offset exists and the assets and liabilities relate to income taxes levied by the same taxation authority.

Tax related to fair value re-measurement of available-for-sale investments and cash flow hedges, which are charged or credited directly to other comprehensive income, is also credited or charged directly to other comprehensive income and is subsequently recognised in profit or loss when the deferred gain or loss is recognised in profit or loss.

The taxation standard NZ IAS 12 has been applied when transacting business combinations. The standard requires certain tax-effect accounting entries to be passed on acquisition date where there is a difference between the tax cost base and accounting carrying value. A taxable temporary difference arises which results in a deferred tax liability.

Notes to and forming part of the Financial Statements *(continued)*

1. Statement of Accounting Policies *(continued)*

Trustee Activities

The HSBC Cash Fund, HSBC Term Fund, HSBC Global Unit Trusts, and HSBC World Selection Funds were managed by HSBC Investments New Zealand Limited with an independent trustee (New Zealand Guardian Trust) responsible for ensuring that the HSBC Cash Fund, HSBC Term Fund, HSBC Global Unit Trusts, and HSBC World Selection Funds were administered in accordance with the trust deed. The Directors of HSBC Investments New Zealand Limited meet regularly to ensure that managed fund activities were managed independently from other activities carried out by the Banking Group. These Unit Trusts are now closed.

2. Risk Management

POLICIES

The Banking Group operates risk management policies in accordance with HBAP policies and procedures established by HSBC Holdings plc ("Group"). Systems and procedures are in place to identify, control and report on major risks including credit, market, liquidity and operational risk (including accounting, tax, legal, compliance, information, physical security and fraud risk). Exposure to these risks is monitored by the Banking Group's Risk Management Committee ("RMC"), Asset and Liability Management Committee ("ALCO") and Executive Committee ("EXCO"). These committees meet on a monthly basis to ensure that risk management systems, controls and procedures are operating effectively. The monitoring and review of the Banking Group's risk management systems is not conducted by a party which is external to the Banking Group or Group. Specific risk management policies and procedures are outlined below.

Credit risk

Credit risk, including concentration of credit risk, intra day credit risk, credit risk to bank counterparties and related party credit risk, is the risk that a customer or counterparty of the Banking Group will be unable or unwilling to meet a commitment that it has entered into with the Banking Group.

It arises from the lending, trade finance, treasury and other finance activities undertaken by the Banking Group. The Banking Group has policies and procedures for the control and monitoring of all such risks.

The HSBC Holdings plc Group Management Office ("GMO") is responsible for the formulation of high level credit policies, the independent review of the Group's largest credit exposures, the control of the Group's cross-border exposures and portfolio management of risk concentrations. It also reviews the efficiency of Group companies' credit approval processes, a key element of which is the Group's universal facility grading system.

HBAP Executive Committee receives regular reports on credit exposures within the Group. These include information on asset concentrations, industry exposures, levels of bad debt provisioning and country exposure limits.

In the Banking Group, local management is responsible for the quality of its credit portfolios. The Banking Group has established a credit process involving delegated approval authorities, credit procedures and regular reviews, the objective of which is to build and maintain risk assets of high quality. Collateral is taken to reduce credit risk where it is considered necessary after local management's credit evaluation of the counterparty.

The Group's credit risk limits to counterparties in the financial and government sectors are managed centrally to optimise the use of credit availability and to avoid excessive risk concentration. The Banking Group remains responsible for its own credit exposures. In addition to the portfolio management undertaken at Group level, the Banking Group manages its own risk concentrations on a market sector, geographical and product basis.

Cross-border risk is controlled through the imposition of country limits, with sub-limits by maturity and type of business. Transactions with higher risk countries are considered on a case-by-case basis.

Special attention is paid to the management of problem loans.

Notes to and forming part of the Financial Statements *(continued)*

2. Risk Management *(continued)*

Credit risk *(continued)*

The Banking Group does have legal right of off-set in some instances under certain conditions. At present all balances have been disclosed gross with the conditions giving rise to the legal right of off-set not being present.

Market risk

Market risk is the risk that movements in foreign exchange rates, interest rates, credit spreads or equity and commodity prices will result in profits or losses to the Banking Group. Market risk arises on financial instruments which are measured at fair value and those which are measured at amortised cost. The objective of market risk management is to control market risk exposures to achieve an optimal return while maintaining risk at acceptable levels.

The Banking Group monitors market risk separately for trading portfolios and non-trading portfolios. Trading portfolios include positions arising from market making in exchange rates, interest rates, credit and equity derivative instruments, as well as in debt and equity securities. Trading risks arise either from customer related business or from proprietary position taking.

The management of market risk is principally undertaken in Global Markets using risk limits approved by the Group Management Board. Group Risk, an independent unit within GMO develops the Group's market risk management policies and measurement techniques.

Risk limits are determined for each location and, within location, for each portfolio. Limits are set by product and risk type with market liquidity being a principal factor in determining the level of limits set. Limits are set using a combination of risk measurement techniques, including position limits, sensitivity limits, as well as value at risk limits at a portfolio level. Similarly, option risks are controlled through full revaluation limits in conjunction with limits on the underlying variables that determine each option's value.

The Banking Group is required to assess the market risks which arise on each product in its business and to transfer these risks to either its local Global Markets unit for management, or to separate books managed under the supervision of ALCO. The aim is to ensure that all market risks are consolidated within operations which have the necessary skills, tools, management and governance to manage such risks professionally. In certain cases where the market risks cannot be adequately captured by the transfer process, simulation modelling is used to identify the impact of varying scenarios on valuations and net interest income.

Notes to and forming part of the Financial Statements *(continued)*

2. Risk Management *(continued)*

Market risk *(continued)*

Value at Risk (“VAR”)

One of the principal tools used by the Group to monitor and limit market risk exposure is VAR. VAR is a technique which estimates the potential losses that could occur on risk positions taken due to movements in market rates and over a specified time horizon and to a given level of confidence (for Group, 99%). VAR is calculated daily.

The Group uses a historical simulation model which derives plausible future scenarios from historical market data. Potential movements in market prices are calculated with reference to market data from the last two years. The model assumes a 1 day holding period, as this reflects the way the risk positions are managed.

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

- the use of historical 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 1 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 1 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;
- VAR is calculated on the basis of exposures outstanding at close of business and therefore does not necessarily reflect intra-day exposures; and
- VAR is unlikely to reflect loss potential on exposures that only arise under significant market moves.

The Group recognises these limitations by augmenting the VAR limits with other position and sensitivity limit structures, as well as with stress testing, both on individual portfolios and on a consolidated basis. The Group’s stress testing regime provides senior management with an assessment of the impact of extreme events on the market risk exposures of the Group.

Stress Testing

Stress testing involves historical simulation calculations conducted under scenario models provided by Group Risk. Stress testing enables firms to gain useful insight into low probability possible losses in situations where normal market relationships breakdown. In such abnormal or crisis situations, vital model inputs swing to extreme values and losses can be much greater than is suggested by VAR models.

The Group carries out stress testing at a regional level in HBAP and at a global level in GMO using data from internal systems. Testing is performed using HBAP’s RiskWatch system and is compiled using the selected scenarios into graphical form on a local level.

The scenarios considered, along with the realism of the currency and interest rate shifts suggested, are discussed and determined at regular meetings of the Stress Test Review Group which comprises senior members of Group staff.

The Banking Group does not hold any significant open trading positions. Under current scenarios the potential adverse profit impact is immaterial. This is consistent with the comparable period.

Notes to and forming part of the Financial Statements *(continued)*

2. Risk Management *(continued)*

Market risk *(continued)*

Trading

The Group's control of market risk is based on restricting individual operations to trading within a list of permissible instruments authorised for each site by Group Risk, and enforcing rigorous new product approval procedures. In particular, trading in the more complex derivative products is concentrated in offices with appropriate levels of product expertise and robust control systems.

In addition, at both portfolio and position levels, market risk in trading portfolios is monitored and controlled using a complementary set of techniques such as VAR and present value of a basis point ("PVBP"), together with stress and sensitivity testing and concentration limits. These techniques quantify the impact on capital of defined market movements.

Non-trading

Market risk in non-trading portfolios arises principally from mismatches between the future yield on assets and their funding cost, as a result of interest rate changes. Analysis of this risk is complicated by having to make assumptions on optionality in certain product areas, for example, mortgage prepayments and from behavioural assumptions regarding the economic duration of liabilities which are contractually repayable on demand, for example, current accounts. In order to manage this risk optimally, market risk in non-trading portfolios is transferred to Global Markets or to separate books and managed under the supervision of ALCO.

The transfer of market risk to books managed by Global Markets or supervised by ALCO is usually achieved by a series of internal deals between the business units and these books. When the behavioural characteristics of a product differ from its contractual characteristics the behavioural characteristics are assessed to determine the true underlying interest rate risk. ALCO regularly monitors all such behavioural assumptions and interest rate risk positions to ensure they comply with interest rate risk limits established by HBAP Executive Committee.

As noted above in certain cases the non-linear characteristics of products cannot be adequately captured by the risk transfer. For example both the flow from customer deposit accounts to alternate investment products and the precise prepayment speeds of mortgages will vary at different interest rate levels. In such circumstances simulation modelling is used to identify the impact of varying scenarios on valuations and net interest income.

Once market risk has been consolidated in Global Markets or ALCO managed books, the net exposure is typically managed through the use of interest rate swaps within agreed limits.

Within the Group, banking entities also monitor the sensitivity of projected net interest income under varying interest rate scenarios. The Group aims through its management of market risk in non-trading portfolios to mitigate the impact of prospective interest rate movements which could reduce future net interest income, whilst balancing the cost of such hedging activities on the current net revenue stream.

Currency risk

The Banking Group's foreign currency exposures comprise those which arise from foreign exchange dealing within Global Markets and currency exposures originated by other banking business. The latter are transferred to Global Markets where they are managed together with exposures which result from dealing within limits approved by HBAP Executive Committee. These exposures are managed on a daily basis.

Foreign currency risk exposure is disclosed in note 28. A sensitivity analysis is not performed due to the Banking Group FX exposure being materially hedged.

Notes to and forming part of the Financial Statements *(continued)*

2. Risk Management *(continued)*

Interest rate risk

The Banking Group's interest rate exposures comprise those originating in its trading activities and structural interest rate exposures; both are managed under limits described above.

Structural interest rate risk arises primarily from fixed rate loans and liabilities other than those generated by Global Markets business. Each business unit's structural interest rate risk is transferred to Global Markets.

These interest rate positions are regularly monitored by ALCO. While the primary objective of such interest rate risk management is to limit potential adverse effects of interest rate movements on net interest income, the Banking Group also seeks to enhance net interest income, subject to risk limits approved by HBAP Executive Committee.

The Group predominantly uses the PVBP calculation for measuring and monitoring interest rate risk globally. The PVBP calculation, which measures the change in mark to market for a 1 basis point movement in interest rates, provides a useful real-time tool to monitor interest rate risk. PVBP is measured in USD.

The analysis below shows the impact on before tax profit and loss and equity reserves of a 1 basis point increase in interest rates (across all currencies). The opposite impact would be expected for a 1 basis point decrease. Financial instruments recorded at amortised cost are therefore, not included as their reported values are not impacted by interest rate movements. Profit and loss impacts are represented by trading book activities recorded at fair value.

USD PVBP	Audited 31.12.14	Audited 31.12.13
Equity Reserves	33,163	17,031
Profit and Loss	(5,371)	(3,908)

Liquidity and funding

Liquidity risk is the risk that the Banking Group does not have sufficient financial resources to meet its obligations as they fall due, or will have to do so at an excessive cost. This risk arises from mismatches in the timing of cash flows. Funding risk (a form of liquidity risk) arises when the liquidity needed to fund illiquid asset positions cannot be obtained at the expected terms and when required.

The objective of the Group's liquidity and funding management framework is to ensure that all foreseeable funding commitments can be met when due, and that access to the wholesale markets is co-ordinated and cost-effective. To this end, the Group maintains a diversified funding base comprising core retail and corporate customer deposits and institutional balances. This is augmented with wholesale funding and portfolios of highly liquid assets diversified by currency and maturity which are held to enable the Group to respond quickly and smoothly to unforeseen liquidity requirements.

The Group requires its operating entities to maintain strong liquidity positions and to manage the liquidity profiles of their assets, liabilities and commitments with the objective of ensuring that their cash flows are balanced appropriately and that all their anticipated obligations can be met when due.

The Group adapts its liquidity and funding risk management framework in response to changes in the mix of business that it undertakes, and to changes in the nature of the markets in which it operates.

Notes to and forming part of the Financial Statements *(continued)*

2. Risk Management *(continued)*

Liquidity and funding *(continued)*

Policies and procedures

Management of liquidity and funding is primarily undertaken locally in HBAP's operating entities in compliance with practices and limits set by HBAP ALCO. These limits vary according to the depth and liquidity of the market in which the entities operate. It is HBAP's general policy that each banking entity should be self-sufficient when funding its own operations. Exceptions are permitted for certain short-term treasury requirements and start-up operations or branches which do not have access to local deposit markets. These entities are funded from HBAP's largest banking operations and within clearly defined internal and regulatory guidelines and limits. These limits place formal restrictions on the transfer of resources between HBAP entities and reflect the broad range of currencies, markets and time zones within which HBAP operates.

It is the responsibility of ALCO to ensure compliance with local regulatory requirements and limits set by HBAP ALCO. Liquidity is managed on a daily basis by local treasury functions.

HBAP's liquidity and funding management process includes:

- projecting cash flows under various stress scenarios and considering the level of liquid assets necessary in relation thereto;
- monitoring balance sheet liquidity and advances to core funding ratios against internal and regulatory requirements;
- maintaining a diverse range of funding sources with adequate back-up facilities;
- managing the concentration and profile of debt maturities;
- managing contingent liquidity commitment exposures within pre-determined limits;
- maintaining debt financing plans;
- monitoring of depositor concentration in order to avoid undue reliance on large individual depositors and ensuring a satisfactory overall funding mix; and
- maintaining liquidity and funding contingency plans. These plans identify early indicators of stress conditions and describe actions to be taken in the event of difficulties arising from systemic or other crises, while minimising adverse long-term implications for the business.

Primary sources of funding

Current accounts and savings deposits payable on demand or at short notice form a significant part of HBAP's funding, and HBAP places considerable importance on maintaining their stability. For deposits, stability depends upon preserving depositor confidence in HBAP's capital strength and liquidity, and on competitive and transparent pricing. HBAP also accesses professional markets in order to provide funding for non-banking subsidiaries that do not accept deposits, to maintain a presence in local money markets and to optimise the funding of asset maturities not naturally matched by core deposit funding. In aggregate, HBAP's banking entities are liquidity providers to the interbank market, placing significantly more funds with other banks than they themselves borrow.

A contractual maturity analysis of assets and liabilities for the Banking Group is disclosed in note 25.

Core deposits

HBAP's internal framework is based on a categorisation of customer deposits into core and non-core based on the expectation of the behaviour of these deposits during a liquidity stress. This characterisation takes into account the inherent liquidity risk categorisation of the entity originating the deposit, the nature of the customer and the size and pricing of the deposit. Deposits deemed to be core are considered to be a long-term source of funding and are assumed to not be withdrawn in the liquidity stress used for principal liquidity risk metrics.

Notes to and forming part of the Financial Statements *(continued)***2. Risk Management** *(continued)***Liquidity and funding** *(continued)***Management of liquidity risk**

HBAP uses a number of principal measures to manage liquidity risk, as described below.

Advances to core funding ratio

HBAP emphasises the importance of core customer deposits as a source of funds to finance lending to customers, and discourages reliance on short-term professional funding. This is achieved by placing limits on banking entities which restrict their ability to increase loans and advances to customers without corresponding growth in core customer deposits or long term debt funding. This measure is referred to as the ‘advances to core funding’.

Advances to core funding ratio limits are set by the HBAP ALCO and monitored by HBAP Finance. The ratio describes current loans and advances to customers as a percentage of the total of core customer deposits and term funding with a remaining term to maturity in excess of one year. Loans and advances to customers which are part of reverse repurchase arrangements, and where HSBC receives securities which are deemed to be liquid, are excluded from the advances to core funding ratio.

The Branch’s advances to core funding ratios as at the reporting date and during the reporting period were as follows:

	Unaudited 12 months 31.12.14	Unaudited 12 months 31.12.13
	%	%
End of period	107	105
Maximum for the period	109	109
Minimum for the period	100	102
Average for the period	103	106

Projected cash flow scenario analysis

HBAP uses a number of standard hypothetical projected cash flow scenarios designed to model both HBAP specific and market-wide liquidity crises in which the rate and timing of deposit withdrawals and drawdowns on committed lending facilities are varied, and the ability to access interbank funding and term debt markets and to generate funds from asset portfolios are restricted. HBAP applies conservative criteria to those securities that can be deemed ‘liquid’ and are therefore assumed to be a source of funding under stress scenarios. The scenarios are modelled by all HBAP banking entities and by HBAP Finance. The appropriateness of the assumptions under each scenario is regularly reviewed. In addition to HBAP’s standard hypothetical projected cash flow scenarios, individual entities are required to design their own scenarios to reflect specific local market conditions, products and funding bases.

Limits for cumulative net cash flows under stress scenarios are set for each entity. Both ratio and cash flow limits reflect the local market place, the diversity of funding sources available and the concentration from large depositors. Compliance with entity level limits is monitored centrally.

As at 31 December 2014 the Branch has a committed loan facility from HBAP of USD 0.83 billion (December 2013: USD 0.83 billion). Up to USD 0.25 billion is on call, up to USD 0.35 billion may be drawn with 7 days notice, with a further USD 0.23 billion drawn with 30 days notice. The committed loan facility amount may change from time to time depending on the local balance sheet structure.

Notes to and forming part of the Financial Statements *(continued)***2. Risk Management** *(continued)***Liquidity and funding** *(continued)***Management of liquidity risk** *(continued)***Stressed one month coverage ratio**

The stressed one month coverage ratios tabulated below are derived from these scenario analyses, and express the stressed cash inflows as a percentage of stressed cash outflows over a one month time horizon. The Branch is required to target a ratio of 100 per cent or greater.

	Unaudited 12 months 31.12.14	Unaudited 12 months 31.12.13
	%	%
End of period	119	117
Maximum for the period	125	125
Minimum for the period	109	111
Average for the period	118	116

Contingent liquidity risk

In the normal course of business, the Branch provides customers with committed facilities, and standby facilities to corporate customers. These facilities increase the funding requirements of the Branch when customers choose to raise drawdown levels over and above their normal utilisation rates. The liquidity risk consequences of increased levels of drawdown are analysed in the form of projected cash flows under different stress scenarios. The HBAP ALCO also sets limits for non-cancellable contingent funding commitments for the Branch after due consideration of the Branch's ability to fund them. The limits are split according to the borrower, the liquidity of the underlying assets and the size of the committed line.

The Branch's contractual exposures at 31 December monitored under the contingent liquidity risk limit structure were as follows:

	Unaudited 31.12.14	Unaudited 31.12.13
	NZDm	NZDm
Non cancellable undrawn commitment limits		
Five largest	575	511
Largest market sector	618	495

Operational risk

Operational risk is the risk of losses as a result of inadequate systems and controls, human error or management failure. Risks include natural disaster, systems failure, fraud and non-compliance with legislation and regulations.

Local management is responsible for establishing an effective and efficient operational control environment in accordance with Group standards so that the Group's assets are adequately protected, and whereby the operational risks have been identified and adequate risk management procedures maintained to control those risks. Risk management techniques include appropriate systems, staff, internal controls and business continuity planning.

Notes to and forming part of the Financial Statements *(continued)*

2. Risk Management *(continued)*

Internal audit

Internal audit is an integral part of the control environment of the Group. It provides management and, through the Audit Committee, the Board with an independent and objective review of the business activities and support functions of the Group. The Banking Group does not have a separate Audit Committee.

The internal audit department has authority of access to all operations, records, property and staff at each location. All employees are required to co-operate fully with and provide full and complete information to the Group's internal auditors in the performance of their assigned duties.

Though some audit cycles are predetermined by regulatory or similar stipulations, in general, audits throughout the Group are carried out on a frequency determined primarily by the risk grading allocated to the business unit at the time of the previous audit, with units considered to represent greater risks being audited at more frequent intervals, with intervals between internal audits never to exceed two years. There are no regulatory stipulations governing the internal audit cycles of the Banking Group.

Access to parental disclosures on risk management processes and capital adequacy requirements

The most recent publicly available disclosures on risk management processes and capital adequacy requirements of HSBC Holdings plc can be found at HBAP's website, www.hsbc.com.hk under About HSBC, Financial Information, Financial Reports, HSBC Holdings plc.

Notes to and forming part of the Financial Statements (continued)

<i>Dollars in Thousands</i>	Banking Group and Branch	
	Audited 12 months 31.12.14	Audited 12 months 31.12.13
3. Operating income		
Interest income:		
Advances to banks	18,144	14,159
Debt securities	16,529	15,764
Advances to customers	170,615	157,673
Related parties – HBAP	815	742
Related parties – other	333	149
Other	57	7
	<u>206,493</u>	<u>188,494</u>
Interest expense:		
Deposits by banks	(4,946)	(3,289)
Customer deposits	(63,215)	(67,760)
Debt securities	(28,633)	(17,084)
Related parties – HBAP	(19,421)	(21,259)
Related parties – other	(339)	(98)
Other	-	(16)
	<u>(116,554)</u>	<u>(109,506)</u>
Other net operating income:		
Fee and commission income		
Lending and credit facility fees receivable	18,471	23,127
Custody and clearing fees receivable	4,098	2,940
Other fees and commissions receivable from:		
– Third parties	15,579	16,964
– Related parties-HBAP	157	684
– Related parties-other	949	515
	<u>39,254</u>	<u>44,230</u>
Fee and commission expense		
Brokerage expense	(1,653)	(1,308)
Other fees and commissions payable to:		
– Third parties	(384)	(373)
– Related parties-HBAP	(2,385)	(2,825)
– Related parties-other	(107)	(493)
	<u>(4,529)</u>	<u>(4,999)</u>
Other income		
Gain / (loss) on disposal of equipment, fixtures and fittings	-	8
	<u>-</u>	<u>8</u>
	<u>34,725</u>	<u>39,239</u>
Net trading income:		
Foreign exchange gains	11,535	12,997
Revaluation of derivatives	148	1,138
Credit valuation adjustments on derivatives	(19)	(2,000)
Debit valuation adjustments on derivatives	(3,025)	5,776
Loss on hedging instrument in fair value hedge	(2,362)	3,950
Gain on hedged item in fair value hedge	2,373	(3,949)
	<u>8,650</u>	<u>17,912</u>

Included within interest expense on debt securities is \$0.152 million (December 2013: \$0.806 million interest expense) of interest expense from derivatives held in a qualifying cashflow hedging relationship.

Included within interest income on debt securities is \$0.511 million (December 2013: \$0.403 million interest income) of interest income from derivatives held in a qualifying cashflow or fair value hedging relationship.

Included within interest income from advances to customers is \$5.626 million (December 2013: \$0.651 million) of interest income from impaired advances to customers.

Notes to and forming part of the Financial Statements (continued)**3. Operating income** (continued)**Amounts included in operating income relating to unconsolidated structured entities**

The Banking Group considers itself a sponsor of a structured entity when it facilitates the establishment of the structured entity. The table below sets out information in respect of structured entities that the Group sponsored, but in which the Banking Group does not have an interest. The amounts disclosed are recognised within other net operating income.

	<i>Banking Group and Branch</i>	
	Audited 12 months 31.12.14	Audited 12 months 31.12.13
<i>Dollars in Thousands</i>		
Fee income earned from:		
HSBC Global Unit Trusts	-	59
HSBC World Selection Trusts	-	18
	<u>-</u>	<u>77</u>

4. Operating expenses**Rental expense**

Premises	2,651	2,369
Equipment	194	298
	<u>2,845</u>	<u>2,667</u>

Depreciation and amortisation

Leasehold improvements	315	409
Equipment, fixtures and fittings	247	350
Intangibles	1,746	1,718
	<u>2,308</u>	<u>2,477</u>

Auditor's remuneration

Audit of financial statements	419	459
Audit related fees	19	22
Review of interim financial statements	86	87
Tax services	4	26
Other services	135	-
	<u>663</u>	<u>594</u>

Staff costs

Salaries & other staff expenses	25,216	25,298
Defined contribution pension costs	2,098	1,780
Share based payments	228	285
Leave provision movement	(12)	4
Other	1,047	1,195
	<u>28,577</u>	<u>28,562</u>

Other

Related party management and technical fees – HBAP	14,154	13,535
Related party management and technical fees – other	1,630	1,777
Donations	135	166
Other operating expenses	8,614	8,705
	<u>24,533</u>	<u>24,183</u>
	<u>58,926</u>	<u>58,483</u>

The average number of persons employed by the Branch for the twelve months was 225 (December 2013: 224).

Audit related fees include fees charged for the reporting on custodial services and trust deed. Other services provided by the auditor are regulatory compliance assurance services.

Notes to and forming part of the Financial Statements *(continued)***5. Segment reporting**

Segment information is presented in respect of the Banking Group's business segments based on the Banking Group's management and internal reporting structure.

Business segments pay and receive interest to and from Global Banking and Markets on an arm's length basis to reflect the allocation of funding costs.

The Banking Group operates primarily in New Zealand. Geographical information on revenues from external customers is not available and the cost to develop it would be excessive.

Business Segments

The Banking Group comprises the following main business segments:

- *Retail Banking and Wealth Management ("RBWM")*
Includes loans, deposits and other transactions with retail customers.
- *Commercial Banking ("CMB")*
Manages the relationships with corporate customers providing loans, deposits and other transactions including trade finance and payment cash management.
- *Global Banking and Markets ("GBM")*
Manages the relationships with institutional customers and undertakes the Banking Group's treasury and investment banking operations.

Reconciling items primarily include income from the investment of interest free funding from HBAP provided to support thin capitalisation ratios and income from the investment of retained profits.

<i>Banking Group and Branch</i>						
Audited 12 months ended 31.12.14						
<i>Dollars in Thousands</i>	RBWM	CMB	GBM	Total Reportable Segments	Reconciling items	Consolidated
Operating income	33,634	74,961	17,884	126,479	6,835	133,314
Operating profit / (loss) before tax	12,684	65,265	7,732	85,681	6,753	92,434
Net Interest Income	31,361	42,065	9,684	83,110	6,829	89,939
Depreciation and amortisation	231	240	825	1,296	1,012	2,308
Other material non-cash items						
Impairment losses on financial assets	506	3,325	-	3,831	-	3,831
Impairment recoveries on financial assets	(1,030)	(20,847)	-	(21,877)	-	(21,877)
Total other material non-cash items	(524)	(17,522)	-	(18,046)	-	(18,046)

Notes to and forming part of the Financial Statements *(continued)***5. Segment reporting** *(continued)*

The following tables present the segment reporting for the comparative period.

Banking Group and Branch						
Audited 12 months ended 31.12.13						
<i>Dollars in Thousands</i>	RBWM	CMB	GBM	Total Reportable Segments	Reconciling items	Consolidated
Operating income	30,153	74,069	26,009	130,231	5,908	136,139
Operating profit / (loss) before tax	8,112	5,807	14,317	28,236	6,730	34,966
Net Interest Income	26,671	37,319	9,928	73,918	5,070	78,988
Depreciation and amortisation	325	320	847	1,492	985	2,477
Other material non-cash items						
Impairment losses on financial assets	358	46,309	-	46,667	-	46,667
Impairment recoveries on financial assets	(1,275)	(2,702)	-	(3,977)	-	(3,977)
Total other material non-cash items	(917)	43,607	-	42,690	-	42,690

Notes to and forming part of the Financial Statements (continued)

	<i>Banking Group and Branch</i>	
	Audited 12 months 31.12.14	Audited 12 months 31.12.13
<i>Dollars in Thousands</i>		
6. Taxation		
Current tax expense		
Current tax expense	<u>23,069</u>	<u>3,531</u>
	23,069	3,531
Deferred tax expense		
Origination and reversal of temporary differences	<u>2,909</u>	<u>6,368</u>
	2,909	6,368
Total income tax expense included in profit after tax	<u>25,978</u>	<u>9,899</u>
Reconciliation of effective tax rate		
Operating profit before tax	<u>92,434</u>	<u>34,966</u>
Income tax using the domestic corporation tax rate	28.0% <u>25,882</u>	28.0% <u>9,790</u>
Non-deductible expenses	0.1% <u>75</u>	0.3% <u>109</u>
Under / (over) provided in prior periods	0.0% <u>21</u>	0.0% <u>-</u>
Other permanent differences	0.0% <u>-</u>	0.0% <u>-</u>
	28.1% <u>25,978</u>	28.3% <u>9,899</u>
Recognised deferred tax assets and liabilities		
<u>Assets</u>		
Accelerated capital allowances	<u>480</u>	<u>428</u>
Provision for loan impairment	<u>7,267</u>	<u>13,638</u>
Other provisions	<u>771</u>	<u>(140)</u>
Income deferred for accounting purposes	<u>2,956</u>	<u>662</u>
	<u>11,474</u>	<u>14,588</u>
<u>Liabilities</u>		
Other intangible assets	<u>(753)</u>	<u>(958)</u>
Tax deductible premium	<u>(3,595)</u>	<u>(3,595)</u>
Cash flow hedges	<u>(40)</u>	<u>(905)</u>
	<u>(4,388)</u>	<u>(5,458)</u>
Deferred tax asset	<u>7,086</u>	<u>9,130</u>

With the exception of cash flow hedge temporary differences, all deferred tax on temporary differences is recognised in the profit or loss.

Notes to and forming part of the Financial Statements (continued)

<i>Dollars in Thousands</i>	<i>Banking Group and Branch</i>	
	Audited 31.12.14	Audited 31.12.13
7. Additional financial disclosures on the statement of financial position		
Total interest earning and discount bearing assets	5,059,148	4,833,643
Total interest and discount bearing liabilities	4,798,172	4,665,265
Total liabilities net of amounts due to related parties	4,225,221	4,243,409
Advances to banks pledged as collateral for liabilities in respect of credit support annex obligation to derivative counterparties	-	-
8. Advances to banks		
Able to be withdrawn without prior notice	14,871	15,179
9. Debt and equity securities		
Available-for-sale		
Debt securities	491,603	399,563
Treasury bills	2,955	-
Equity shares	22	22
	494,580	399,585

Notes to and forming part of the Financial Statements (continued)

	<i>Banking Group and Branch</i>	
<i>Dollars in Thousands</i>	Audited 31.12.14	Audited 31.12.13
10. Derivative financial instruments - assets		
Related party		
<i>Interest rate contracts</i>		
Trading derivatives	3,188	14,933
<i>Exchange rate contracts</i>		
Trading derivatives	77,269	116,721
Derivative financial instruments – related party	80,457	131,654
<i>Related party breakdown</i>		
HBAP	78,536	126,938
HSBC Bank Plc UK Ops	1,355	4,355
Others	566	361
	80,457	131,654
Others		
<i>Interest rate contracts</i>		
Cash flow hedging derivatives	1,491	3,677
Trading derivatives	13,522	12,707
Fair value hedging derivatives	1,027	2,618
	16,040	19,002
<i>Exchange rate contracts</i>		
Trading derivatives	99,685	97,511
Derivative financial instruments – others	115,725	116,513
Total derivative financial instruments - assets	196,182	248,167

Cashflow hedges

Principal asset balances of hedged items, on which the expected interest cash flows arise, are as follows:

	Audited 31.12.14	Audited 31.12.13
<i>Dollars in Millions</i>		
3 months	843	733

This table reflects the interest rate refixing profile of the underlying hedged items.

The gains and losses on ineffective portions of cash flow hedges are recognised immediately in profit or loss.

Notes to and forming part of the Financial Statements (continued)

<i>Dollars in Thousands</i>	Banking Group and Branch	
	Audited 31.12.14	Audited 31.12.13
11. Advances to customers		
Maturity analysis		
Demand	255,253	195,554
Other short term	1,087,537	875,191
Long term	2,432,150	2,302,020
	<u>3,774,940</u>	<u>3,372,765</u>
12. Other assets		
Prepayments and accrued income – third party	19,587	12,344
Acceptances and endorsements	2,065	2,493
Other	1,269	2,107
	<u>22,921</u>	<u>16,944</u>
13. Intangible assets		
<u>Goodwill</u>		
Cost		
Balance at the beginning of the period	15,744	15,744
Balance at the end of the period	<u>15,744</u>	<u>15,744</u>
Impairment		
Balance at the beginning of the period	(2,043)	(2,043)
Balance at the end of the period	<u>(2,043)</u>	<u>(2,043)</u>
Carrying amounts		
Balance at the beginning of the period	13,701	13,701
Balance at the end of the period	<u>13,701</u>	<u>13,701</u>
<u>Other Intangible Assets</u>		
Customer relationships purchased		
Cost		
Balance at the beginning of the period	8,798	8,798
Balance at the end of the period	<u>8,798</u>	<u>8,798</u>
Amortisation and impairment		
Balance at the beginning of the period	(5,378)	(4,644)
Amortisation of customer relationships	(734)	(734)
Balance at the end of the period	<u>(6,112)</u>	<u>(5,378)</u>
Carrying amounts		
Balance at the beginning of the period	3,420	4,154
Balance at the end of the period	<u>2,686</u>	<u>3,420</u>

Notes to and forming part of the Financial Statements *(continued)*

<i>Dollars in Thousands</i>	Banking Group and Branch	
	Audited 31.12.14	Audited 31.12.13
13. Intangible assets <i>(continued)</i>		
<u>Other Intangible Assets</u> <i>(continued)</i>		
Internally generated computer software		
<i>Cost</i>		
Balance at the beginning of the period	4,540	4,540
Internal development	-	-
Balance at the end of the period	<u>4,540</u>	<u>4,540</u>
<i>Amortisation and impairment</i>		
Balance at the beginning of the period	(2,203)	(1,295)
Amortisation of internally generated computer software	(908)	(908)
Balance at the end of the period	<u>(3,111)</u>	<u>(2,203)</u>
<i>Carrying amounts</i>		
Balance at the beginning of the period	2,337	3,245
Balance at the end of the period	<u>1,429</u>	<u>2,337</u>
Purchased software		
<i>Cost</i>		
Balance at the beginning of the period	520	372
Additions	-	148
Balance at the end of the period	<u>520</u>	<u>520</u>
<i>Amortisation and impairment</i>		
Balance at the beginning of the period	(131)	(55)
Amortisation of purchased software	(104)	(76)
Balance at the end of the period	<u>(235)</u>	<u>(131)</u>
<i>Carrying amounts</i>		
Balance at the beginning of the period	389	317
Balance at the end of the period	<u>285</u>	<u>389</u>
Total Intangible Assets	<u>18,101</u>	<u>19,847</u>

Notes to and forming part of the Financial Statements *(continued)***13. Intangible assets** *(continued)***Goodwill****a) goodwill arising from the acquisition of AMP Bank Limited's loan and deposit portfolio**

Goodwill arose in 2003 upon acquisition of part of AMP Bank Limited's ("AMP") loan and deposit portfolio.

This goodwill relates entirely to the Branch's retail banking business, being the cash-generating unit ("CGU") as defined in NZ IAS 36. The carrying amount that relates to this CGU at 31 December 2014 is \$12.840 million (December 2013: \$12.840 million).

Goodwill is assessed at each reporting date for indicators of impairment as it is not amortised.

The recoverable amount of the CGU is determined based on value-in-use calculations. These calculations use discounted cash flow projections based on profit forecasts approved by management as part of the rolling operating plan process. The rolling operating plan covers a detailed two year time frame, approved by HBAP senior management. Profit forecasts greater than two years are estimated by Branch management based on their assessment of sustainable growth. The discounted cash flow model has used a five year profit projection, a discount rate (pre tax) of 14.9% (December 2013: 15.6%), average annual growth rates for revenues and direct expenses (as detailed in the following table) supported by December 2014 actual results, and a terminal value of \$157.3 million (December 2013: \$105.6 million).

Average annual growth rate projections as at 31 December 2014

	Years 1-2	Years 3-5	5 Year Average
Revenues	5.8%	3.0%	4.1%
Direct Expenses	(1.8)%	2.0%	0.4%

The net average annual growth rate for revenues and expenses for years 3 to 5 is supported by the actual December 2014 results and is consistent with December 2013 forecasted growth. This shows stable cash flow projections. Average annual growth beyond 5 years does not exceed the average growth in GDP for New Zealand over the last 10 years.

Average annual growth rate projections as at 31 December 2013

	Years 1-2	Years 3-5	5 Year Average
Revenues	5.6%	3.0%	4.0%
Direct Expenses	(1.7)%	2.0%	0.5%

Key assumptions underlying the valuation relate to management's assessment of balance sheet growth, net interest margins, fee generation, bad debts, operating expenses and terminal value. Management utilise local market data as well as Group expertise and experience to validate key assumptions.

The most significant variable underlying the valuation is the terminal value. Terminal value is calculated using a stable growth model. The key variables used to calculate terminal value are the post tax discount rate of 10.7% (December 2013: 11.2% and an annual sustainable growth rate from January 2019 onwards of 1.9% (December 2013 2.2 %) which is equal to the average growth in GDP for New Zealand over the last 10 years. The terminal value would need to reduce by around 138% (December 2013: 134%), all other variables being equal, in order for the CGU's recoverable amount to be equal to its carrying value. As at 31 December 2014 the recoverable amount exceeds the carrying amount by \$130.5million (December 2013: \$83.3million).

Notes to and forming part of the Financial Statements *(continued)***13. Intangible assets** *(continued)***Goodwill****b) goodwill arising from the acquisition of Westpac Banking Corporation's ("WBC") custody and clearing business in New Zealand**

Goodwill arose in September 2006 upon acquisition by the Branch of Westpac Banking Corporation's New Zealand custody and clearing business.

This goodwill relates entirely to the Branch's custody and clearing business, being the cash-generating unit ("CGU") as defined in NZ IAS 36. The carrying value that relates to this CGU at 31 December 2014 is \$0.861 million (December 2013: \$0.861 million).

The goodwill is assessed at each reporting date for indicators of impairment as it is not amortised.

The recoverable amount of the CGU is determined based on value-in-use calculations. These calculations use discounted cash flow projections based on profit forecasts approved by management as part of the rolling operating plan process. The rolling operating plan covers a detailed two year time frame, approved by HBAP senior management. Profit forecasts greater than two years are estimated by Branch management based on their assessment of sustainable growth. The discounted cash flow model has used a five year profit projection, a discount rate (pre tax) of 14.9% (December 2013: 15.6%), annual growth rate for revenues and direct expenses (as detailed in the following table) supported by December 2014 actual results, and a terminal value of \$23.9 million (December 2013: \$15.2 million).

Average annual growth rate projections as at 31 December 2014

	Years 1-2	Years 3-5	5 Year Average
Revenues	1.9%	3.0%	2.5%
Direct Expenses	10.7%	2.0%	5.2%

The net average annual growth rate for revenues and expenses for years 3 to 5 is supported by the actual December 2014 results and is consistent with December 2013 forecasted growth. This shows stable cash flow projections. Average annual growth beyond 5 years does not exceed the average growth in GDP for New Zealand over the last 10 years.

Average annual growth rate projections as at 31 December 2013

	Years 1-2	Years 3-5	5 Year Average
Revenues	3.9%	3.0%	3.3%
Direct Expenses	15.6%	2.0%	6.8%

Key assumptions underlying the valuation relate to management's assessment of customer transaction volumes, share market turnover and value, fee structures, operating expenses and terminal value. Management utilise local market data as well as Group expertise and experience to validate key assumptions.

The most significant variable underlying the valuation is the terminal value. Terminal value is calculated using a stable growth model. The key variables used to calculate terminal value are the post tax discount rate of 10.7% (December 2013: 11.2%) and an annual sustainable growth rate from January 2019 onwards of 1.9% (December 2013: 2.2%) which is equal to the average growth in GDP for New Zealand over the last 10 years. The terminal value would need to reduce by around 131% (December 2013: 109%), all other variables being equal, in order for the CGU's recoverable amount to be equal to its carrying value. As at 31 December 2014 the recoverable amount exceeds the carrying amount by \$18.8 million (December 2013: \$9.7 million)

Notes to and forming part of the Financial Statements *(continued)*

13. Intangible assets *(continued)*

Other Intangible Assets

Other intangible assets primarily represent purchased software, internally generated computer software and customer relationships arising from the Branch's acquisition of Westpac Banking Corporation's New Zealand custody and clearing business.

The purchased software is amortised on a straight line basis over 5 years.

The internally generated computer software is amortised on a straight line basis over 5 years. The remaining unamortised periods at 31 December 2014 are between 1 year 5 months and 1 year 11 months (December 2013: 2 years 5 months and 2 years 11 months).

These customer relationships are amortised on a straight-line basis over 12 years based on a statistical analysis of expected customer life. The remaining unamortised period at 31 December 2014 is 3 years 8 months (December 2013: 4 years 8 months).

These intangible assets are assessed at each reporting date for indications of impairment.

Notes to and forming part of the Financial Statements (continued)

<i>Dollars in Thousands</i>	Banking Group and Branch	
	Audited 31.12.14	Audited 31.12.13
14. Fixed assets		
Leasehold improvements		
<i>Cost</i>		
At beginning of period	6,737	6,530
Additions	-	207
Disposals	-	-
At end of period	<u>6,737</u>	<u>6,737</u>
<i>Accumulated depreciation</i>		
At beginning of period	5,940	5,531
Depreciation charge	315	409
Disposals	-	-
At end of period	<u>6,255</u>	<u>5,940</u>
Closing net book value	<u>482</u>	<u>797</u>
Equipment, fixtures and fittings		
<i>Cost</i>		
At beginning of period	4,018	4,106
Additions	217	234
Disposals	(54)	(322)
At end of period	<u>4,181</u>	<u>4,018</u>
<i>Accumulated depreciation</i>		
At beginning of period	3,498	3,470
Depreciation charge	247	350
Disposals	(54)	(322)
At end of period	<u>3,691</u>	<u>3,498</u>
Closing net book value	<u>490</u>	<u>520</u>
Total net book value	<u>972</u>	<u>1,317</u>

Notes to and forming part of the Financial Statements (continued)

	Banking Group and Branch	
<i>Dollars in Thousands</i>	Audited 31.12.14	Audited 31.12.13
15. Asset quality		
Past due but not impaired		
Less than 30 days	90,758	38,212
At least 30 days but less than 60 days	2,166	1,287
At least 60 days but less than 90 days	113	116
At least 90 days	-	-
Carrying amount	<u>93,037</u>	<u>39,615</u>
In the current and prior period, there was only one class of impaired financial assets, being advances to customers.		
Gross individually impaired assets		
Balance at the beginning of the period	141,964	65,217
Exchange adjustment	-	-
Transfers from performing	2,497	142,317
Transfers to performing	(117)	(636)
Write-offs	(6)	(7,410)
Repayment	(22,425)	(7,659)
Sale of portfolio of impaired assets	-	(49,865)
Balance at the end of the period	<u>121,913</u>	<u>141,964</u>
Specific provision for loan impairment		
Balance at the beginning of the period	40,317	49,533
New and additional provisions charged to profit or loss	506	40,914
Provisions released during the period to profit or loss	(14,471)	(1,246)
Write-offs	(6)	(7,410)
Discount unwind ¹	(5,626)	(590)
Discount unwind ¹ - sale of portfolio of impaired loans	-	(61)
Provisions released - sale of portfolio of impaired loans	-	(40,823)
Balance at the end of the period	<u>20,720</u>	<u>40,317</u>
Collective provision for loan impairment		
Balance at the beginning of the period	8,391	3,817
Additional provision charged to profit or loss	3,325	5,753
Provisions released during the period to profit or loss	(6,482)	(1,179)
Balance at the end of the period	<u>5,234</u>	<u>8,391</u>
Total provisions for loan impairment	<u>25,954</u>	<u>48,708</u>
Profit or loss charge / (credit)		
Specific provisions for impairment against advances	506	40,914
Collective provisions for impairment against advances	3,325	5,753
Total provisions for impairment against advances	<u>3,831</u>	46,667
Specific provisions released	(14,471)	(1,246)
Collective provisions released	(6,482)	(1,179)
Total provisions released no longer required	<u>(20,953)</u>	<u>(2,425)</u>
Net increase / (decrease) in provisions for impairment against advances	(17,122)	44,242
Recoveries of amounts written off in previous period	(924)	(1,552)
	<u>(18,046)</u>	<u>42,690</u>

¹ The impairment loss on an impaired asset is calculated as the difference between the asset's carrying amount and the estimated future cash flows discounted to its present value using the original effective interest rate for the asset. This discount unwinds as interest income over the period the asset is held.

There are no restructured assets, assets acquired through the enforcement of security or assets under administration. The aggregate amount as at 31 December 2014 of any undrawn balances on lending commitments to counterparties for whom drawn balances are classified as individually impaired, before deducting allowances for credit impairment loss where applicable, is \$21.2 million (December 2013: \$9.3 million).

Notes to and forming part of the Financial Statements (continued)

	<i>Banking Group and Branch</i>	
<i>Dollars in Thousands</i>	Audited 31.12.14	Audited 31.12.13
16. Deposits by banks		
Demand	182,194	153,521
Other short term	-	4,157
	<u>182,194</u>	<u>157,678</u>
17. Derivative financial instruments – liabilities		
Related party		
<i>Interest rate contracts</i>		
Trading derivatives	14,057	12,170
<i>Exchange rate contracts</i>		
Trading derivatives	100,367	91,105
Derivative financial instruments – related party	<u>114,424</u>	<u>103,275</u>
<i>Related party breakdown</i>		
HBAP	113,206	102,166
HSBC Bank Plc UK Ops	712	948
Others	506	161
	<u>114,424</u>	<u>103,275</u>
Others		
<i>Interest rate contracts</i>		
Cash flow hedging derivatives	1,296	573
Trading derivatives	2,540	15,261
Fair value hedging derivatives	733	228
	<u>4,569</u>	<u>16,062</u>
<i>Exchange rate contracts</i>		
Trading derivatives	67,921	103,837
Derivative financial instruments – others	<u>72,490</u>	<u>119,899</u>
Total derivative financial instruments – liabilities	<u>186,914</u>	<u>223,174</u>

Cash flow hedges

Principal liability balances of hedged items, on which the expected interest cash flows arise, are as follows:

<i>Dollars in Millions</i>	Audited 31.12.14	Audited 31.12.13
3 months	668	213

This table reflects the interest rate refixing profile of the underlying hedged items.

The gains and losses on ineffective portions of cash flow hedges are recognised immediately in profit or loss.

Notes to and forming part of the Financial Statements (continued)

<i>Dollars in Thousands</i>	Banking Group and Branch	
	Audited 31.12.14	Audited 31.12.13

18. Customer deposits

Deposits on demand	1,895,376	1,732,909
Savings and term deposits	1,285,558	1,403,041
	<u>3,180,934</u>	<u>3,135,950</u>

The total retail term deposits as at 31 December 2014 were \$1,249,730 thousand (December 2013: \$1,360,470 thousand).

The balance of retail deposits issued to unit holders of the HSBC Cash Fund is \$0 (December 2013: \$0) and the balance of retail deposits issued to unit holders of the HSBC Term Fund is \$0 (December 2013: \$0).

The total other money market deposits as at 31 December 2014 were \$60,082 thousand (December 2013: \$140,575 thousand).

19. Debt securities

Certificates of deposit issued	339,746	392,482
Medium term notes issued	400,000	400,000
	<u>739,746</u>	<u>792,482</u>

There are no debt securities on demand.

20. Other liabilities

Accruals and deferred income	32,897	30,425
Acceptances and endorsements	2,065	2,493
Other	7,748	4,482
	<u>42,710</u>	<u>37,400</u>

Accruals as at 31 December 2014 include \$6.2 million for employee entitlements (December 2013: \$6.8 million).

Notes to and forming part of the Financial Statements *(continued)***21. Related party transactions**

Related party transactions are unsecured and entered into in the normal course of business. During the period there have been dealings between the Branch, Banking Group, HBAP and its subsidiaries and associated companies and other members of the ultimate holding company. Dealings include activities such as funding, accepting deposits, derivative transactions together with management and technical fees.

The balances for derivative financial instruments with related parties have been disclosed in Note 10 and Note 17.

The financial statements of the Banking Group should be read in conjunction with the financial statements of HBAP for period ended 31 December 2014.

<i>Dollars in Thousands</i>	Banking Group and Branch	
	Audited 31.12.14	Audited 31.12.13
Key management compensation		
(a) Salaries and other short-term benefits	5,200	4,766
(b) Post-employment benefits	172	155
(c) Share-based payments expenses recognised	181	201
	5,553	5,122

(d) Shares, options and other incentive plans

(i) HSBC Holdings Savings-Related Share Option Plan (International)

The subscription to this share option plan was closed in 2013 and therefore no share option was granted since 2013.

(ii) HSBC Restricted Share Award Scheme

Number of options awarded	15,621	15,909
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The total fair value of the options awarded under the restricted share award scheme is \$190 thousand when converted into NZ dollars at grant date (December 2013: \$211 thousand).

The vesting period of the restricted share awards is staggered over three years.

The fair value of the share option granted under the HSBC Restricted Share Award Scheme is £6.16 (December 2013: £7.35).

Key management personnel represent the members of the New Zealand EXCO who are employees of the Registered Bank.

Interest Free Funding

The Branch has received an interest free loan from HBAP of \$194 million (December 2013: \$194 million) to support the thin capitalisation ratio imposed under New Zealand tax law.

Notes to and forming part of the Financial Statements (continued)

<i>Dollars in Thousands</i>	Banking Group and Branch	
	Audited 31.12.14	Audited 31.12.13
21. Related party transactions (continued)		
Amounts due from related parties		
On demand	10,965	51,965
Other short term	356,554	256,903
	<u>367,519</u>	<u>308,868</u>
The Hongkong and Shanghai Banking Corporation Limited (HBAP):		
Hong Kong Branch	354,527	258,303
Singapore Branch	3,429	3,689
Sri Lanka Branch	3,306	-
Tokyo Branch	381	21,802
Other	138	294
Other:		
HSBC Bank plc	4,117	23,168
HUSI Non-Insurance North America	873	878
HSBC Bank Australia Limited	348	588
Other	400	146
	<u>367,519</u>	<u>308,868</u>
Amounts due to related parties		
On demand	262,531	313,652
Other short term	451,192	483,610
Long term	211,403	11,434
	<u>925,126</u>	<u>808,696</u>
The Hongkong and Shanghai Banking Corporation Limited (HBAP):		
Singapore Branch	13,306	18,680
Hong Kong Branch	850,249	675,406
Brunei Branch	172	5,090
Other	4,424	5,280
Other:		
HSBC Bank USA	11,189	5,364
HSBC Bank Plc UK Ops	27,717	24,416
HSBC Bank Malaysia Berhad	1,178	12,348
Bank of Bermuda – Bermuda	4,010	32,153
HIB plc London Branch	-	11,340
HSBC Bank Taiwan	1,437	6,039
Other	11,444	12,580
	<u>925,126</u>	<u>808,696</u>

Notes to and forming part of the Financial Statements (continued)**22. Fair value of financial instruments****Determination of fair value of financial instruments carried at fair value**

Fair values are determined according to the following hierarchy:

Level 1 – quoted market price

Financial instruments with quoted prices for identical instruments in active markets.

Level 2 – valuation technique using observable inputs

Financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.

Level 3- valuation technique with significant unobservable inputs

Financial instruments valued using valuation techniques where one or more significant inputs are unobservable.

The best evidence of fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In the event that the market for a financial instrument is not active, a valuation technique is used.

The judgement as to whether a market is active may include, but is not restricted to, the consideration of factors such as the magnitude and frequency of trading activity, the availability of prices and the size of bid / offer spreads. In inactive markets, obtaining assurance that the transaction price provides evidence of fair value or determining the adjustments to transaction prices that are necessary to measure the fair value of the instrument requires additional work during the valuation process.

The table below provides an analysis of the various bases described above which have been deployed for valuing financial assets and financial liabilities measured at fair value.

	<i>Banking Group and Branch</i>			
	Audited 31.12.14			
<i>Dollars in Thousands</i>	Level 1	Level 2	Level 3	TOTAL
ASSETS				
Debt and equity securities	356,621	137,937	22	494,580
Derivatives financial instruments	-	196,182	-	196,182
LIABILITIES				
Derivatives financial instruments	-	186,914	-	186,914

	<i>Banking Group and Branch</i>			
	Audited 31.12.13			
<i>Dollars in Thousands</i>	Level 1	Level 2	Level 3	TOTAL
ASSETS				
Debt and equity securities	280,136	119,427	22	399,585
Derivatives financial instruments	-	248,167	-	248,167
LIABILITIES				
Derivatives financial instruments	-	223,174	-	223,174

There have been no significant transfers between levels 1 and 2 in the period to 31 December 2014 (December 2013: Nil).

Notes to and forming part of the Financial Statements *(continued)***22. Fair value of financial instruments** *(continued)***Reconciliation of fair value measurements in level 3 of the fair value hierarchy**

The following table provides a reconciliation of the movement between opening and closing balance of level 3 financial instruments, measured at fair value using a valuation technique with significant unobservable inputs.

<i>Dollars in Thousands</i>	<i>Banking Group and Branch Audited 31.12.14</i>		
	<u>Assets</u>	<u>Assets</u>	<u>Liabilities</u>
	<u>Available- For-sale</u>	<u>Derivatives</u>	<u>Derivatives</u>
Balance at the beginning of the period	22	-	-
Balance at the end of the period	<u>22</u>	<u>-</u>	<u>-</u>

<i>Dollars in Thousands</i>	<i>Banking Group and Branch Audited 31.12.13</i>		
	<u>Assets</u>	<u>Assets</u>	<u>Liabilities</u>
	<u>Available- For-sale</u>	<u>Derivatives</u>	<u>Derivatives</u>
Balance at the beginning of the period	22	-	-
Balance at the end of the period	<u>22</u>	<u>-</u>	<u>-</u>

Sources of uncertainty for fair value measurement in level 3

For the available-for-sale equity securities, the unobservability of valuation of certain equity shares resulted in these assets being determined as level 3. There is no quoted market price in an active market. The valuation is based on management judgement.

Effects of changes in significant non-observable assumptions to reasonably possible alternatives

For the available-for-sale equity securities, given that their total carrying amount at December 2014 is \$22 thousand (2013: \$22 thousand), the effect in equity arising from changes in significant non-observable assumptions is insignificant.

Notes to and forming part of the Financial Statements *(continued)*

22. Fair value of financial instruments *(continued)*

Methodologies

The methodologies and assumptions used when determining fair value depend on the terms and risk characteristics of the various instruments and include the following:

Cash and demand balances with central banks

For cash and short - term funds the carrying amount is equivalent to the fair value.

Debt securities issued

Fair value for certificates of deposit and medium term notes issued with maturities less than six months is approximated to be the carrying value. For certificates of deposit and medium term notes issued with a maturity greater than six months but less than a year, fair value is determined by using discounted cash flow methods using the interest rates applicable to financial instruments of similar maturity. Inputs applied in getting the fair value of debt securities between 6 and 12 months are observable market-corroborated inputs which include interest rates and forward curves observable at commonly reported intervals, and credit spreads. Debt securities greater than 12 months are fair valued using market-corroborated swap rates.

Debt securities

For available-for-sale securities that are quoted in active markets, fair values are determined by reference to the current quoted bid/offer price. Where quoted market prices are not available, fair value is determined with reference to quoted prices for similar instruments in active markets, or through the use of a valuation model where inputs are observable.

Advances to customers, advances to banks, and amounts due from related parties

Fair values of advances to customers, advances to banks, and amounts due from related parties with maturities of six months or longer have been estimated by discounting cashflows up to the next repricing date with reference to current rates at which similar loans and advances would be made to other borrowers with a similar credit rating and the same maturities. The fair values of advances to customers, advances to banks, and amounts due from related parties with maturities less than six months are approximated to be the carrying value.

Deposits, other accounts and amounts due to related parties

The fair values of deposits and other liabilities with maturities of less than six months are approximated to be the carrying amount. For liabilities with maturities of six months or longer, fair values have been based on quoted market prices, where such prices exist. Otherwise, fair values have been estimated by reference to rates currently offered by the Banking Group for similar liabilities of similar maturities.

Derivative financial instruments

The fair values of exchange rate and interest rate contracts were obtained from quoted market prices or discounted cash flow models. Inputs applied in getting the fair value of derivative financial instruments are observable market-corroborated inputs which include interest rates and forward curves observable at commonly reported intervals where required.

Other assets and other liabilities

For other assets and other liabilities the carrying amount is considered to be the fair value.

Notes to and forming part of the Financial Statements *(continued)***22. Fair value of financial instruments** *(continued)*

The following table summarises the carrying values and fair values of financial assets and liabilities in the Banking Group.

<i>Dollars in Thousands</i>	Banking Group and Branch			
	Audited 31.12.14 Carrying Value	Audited 31.12.14 Fair Value	Audited 31.12.13 Carrying Value	Audited 31.12.13 Fair Value
ASSETS				
Advances to customers	3,774,940	3,782,726	3,372,765	3,377,023
Total financial assets not carried at fair value	3,774,940	3,782,726	3,372,765	3,377,023
Total financial assets whose carrying value approximates fair value	1,507,374	1,507,374	1,751,751	1,751,751
Total financial assets	5,282,314	5,290,100	5,124,516	5,128,774
Total non-financial assets	26,406		31,165	
Total assets	5,308,720		5,155,681	
LIABILITIES				
Customer deposits	3,180,934	3,182,901	3,135,950	3,139,382
Debt securities	739,746	739,735	792,482	792,430
Amounts due to related parties	925,126	925,438	808,696	808,495
Total financial liabilities not carried at fair value	4,845,806	4,848,074	4,737,128	4,740,307
Total financial liabilities whose carrying value approximates fair value	406,359	406,359	415,595	415,595
Total financial liabilities	5,252,165	5,254,433	5,152,723	5,155,902
Total non-financial liabilities	12,606		2,657	
Total liabilities	5,264,771		5,155,380	

Notes to and forming part of the Financial Statements *(continued)***22. Fair value of financial instruments** *(continued)*

The table below provides an analysis of the various bases described on page 58 which have been deployed for summarising financial assets and financial liabilities fair value which are not carried at fair value.

<i>Banking Group and Branch</i>				
Audited				
31.12.14				
<i>Dollars in Thousands</i>	Level 1	Level 2	Level 3	TOTAL
ASSETS				
Advances to customers	-	-	3,782,726	3,782,726
LIABILITIES				
Customer deposits	-	-	3,182,901	3,182,901
Debt securities	-	739,735	-	739,735
Amounts due to related parties	-	-	925,438	925,438

<i>Banking Group and Branch</i>				
Audited				
31.12.13				
<i>Dollars in Thousands</i>	Level 1	Level 2	Level 3	TOTAL
ASSETS				
Advances to customers	-	-	3,377,023	3,377,023
LIABILITIES				
Customer deposits	-	-	3,139,382	3,139,382
Debt securities	-	792,430	-	792,430
Amounts due to related parties	-	-	808,495	808,495

Refer page 60 for the methodologies and assumptions used when determining fair value for the above financial assets and financial liabilities.

Notes to and forming part of the Financial Statements (continued)**23. Concentrations of credit and funding risk**

The maximum credit risk of on-balance sheet financial assets is best represented by the carrying amount of the assets, net of any provision for credit impairment. The credit risk exposure does not take into account the fair value of any collateral, in the event of other parties failing to perform their obligations under financial instruments.

<i>Dollars in Thousands</i>	<i>Banking Group and Branch</i>	
	Audited 31.12.14	Audited 31.12.13
On-balance sheet credit exposures		
Cash and demand balances with central banks	411,548	763,286
Advances to banks	14,871	15,179
Debt and equity securities	494,580	399,585
Advances to customers	3,774,940	3,372,765
Amounts due from related parties	367,519	308,868
Other assets	22,674	16,666
	5,086,132	4,876,349
Off-balance sheet credit exposures and derivatives	2,330,650	2,259,683
Total credit exposures	7,416,782	7,136,032

Concentrations of credit risk exist if a number of counterparties are engaged in similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. The following analysis of financial assets by industry sector is based on categories and definitions used by the Hong Kong Monetary Authority:

Concentrations of credit risk by industry

Individual	1,254,185	1,266,002
Commercial and industrial	2,337,304	2,356,767
Commercial real estate and construction	744,757	530,449
Banks and financial institutions	1,887,117	2,094,315
Agriculture, forestry and mining	305,858	164,023
Other	887,561	724,476
	7,416,782	7,136,032

Concentrations of credit risk by geographical area

New Zealand	6,271,096	5,973,892
Hong Kong	424,858	294,969
Other Overseas	720,828	867,171
	7,416,782	7,136,032

Concentration of Credit Exposures to Individual counterparties

The Banking Group has no credit exposures equal to or in excess of 10% of HBAP Group's equity, during the current reporting period and the previous corresponding period. These exposures do not include exposures to counterparties if they are booked outside of New Zealand.

Notes to and forming part of the Financial Statements *(continued)***23. Concentrations of credit and funding risk** *(continued)*

	<i>Banking Group and Branch</i>	
<i>Dollars in Thousands</i>	Audited 31.12.14	Audited 31.12.13
Concentrations of funding		
Concentrations of funding by product		
Deposits by banks	182,194	157,678
Customer deposits	3,180,934	3,135,950
Debt securities	739,746	792,482
Amounts due to related parties	925,126	808,696
	<u>5,028,000</u>	<u>4,894,806</u>
Concentrations of funding by industry		
Agriculture, forestry, fishing and mining	70,037	63,842
Manufacturing	296,575	192,601
Electricity, gas and water	146	376
Wholesale and retail trade	139,219	132,455
Accommodation and restaurants	35,648	31,339
Banking and finance	2,159,864	2,113,868
Property and business services	201,627	268,524
Local authorities	13,193	5,960
Individual	1,911,748	1,954,688
Other	199,943	131,153
	<u>5,028,000</u>	<u>4,894,806</u>
Concentrations of funding by geographical area		
New Zealand	2,644,198	2,606,314
Australia	48,431	51,009
China	366,532	374,640
Great Britain	171,884	166,401
Hong Kong	1,153,718	925,343
Malaysia	37,207	55,278
Singapore	59,963	68,052
Taiwan	56,597	64,372
Other Overseas	489,470	583,397
	<u>5,028,000</u>	<u>4,894,806</u>

Notes to and forming part of the Financial Statements *(continued)***23. Concentrations of credit and funding risk** *(continued)*

The credit quality of impaired advances is assessed by reference to a standard credit rating system.

Grades 1 and 2 include corporate facilities demonstrating financial condition, risk factors and capacity to repay that are good to excellent, residential mortgages with low to moderate loan to value ratios and other retail accounts which are maintained within product guidelines.

Grade 3 represents satisfactory risk, and includes corporate facilities that require closer monitoring, mortgages with higher loan to value ratios, and other retail exposures which operate outside product guidelines.

Grades 4 and 5 include facilities that require varying degrees of special attention.

Grades 6 and 7 relate to impaired loans and advances.

	<i>Banking Group and Branch</i>	
<i>Dollars in Thousands</i>	Audited 31.12.14	Audited 31.12.13
Carrying amount		
Advances to customers	3,774,940	3,372,765
Individually Impaired		
Grade 6: Impaired	121,913	141,964
Gross amount	121,913	141,964
Allowance for impairment	(20,720)	(40,317)
Carrying amount	101,193	101,647
Collectively Impaired		
Allowance for impairment	(5,234)	(8,391)
Carrying amount	(5,234)	(8,391)
Past due but not impaired		
Grade 1-3: Low-fair risk	86,846	33,129
Grade 4-5: Watch List	6,191	6,486
Carrying amount	93,037	39,615
Past due comprises:		
0-30 days	90,758	38,212
30-90 days	2,279	1,403
90 days +	-	-
Carrying amount	93,037	39,615
Neither past due nor impaired		
Grade 1-3: Low-fair risk	3,442,909	3,089,328
Grade 4-5: Watch List	143,035	150,566
Carrying amount	3,585,944	3,239,894
Total carrying amount	3,774,940	3,372,765

Notes to and forming part of the Financial Statements *(continued)***23. Concentration of credit and funding risk** *(continued)*

The Banking Group holds collateral against advances to customers in the form of mortgage interest over property, other registered securities over assets, and guarantees. The Banking Group generally applies a loan to value ratio for customer advances of 80%, however this ratio may be varied according to other criteria such as customer income streams, mortgage protection insurance and relationship with HSBC. Estimates of fair value are based on the value of the collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired.

Collateral is generally not held over advances to banks, except when securities are held as part of reverse repurchase and securities borrowing activity.

There are no other assets, including Cash and demand balances with central banks, Advances to banks, Debt securities, Derivative financial instruments, and Amounts due from related parties which are considered past due, or impaired at the end of the reporting period (December 2013: Nil).

Other financial assets neither past due nor impaired

The credit quality of other financial assets that were neither past due or impaired can be assessed by reference to the internal rating system adopted by the Banking Group. The below schedule excludes accrued interest.

<i>Dollars in Thousands</i>	<i>Banking Group and Branch</i>			
	TOTAL	Grade 1-2	Grade 3	Grade 4-5
31 December 2014 (Audited)				
Cash and demand balances with central banks	411,548	411,548	-	-
Advances to banks	14,871	14,820	51	-
Debt and equity securities	494,580	494,580	-	-
Derivative financial instruments	196,182	184,104	10,165	1,913
Amounts due from related parties	367,519	367,519	-	-
31 December 2013 (Audited)				
Cash and demand balances with central banks	763,286	763,286	-	-
Advances to banks	15,179	14,781	398	-
Debt and equity securities	399,585	399,585	-	-
Derivative financial instruments	248,167	227,404	19,533	1,230
Amounts due from related parties	308,868	308,868	-	-

Notes to and forming part of the Financial Statements (continued)**24. Interest rate risk – repricing schedule**

The table below analyses the Banking Group's assets and liabilities into relevant maturity groupings based on the earlier of residual contractual maturity or interest repricing date.

<i>Dollars in Millions</i>	Banking Group and Branch							<i>Total</i>
	<i>Up to 3 months</i>	<i>Over 3 months and up to 6 months</i>	<i>Over 6 months and up to 1 year</i>	<i>Over 1 year and up to 2 years</i>	<i>Over 2 years</i>	<i>Total interest bearing</i>	<i>Non interest bearing</i>	
31 December 2014 (Audited)								
<i>Assets</i>								
Cash and demand balances with central banks	411	-	-	-	-	411	-	411
Advances to banks	15	-	-	-	-	15	-	15
Debt and equity securities	122	128	5	30	210	495	-	495
Derivative financial instruments	-	-	-	-	-	-	196	196
Advances to customers	2,825	165	140	396	249	3,775	-	3,775
Amounts due from related parties	363	-	-	-	-	363	4	367
Other assets	-	-	-	-	-	-	23	23
Deferred taxation	-	-	-	-	-	-	7	7
Current taxation	-	-	-	-	-	-	-	-
Intangible assets	-	-	-	-	-	-	18	18
Fixed assets	-	-	-	-	-	-	1	1
<i>Total assets</i>	3,736	293	145	426	459	5,059	249	5,308
<i>Liabilities</i>								
Deposits by banks	182	-	-	-	-	182	-	182
Derivative financial instruments	-	-	-	-	-	-	187	187
Customer deposits	2,538	359	179	54	30	3,160	21	3,181
Debt securities	662	78	-	-	-	740	-	740
Amounts due to related parties	705	-	-	-	11	716	209	925
Other liabilities	-	-	-	-	-	-	43	43
Current taxation	-	-	-	-	-	-	7	7
<i>Total liabilities</i>	4,087	437	179	54	41	4,798	467	5,265
<i>Off-balance sheet financial instruments</i>								
Net notional interest rate contracts	626	(135)	-	(258)	(233)	-	-	-
31 December 2013 (Audited)								
<i>Assets</i>								
Cash and demand balances with central banks	763	-	-	-	-	763	-	763
Advances to banks	15	-	-	-	-	15	-	15
Debt and equity securities	101	-	83	136	80	400	-	400
Derivative financial instruments	-	-	-	-	-	-	248	248
Advances to customers	2,537	185	243	140	268	3,373	-	3,373
Amounts due from related parties	283	-	-	-	-	283	26	309
Other assets	-	-	-	-	-	-	17	17
Deferred taxation	-	-	-	-	-	-	9	9
Current taxation	-	-	-	-	-	-	1	1
Intangible assets	-	-	-	-	-	-	20	20
Fixed assets	-	-	-	-	-	-	1	1
<i>Total assets</i>	3,699	185	326	276	348	4,834	322	5,156
<i>Liabilities</i>								
Deposits by banks	157	1	-	-	-	158	-	158
Derivative financial instruments	-	-	-	-	-	-	223	223
Customer deposits	2,483	395	161	42	33	3,114	22	3,136
Debt securities	593	155	44	-	-	792	-	792
Amounts due to related parties	591	-	-	-	11	602	207	809
Other liabilities	-	-	-	-	-	-	37	37
<i>Total liabilities</i>	3,824	551	205	42	44	4,666	489	5,155
<i>Off-balance sheet financial instruments</i>								
Net notional interest rate contracts	204	-	169	(135)	(238)	-	-	-

Notes to and forming part of the Financial Statements (continued)**25. Liquidity risk management**

Liquidity risk is the risk that the Banking Group does not have sufficient financial resources to meet its obligations as they fall due, or will have to do so at an excessive cost. This risk arises from mismatches in the timing of cash flows.

Liquid assets are assets which are readily convertible to cash to meet the Banking Group's liquidity requirement. Liquid assets consist of demand balances with the central bank, treasury bills, government and local government bonds, and registered certificates of deposits issued by other banks. The Banking Group holds the following liquid assets in order to manage its liquidity risk:

<i>Dollars in Thousands</i>	<i>Banking Group and Branch</i>	
	Audited 31.12.14	Audited 31.12.13
Demand balances with the central bank	411,148	762,856
Available-for-sale debt securities and treasury bills	494,558	399,563
	905,706	1,162,419

Maturity Analysis

The table below analyses the Banking Group's assets and liabilities into relevant maturity groupings based on the remaining period at the end of the reporting period to the contractual maturity date.

<i>Dollars in Millions</i>	<i>Banking Group and Branch</i>							<i>Total</i>
	<i>On Demand</i>	<i>0-1 month</i>	<i>1-3 months</i>	<i>3-12 months</i>	<i>1-5 years</i>	<i>Over 5 years</i>	<i>No specific maturity</i>	
31 December 2014 (Audited)								
Assets								
Cash and demand balances with central banks	412	-	-	-	-	-	-	412
Advances to banks	15	-	-	-	-	-	-	15
Debt and equity securities	-	100	22	132	239	2	-	495
Advances to customers	255	115	196	777	1,468	964	-	3,775
Amounts due from related parties	11	356	-	-	-	-	-	367
Other assets	-	22	1	-	-	-	-	23
Deferred taxation	-	-	-	-	-	-	7	7
Intangible assets	-	-	-	1	3	-	14	18
Fixed assets	-	-	-	-	-	-	1	1
Total	693	593	219	910	1,710	966	22	5,113
Derivative financial instruments – inflow	-	24	233	628	1,289	1,738	-	3,912
Derivative financial instruments – (outflow)	-	-	(207)	(600)	(1,228)	(1,681)	-	(3,716)
Derivative financial instruments - assets	-	24	26	28	61	57	-	196
Liabilities								
Deposits by banks	182	-	-	-	-	-	-	182
Customer deposits	1,895	328	333	525	97	3	-	3,181
Debt securities	-	100	162	78	400	-	-	740
Amounts due to related parties	262	184	268	-	211	-	-	925
Other liabilities	-	29	13	-	1	-	-	43
Current taxation	-	-	7	-	-	-	-	7
Total	2,339	641	783	603	709	3	-	5,078
Derivative financial instruments – (inflow)	-	-	(207)	(600)	(1,228)	(1,679)	-	(3,714)
Derivative financial instruments – outflow	-	24	231	624	1,287	1,735	-	3,901
Derivative financial instruments – liabilities	-	24	24	24	59	56	-	187
Net assets	(1,646)	(48)	(562)	311	1,003	964	22	44

Notes to and forming part of the Financial Statements (continued)**25. Liquidity risk management** (continued)**Maturity Analysis** (continued)

<i>Dollars in Millions</i>	Banking Group and Branch							<i>Total</i>
	<i>On Demand</i>	<i>0-1 month</i>	<i>1-3 months</i>	<i>3-12 months</i>	<i>1-5 years</i>	<i>Over 5 years</i>	<i>No specific maturity</i>	
31 December 2013 (Audited)								
<i>Assets</i>								
Cash and demand balances with central banks	763	-	-	-	-	-	-	763
Advances to banks	15	-	-	-	-	-	-	15
Debt and equity securities	-	101	-	83	216	-	-	400
Advances to customers	196	108	175	592	1,297	1,005	-	3,373
Amounts due from related parties	52	243	14	-	-	-	-	309
Other assets	-	13	2	2	-	-	-	17
Deferred taxation	-	-	-	-	-	-	9	9
Current tax	-	-	-	1	-	-	-	1
Intangible assets	-	-	-	1	5	-	14	20
Fixed assets	-	-	-	-	-	-	1	1
<i>Total</i>	<u>1,026</u>	<u>465</u>	<u>191</u>	<u>679</u>	<u>1,518</u>	<u>1,005</u>	<u>24</u>	<u>4,908</u>
Derivative financial instruments – inflow	-	27	29	53	1,618	1,722	-	3,449
Derivative financial instruments – (outflow)	-	-	-	-	(1,548)	(1,653)	-	(3,201)
Derivative financial instruments - assets	-	27	29	53	70	69	-	248
<i>Liabilities</i>								
Deposits by banks	154	1	2	1	-	-	-	158
Customer deposits	1,733	342	428	541	75	17	-	3,136
Debt securities	-	114	79	199	400	-	-	792
Amounts due to related parties	314	121	163	200	11	-	-	809
Other liabilities	1	24	11	-	1	-	-	37
Current taxation	-	-	-	-	-	-	-	-
<i>Total</i>	<u>2,202</u>	<u>602</u>	<u>683</u>	<u>941</u>	<u>487</u>	<u>17</u>	<u>-</u>	<u>4,932</u>
Derivative financial instruments – (inflow)	-	-	-	-	(1,548)	(1,651)	-	(3,199)
Derivative financial instruments – outflow	-	23	25	48	1,607	1,719	-	3,422
Derivative financial instruments – liabilities	-	23	25	48	59	68	-	223
<i>Net assets</i>	<u>(1,176)</u>	<u>(133)</u>	<u>(488)</u>	<u>(257)</u>	<u>1,042</u>	<u>989</u>	<u>24</u>	<u>1</u>

Notes to and forming part of the Financial Statements (continued)**25. Liquidity risk management** (continued)**Maturity Analysis – undiscounted cashflows basis**

The table below analyses the Banking Group's financial assets and liabilities into relevant maturity groupings based on their remaining contractual maturities. The amounts in the table below represent all cash flows relating to principal and future interest payments on an undiscounted basis. Therefore they may differ to the carrying amounts on the Statement of Financial Position.

The Banking Group does not manage its liquidity risk on the basis of information below.

<i>Dollars in Millions</i>	Banking Group and Branch							<i>Total</i>
	<i>On Demand</i>	<i>0-1 month</i>	<i>1-3 months</i>	<i>3-12 months</i>	<i>1-5 years</i>	<i>Over 5 years</i>	<i>No specific maturity</i>	
31 December 2014 (Audited)								
Financial Assets								
Cash and demand balances with central banks	412	-	-	-	-	-	-	412
Advances to banks	15	-	-	-	-	-	-	15
Debt and equity securities	-	100	27	145	265	2	-	539
Advances to customers	255	131	225	898	1,804	1,754	-	5,067
Amounts due from related parties	11	356	-	-	-	-	-	367
Other assets	-	22	1	-	-	-	-	23
Total non-derivative financial assets	693	609	253	1,043	2,069	1,756	-	6,423
Derivative financial instruments – held for hedging purposes (net settled)								
Inflow / (outflow)	-	-	-	-	-	-	-	-
Total undiscounted financial assets	693	609	253	1,043	2,069	1,756	-	6,423
Financial Liabilities								
Deposits by banks	182	-	-	-	-	-	-	182
Customer deposits	1,895	332	339	544	110	3	-	3,223
Debt securities	-	102	166	93	432	-	-	793
Amounts due to related parties	262	185	269	6	218	-	-	940
Other liabilities	-	29	13	-	1	-	-	43
Total non-derivative financial liabilities	2,339	648	787	643	761	3	-	5,181
Derivative financial instruments – held for hedging purposes (net settled)								
(Inflow) / outflow	-	-	-	(1)	-	-	-	(1)
Total undiscounted financial liabilities	2,339	648	787	642	761	3	-	5,180
Undrawn loan commitments	591	-	1,151	-	-	-	-	1,742

Notes to and forming part of the Financial Statements (continued)**25. Liquidity risk management** (continued)**Maturity Analysis – undiscounted cashflows basis** (continued)

<i>Dollars in Millions</i>	Banking Group and Branch							<i>Total</i>
	<i>On Demand</i>	<i>0-1 month</i>	<i>1-3 months</i>	<i>3-12 months</i>	<i>1-5 years</i>	<i>Over 5 years</i>	<i>No specific maturity</i>	
31 December 2013 (Audited)								
<i>Financial Assets</i>								
Cash and demand balances with central banks	763	-	-	-	-	-	-	763
Advances to banks	15	-	-	-	-	-	-	15
Debt and equity securities	-	101	1	97	227	-	-	426
Advances to customers	196	120	198	691	1,586	1,767	-	4,558
Amounts due from related parties	52	243	14	-	-	-	-	309
Other assets	-	13	2	2	-	-	-	17
Total non-derivative financial assets	1,026	477	215	790	1,813	1,767	-	6,088
Derivative financial instruments – held for hedging purposes (net settled)								
Inflow / (outflow)	-	-	-	-	(1)	-	-	(1)
Total undiscounted financial assets	1,026	477	215	790	1,812	1,767	-	6,087
<i>Financial Liabilities</i>								
Deposits by banks	154	1	2	1	-	-	-	158
Customer deposits	1,733	344	435	557	89	17	-	3,175
Debt securities	-	114	83	213	440	-	-	850
Amounts due to related parties	314	121	164	204	11	-	-	814
Other liabilities	1	24	11	-	1	-	-	37
Total non-derivative financial liabilities	2,202	604	695	975	541	17	-	5,034
Derivative financial instruments – held for hedging purposes (net settled)								
(Inflow) / outflow	-	-	-	1	3	-	-	4
Total undiscounted financial liabilities	2,202	604	695	976	544	17	-	5,039
<i>Undrawn loan commitments</i>	577	-	996	-	-	-	-	1,553

Notes to and forming part of the Financial Statements *(continued)***26. Offsetting financial asset and financial liabilities**

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

Derivative agreements included in the ‘Related financial instruments that are not offset’ and ‘Cash collateral received that is not offset’ columns below relate to transactions where the counterparty has an offsetting exposure with the Banking Group and a master netting or similar arrangement is in place with a right of set off.

<i>Dollars in Millions</i>	Gross amounts of financial instruments in the statement of financial position	Related financial instruments that are not offset	Cash collateral received that is not offset	Net amount
31 December 2014				
Financial assets				
Derivative financial instruments	196	(17)	(23)	156
	<u>196</u>	<u>(17)</u>	<u>(23)</u>	<u>156</u>
Financial liabilities				
Deposits by banks	182	-	(23)	159
Derivative financial instruments	187	(17)	-	170
	<u>369</u>	<u>(17)</u>	<u>(23)</u>	<u>329</u>
31 December 2013				
Financial assets				
Derivative financial instruments	248	(42)	(7)	199
	<u>248</u>	<u>(42)</u>	<u>(7)</u>	<u>199</u>
Financial liabilities				
Deposits by banks	158	-	(7)	151
Derivative financial instruments	223	(42)	-	181
	<u>381</u>	<u>(42)</u>	<u>(7)</u>	<u>332</u>

Notes to and forming part of the Financial Statements *(continued)***27. Additional mortgage information****Residential mortgages by loan-to-valuation ratio**

	<i>Banking Group and Branch</i>			
	Principal Amount			Total
	Does not exceed 80% \$m	Exceeds 80% and not 90% \$m	Exceeds 90% \$m	
31 December 2014 (Unaudited)				
Value of exposures on balance sheet	1,023.8	14.4	2.4	1,040.6
Value of exposures off balance sheet	24.5	-	0.1	24.6
Total value of exposures	1,048.3	14.4	2.5	1,065.2
31 December 2013 (Unaudited)				
Value of exposures on balance sheet	1,036.0	21.8	2.7	1,060.5
Value of exposures off balance sheet	25.2	0.0	0.0	25.2
Total value of exposures	1,061.2	21.8	2.7	1,085.7

28. Foreign currency risk exposure

The net open position in each foreign currency, detailed in the table below, represents the on-balance sheet assets and liabilities in that foreign currency aggregated with the net expected future cash flows from off-balance sheet purchases and sales from foreign exchange transactions in that foreign currency. The amounts are stated in New Zealand dollar equivalents translated using the spot exchange rates as at the end of the reported period.

<i>Dollars in Millions</i>	<i>Banking Group and Branch</i>	
	Audited 31.12.14	Audited 31.12.13
Receivable / (payable)		
AUD	0.0	0.0
GBP	0.0	0.0
USD	0.1	0.0
Other	0.1	0.1
	0.2	0.1

Notes to and forming part of the Financial Statements *(continued)***29. Market risk exposures**

Aggregate market risk exposures are derived in accordance with the Capital Adequacy Framework (Standardised Approach) (BS2A) as stated in clauses 2 to 4 of the Ninth Schedule to the Order.

The period end exposure is the exposure as at the end of the period reported. The peak exposure is the peak end-of-day market risk exposure over the half year accounting period at the close of each business day. The peak is calculated separately for each category of exposure and may not have occurred at the same time.

<i>Dollars in Millions</i>	Banking Group	
	<i>Implied risk weighted Exposure</i>	<i>Notional capital charge</i>
<i>Exposure at 31 December 2014 (Unaudited)</i>		
Interest rate risk	34.13	2.73
Foreign currency risk	0.25	0.02
Equity risk	-	-
<i>Peak exposure period 1 July 2014 to 31 December 2014 (Unaudited)</i>		
Interest rate risk	58.13	4.65
Foreign currency risk	0.63	0.05
Equity risk	-	-
<i>Exposure at 31 December 2013 (Unaudited)</i>		
Interest rate risk	44.13	3.53
Foreign currency risk	0.13	0.01
Equity risk	-	-
<i>Peak exposure period 1 July 2013 to 31 December 2013 (Unaudited)</i>		
Interest rate risk	49.38	3.95
Foreign currency risk	1.88	0.15
Equity risk	-	-

Notes to and forming part of the Financial Statements *(continued)***30. Share options**

The Branch participated in the following share compensation plans operated by the Group for the acquisition of HSBC Holdings plc shares. The options were granted at nil consideration. No options have been granted to substantial shareholders, suppliers of goods and services, or in excess of the individual limit of each share plan. In April 2009, HSBC Holdings plc raised £12.5 billion (US\$17.8 billion), net of expenses, by the way of a fully underwritten rights issue, offering its shareholders 5 new ordinary shares for every 12 ordinary shares at a price of 254 pence per new ordinary share. The Remuneration Committee agreed to make adjustments to all unexercised share options and share awards under HSBC's various share plans and share schemes as a consequence of the rights issue.

a. HSBC Holdings Group Share Option Plan
HSBC Holdings ordinary shares of US\$0.50

The HSBC Holdings Group Share Option Scheme is a long-term incentive scheme available to certain HSBC employees with grants usually made each year between 2001 and 2004. The Scheme expired on 26 May 2005. No options have been granted under the Plan since that date. Options were granted at market value and are normally exercisable between the third and tenth anniversaries of the date of the grant, subject to vesting conditions. The exercisable date may be advanced in certain circumstances e.g. retirement. The final exercisable dates are from April 2011 to April 2014.

	Banking Group and Branch			
	Audited		Audited	
	31.12.14		31.12.13	
	<i>Weighted</i>		<i>Weighted</i>	
	<i>average</i>	<i>Number of</i>	<i>average</i>	<i>Number</i>
	<i>exercise</i>	<i>options</i>	<i>exercise</i>	<i>of options</i>
	<i>price</i>		<i>price</i>	
Share options at beginning of the period	£7.22	39,023	£6.92	55,424
Share options forfeited during the period		-	£7.22	(459)
Share options exercised during the period		-	£6.28	(9,573)
Share options expired during the period	£7.22	(39,023)	£6.02	(6,369)
Share options outstanding at the end of the period		-	£7.22	<u>39,023</u>
Share options exercisable at the end of the period		-	£7.22	<u>39,023</u>

No options were exercised during 2014. The weighted average share price on the dates on which options were exercised was £6.95 for December 2013.

No options outstanding at 31 December 2014. The options outstanding at 31 December 2013 had an exercise price of £7.22 and a weighted average remaining contractual life of 4 months.

Notes to and forming part of the Financial Statements *(continued)***30. Share options** *(continued)***b. HSBC Holdings Savings-Related Share Option Plan (International)**
HSBC Holdings ordinary shares of US\$0.50

The HSBC Holdings Savings-Related Share Option Plan invites eligible employees to enter into savings contracts to save with the option to use the savings to acquire shares. Options have a vesting period of either 1, 3 or 5 years. The options are exercisable within 3 months following the first anniversary of the commencement of a 1 year savings contract or within 6 months following either the third or the fifth anniversary of the commencement of the 3 year or 5 year savings contract depending on conditions set at the date of grant. There is generally one grant each year (in April or May). The first grant was in 1999.

The subscription to this share option plan had been closed in 2013 and therefore no share option was granted in 2014 (2013: Nil).

	Banking Group and Branch			
	Audited		Audited	
	31.12.14		31.12.13	
	<i>Weighted</i>		<i>Weighted</i>	
	<i>average</i>	<i>Number</i>	<i>average</i>	<i>Number</i>
	<i>exercise</i>	<i>of options</i>	<i>exercise</i>	<i>of options</i>
	<i>price</i>		<i>price</i>	
Share options at beginning of the period	£4.13	54,571	£4.20	88,600
Share options granted during the period		-		-
Share options exercised during the period	£3.73	(14,989)	£4.19	(22,854)
Share options expired during the period	£5.19	(2,123)	£4.48	(5,609)
Share options cancelled during the period	£4.60	(2,581)	£4.83	(3,479)
Share options forfeited during the period		-	£4.46	(741)
Share options transferred in during the period		-	£4.46	672
Share options transferred out during the period	£3.31	(4,529)	£4.46	(2,018)
Share options outstanding at the end of the period	£4.32	30,349	£4.13	54,571
Share options exercisable at the end of the period	£3.54	5,209	£5.46	2,688

The weighted average share price on the dates on which options were exercised was £6.38 for December 2014 (December 2013: £7.12).

The options outstanding at 31 December 2014 have an exercise price in the range of £3.31 to £5.10 (December 2013: £3.31 to £5.46) and a weighted average remaining contractual life of 12 months (December 2013: 19 months).

Notes to and forming part of the Financial Statements *(continued)***30. Share options** *(continued)***c. HSBC Restricted Share Award Scheme**

Awards of Restricted Shares may be made to other senior executives. These awards are typically made to certain employees as part of the Group's bonus deferral policy. Awards of Restricted Shares define the number of shares to which the employee will become entitled, generally between one and three years from the date of the award, and normally subject to the individual remaining in employment.

	Audited 31.12.14 Number of shares	Audited 31.12.13 Number of shares
Shares at beginning of the period	48,004	50,027
New shares granted during the period	22,648	19,556
Additional shares arising from scrip dividends	2,662	2,349
Shares released during the period	(34,218)	(32,302)
Shares forfeited during the period	-	-
Shares transferred in during the period	1,176	8,374
Shares transferred out during the period	(2,783)	-
Shares outstanding at the end of the period	<u>37,489</u>	<u>48,004</u>

The fair value of the share option granted under the HSBC Restricted Share Award Scheme is £6.16 (December 2013: £7.35).

Calculation of fair values

The fair value of services received in return for share options granted are measured by referring to the fair value of share options granted.

Fair values of share options/awards, measured at the date of grant of the option/award, are calculated using a Black-Scholes model.

The fair value of share option/award is based on the share price at the date of the grant. The fair value of share option/award is inherently subjective and uncertain due to the assumptions made and the limitations of the model used.

The fair value of the shares awarded under the HSBC Restricted Share Award Scheme is the market value of the shares at the date of award.

Notes to and forming part of the Financial Statements (continued)

<i>Dollars in Thousands</i>	Banking Group and Branch	
	Audited 31.12.14	Audited 31.12.13

31. Lease commitments**Future rentals in respect of operating leases are:**

Within one year	3,174	3,307
Between one year and two years	3,006	3,013
Between two years and five years	760	3,835
More than five years	-	-
	<u>6,940</u>	<u>10,155</u>

32. Contingent liabilities and other commitments**Contingent liabilities**

Contingent liabilities and commitments are credit-related instruments which include letters of credit, guarantees and commitments to extend credit. The amounts below represent the amount at risk should contracts be fully drawn upon and clients default.

Direct credit substitutes	55,509	53,264
Transaction related contingent items	191,202	252,154
Trade related contingent items	145,726	132,773
Commitments, maturity one year or more	1,039,495	922,668
Commitments, maturity up to one year	702,536	650,657
	<u>2,134,468</u>	<u>2,011,516</u>

Capital commitments

Contracted expenditure	-	80
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The contracted expenditure in 2013 relates to electrical infrastructure.

33. Custodial services, funds management and other fiduciary activities**Custodial services**

The financial statements of the Branch include income in respect of custodial services provided to customers. It is the Branch who contracts with the customers. The securities are held in the name of the Branch's nominee company, HSBC Nominees (New Zealand) Limited. As at 31 December 2014, securities held by the nominee company on behalf of the Branch's customers were excluded from the nominee company and the Branch's Statement of Financial Position. The value of securities held by the nominee company at 31 December 2014 was NZD 61,540 million (December 2013: NZD 52,726 million).

HSBC Nominees (New Zealand) Limited is subject to the standard risks incurred by custodial operations. HSBC Holdings plc holds Banker's Blanket Bond insurance that provides cover for it, and its subsidiary companies in respect of loss of cash and other assets (incurred accidentally or by reason of fraud). Such Banker's Blanket Bond insurance is maintained with limits of cover which vary from time to time but which are considered prudent and in accordance with international levels and insurance market capacity. In addition, securities custody operations are specifically covered by a wrap-around Papers of Value Cover.

Notes to and forming part of the Financial Statements *(continued)***33. Custodial services, funds management and other fiduciary activities** *(continued)***Funds management**

The aggregate value of funds managed by the Banking Group at the end of the reporting period was:

<i>Dollars in Thousands</i>	Banking Group and Branch	
	Audited 31.12.14	Audited 31.12.13
Discretionary funds	-	4,141
Totals funds under management	-	4,141

Discretionary funds are represented by the HSBC Global Unit Trusts, and HSBC World Selection Funds.

The Banking Group has established governance and legal structures to ensure that difficulties arising from custodial and fund management activities would not impact adversely on the Banking Group. The governance and legal structures are detailed within the Statement of Accounting Policies.

34. Marketing and distribution of insurance products

The Branch markets and distributes both life and general insurance products. The life and general insurance products are underwritten by external third party insurance companies. Disclosure statements are made in all marketing material that the products are underwritten by those companies and the Branch does not guarantee the obligations of, or any products issued by, those companies. Such arrangements have been put in place to ensure that difficulties arising from these activities would not impact adversely on the Banking Group.

35. Insurance and non-financial activities

The Banking Group does not conduct any insurance business or non-financial activities in New Zealand. HBAP does not carry on any insurance business or non-financial activities in New Zealand that is outside its banking group.

36. Subsequent event

There was no event subsequent to the balance sheet date which would materially affect the financial statements.

Notes to and forming part of the Financial Statements *(continued)***37. Profitability, size and asset quality of HBAP Group**

<i>Dollars in HK\$ millions</i>	Unaudited 12 months ended 31.12.14	Audited 12 months ended 31.12.13
Profitability		
Net profit after tax	92,177	129,055
Net profit after tax over the previous 12 month period, as a percentage of average total assets	1.4%	2.1%
Size		
Total assets	6,876,746	6,439,355
Percentage increase in total assets over the previous 12 months period	6.8%	6.2%
Asset quality		
Individually impaired assets	14,515	11,795
Individual impairment provision against advances to customers	(6,299)	(5,007)
Collective impairment provision against advances to customers	(4,221)	(4,494)
Individually impaired assets / total assets	0.2%	0.2%
Individual impairment provision / individually impaired assets	43.4%	42.5%

Notes to and forming part of the Financial Statements *(continued)***38. Capital adequacy ratios**

HBAP Group is subject to the capital requirements as specified by the Hong Kong Monetary Authority (HKMA).

HBAP Group uses the advanced internal ratings-based approach to calculate its credit risk for the majority of its non-securitisation exposures and the internal ratings-based (securitisation) approach to determine credit risk for its banking book securitisation exposures. For market risk, HBAP Group uses an internal models approach to calculate its general market risk for the risk categories of interest rate exposures, foreign exchange (including gold) exposures and equity exposures. HBAP Group also uses an internal models approach to calculate its market risk in respect of specific risk for interest rate exposures and equity exposures. HBAP Group uses the standardised (market risk) approach for calculating other market risk positions as well as trading book securitisation exposures, and the standardised (operational risk) approach to calculate its operational risk.

The capital requirements of HKMA are at least equal to those specified under the Basel framework (“Basel III”). HBAP Group exceeds the minimum capital ratio requirements as specified by the HKMA as at 31 December 2014 and 31 December 2013.

The capital adequacy disclosure made by the HBAP Group can be found in the Annual Report and Accounts at this website, <http://www.hsbc.com/investor-relations/financial-and-regulatory-reports>.

HBAP Group reported the following capital adequacy ratios under Basel III, which were the most recent publicly available information:

	Unaudited 31.12.14	Unaudited 31.12.13
Basel III Capital Ratios		
Common Equity Tier 1 (“CET1”) capital	14.4%	14.1%
Tier 1 capital	14.4%	14.1%
Total capital	15.7%	15.2%

The capital ratios for HBAP, as a stand-alone entity, are not publicly available.

Directors' and New Zealand Chief Executive Officer's Statements

Each Director and the New Zealand Chief Executive officer believes, after due enquiry by them, that:

- The Disclosure Statement contains all the information that is required by the Registered Bank Disclosure Statements (Overseas Incorporated Registered Banks) Order 2014 (as amended);
- The Disclosure Statement is not false or misleading;

as at the date on which the Disclosure Statement is signed; and

each Director and the New Zealand Chief Executive officer believes, after due enquiry by them, that:

- the Branch had systems in place to monitor and control adequately the material risks of the Banking Group including credit risk, concentration of credit risk, interest rate risk, currency risk, equity risk, liquidity risk and other business risks, and that those systems were being properly applied; and
- the Registered Bank has complied with all Conditions of Registration that applied;

over the year ended 31 December 2014.

This Disclosure Statement has been signed for and on behalf of the Directors of The Hongkong and Shanghai Banking Corporation Limited (as listed on pages 3 to 5) by their attorney, Noel Gerard McNamara, and also in his capacity as Chief Executive Officer:



Noel Gerard McNamara
Chief Executive Officer
New Zealand Branch

26 March 2015

It is confirmed that the said powers of attorney appointing Noel Gerard McNamara are still in force and have not been revoked.



Independent auditor's report

To the Shareholder of The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch

Report on the Branch and Banking Group Disclosure Statement (excluding the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy)

We have audited the accompanying financial statements and supplementary information (excluding the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy, disclosed in notes 27, 29 and 38) of The Hongkong and Shanghai Banking Corporation Limited – New Zealand Branch (“the Branch”) and its related entities (“the Banking Group”) on pages 12 to 81. The financial statements comprises the statement of financial position as at 31 December 2014, the statements of comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information of the Branch and Banking Group. The supplementary information comprises the information that is required to be disclosed in accordance with Schedules 4, 7, 10, 11 and 13 of the Registered Bank Disclosure Statements (Overseas Incorporated Registered Banks) Order 2014 (as amended) (the “Order”).

Directors' responsibility for the Disclosure Statement

The directors are responsible for the preparation of the Disclosure Statement, including Branch and Banking Group financial statements prepared in accordance with Clause 25 of the Order and generally accepted accounting practice in New Zealand and that give a true and fair view of the matters to which they relate. The directors are also responsible for the preparation and fair presentation of the supplementary information, in accordance with Schedules 2, 4, 7, 9 to 11 and 13 of the Order.

The directors are responsible for such internal controls as they determine is necessary to enable the preparation of a Disclosure Statement that is free from material misstatement whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on the Disclosure Statement, including the financial statements prepared in accordance with Clause 25 of the Order and supplementary information disclosed in accordance with Schedules 4, 7, 10, 11 and 13 of the Order (excluding the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy disclosed in notes 27, 29 and 38, which is covered in the Review opinion on the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy below). We conducted our audit in accordance with International Standards on Auditing (New Zealand). Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the Disclosure Statement is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements and supplementary information (excluding the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy). The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the Disclosure Statement, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the Branch and Banking Group's preparation of the Disclosure Statement that gives a true and fair view of the matters to which it relates in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Branch and Banking Group's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, as well as evaluating the presentation of the Disclosure Statement.

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

Opinion on the financial statements

In our opinion, the financial statements of The Hongkong and Shanghai Banking Corporation Limited – New Zealand Branch and its related entities ("the Branch and Banking Group") on pages 12 to 81:

- comply with generally accepted accounting practice in New Zealand; and
- give a true and fair view of the financial position as at 31 December 2014 and of the financial performance and cash flows for the year ended on that date.

Opinion on supplementary information (excluding supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy)

In our opinion, the supplementary information (excluding supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy) that is required to be disclosed in accordance with Schedules 4, 7, 10, 11 and 13 of the Order, and is included within notes 2, 7, 15, 23, 24, 25, 33, 34, 35 and 37 of the Disclosure Statement:

- has been prepared, in all material respects, in accordance with the guidelines issued pursuant to section 78(3) of the Reserve Bank of New Zealand Act 1989 and any Conditions of Registration;
- is in accordance with the books and records of the Branch and Banking Group; and
- fairly states, in all material respects, the matters to which it relates in accordance with those schedules.

Review Report on the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy

We have completed a review of the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy, as disclosed in notes 27, 29 and 38 of the Disclosure Statement for the year ended 31 December 2014.

Directors' responsibility for the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy

The directors are responsible for the preparation of the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy that is required to be disclosed in accordance with Schedule 9 of the Order and prepared in accordance with the Capital Adequacy Framework (Standardised Approach) (BS2A), and described in notes 27, 29 and 38 of the Disclosure Statement and for such internal control as the directors determine is necessary to enable the preparation of the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy that is free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express a conclusion on the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy disclosed in accordance with Schedule 9 of the Order based on our review. We conducted our review in accordance with NZ SRE 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity* ("NZ SRE 2410"). NZ SRE 2410 requires us to conclude whether anything has come to our attention that causes us to believe that the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy is not, in all material respects:

- prepared in accordance with Capital Adequacy Framework (Standardised Approach) (BS2A); and
- disclosed in accordance with Schedule 9 of the Order.

As the auditor of the Branch and Banking Group, NZ SRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial statements.

A review of the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy in accordance with NZ SRE 2410 is a limited assurance engagement. The auditor performs procedures, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures.

The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with International Standards on Auditing (New Zealand). Accordingly we do not express an audit opinion on the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy disclosures.



Review conclusion on the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy

Based on our review, nothing has come to our attention that causes us to believe that the supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy, disclosed in notes 27, 29 and 38 of the Disclosure Statement, is not in all material respects:

- prepared in accordance with Capital Adequacy Framework (Standardised Approach) (BS2A); and
- disclosed in accordance with Schedule 9 of the Order.

Independence

The New Zealand firm has also provided other services to the Branch and Banking Group in relation to review of the June Disclosure Statement, reporting on custodial services, trust deed reporting and taxation services and other regulatory compliance assurance services. Subject to certain restrictions, partners and employees of our firm may also deal with The Hongkong and Shanghai Banking Corporation Limited (the “Registered Bank”), the Branch and Banking Group on normal terms within the ordinary course of trading activities of the business of the Registered Bank, Branch and Banking Group. There are, however, certain restrictions on dealings which the partners and employees of our firm can have with the Registered Bank, the Branch and Banking Group. These matters have not impaired our independence as auditor of the Branch and Banking Group. The New Zealand firm has no other relationships with, or interest in, the Registered Bank, the Branch and Banking Group.

Report on other legal and regulatory requirements (excluding supplementary information relating to Credit and Market Risk Exposures and Capital Adequacy)

In accordance with the requirements of sections 16(1)(d) and 16(1)(e) of the Financial Reporting Act 1993, and Clauses 2(1)(d) and 2(1)(e) of Schedule 1 of the Order, we report that:

- we have obtained all the information and explanations we have required; and
- in our opinion proper accounting records have been kept by the Branch and Banking Group, as far as appears from our examination of those records.

KPMG

26 March 2015
Auckland

