

**MEVAS BANK LIMITED
DIRECTORS' REPORT AND FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008**

MEVAS Bank Limited
Report of the Directors

The Directors submit their report together with the audited financial statements for the year ended 31 December 2008.

Principal Activities

The principal activities of MEVAS Bank Limited (the "Bank") are the provision of banking and related financial services. The principal activity of the subsidiary is shown in note 22 to the financial statements.

Results and Appropriations

The results of the Bank for the year ended 31 December 2008 are set out in the income statement on page 4.

The Directors declared an interim dividend of HK\$0.75 per share for each of "A" share and "B" share amounting to HK\$30,000,000 which was paid on 31 March 2008.

The Directors do not recommend the payment of a final dividend.

Reserves

Movements in reserves of the Bank during the year are set out in note 31 to the financial statements.

Fixed Assets

Details of the movements in fixed assets of the Bank during the year are shown in note 20 to the financial statements.

DIRECTORS

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

David Shou-Yeh Wong
Chairman

*John William Simpson

*David Richard Hinde

*Robert Tsai-To Sze

Hon-Hing Wong (Derek Wong)

Gary Pak-Ling Wang

Harold Tsu-Hing Wong
Chief Executive

Frederic Suet-Chiu Lau

John Cheung-Wah Lam
Alternate Chief Executive

**Independent Non-executive Directors*

There being no provision in the Bank's Articles of Association for retirement by rotation, all Directors continue in office.

MEVAS Bank Limited

Report of the Directors

Directors' Interests

Pursuant to the Share Option Schemes (the "Schemes") as approved by the shareholders of Dah Sing Financial Holdings Limited ("DSFH") and Dah Sing Banking Group Limited ("DSBG"), the Bank's ultimate and immediate holding companies respectively, certain Directors of the Bank were granted options at a consideration of HK\$1 per option to subscribe for shares of DSFH or DSBG with a par value of HK\$2 and HK\$1 each respectively. The exercise price per share for the options varied by tranches of grant, which was determined in accordance with Rule 17.03(9) of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited being calculated as the higher of (i) the closing price of relevant shares traded on The Stock Exchange of Hong Kong Limited ("SEHK") on the date of grant; and (ii) the average closing price of relevant shares traded on the SEHK for the five trading days immediately preceding the date of the grant. The options can be exercised in varying amounts between the first and sixth anniversaries from the date of grant.

Details of the share options outstanding as at 31 December 2008 which have been granted under the Schemes are as follows:

Director	Held at 1/1/2008	Granted during 2008	Exercised during 2008	Lapsed / cancelled during 2008	Held at 31/12/2008	Exercise price HK\$	Grant date (d/m/y)	Exercise period	
								From (d/m/y)	To (d/m/y)
Number of DSBG share options									
Frederic Suet-Chiu Lau	250,000	-	-	-	250,000	14.40	25/8/2005	25/8/2006	25/8/2011
John Cheung-Wah Lam	250,000	-	-	-	250,000	14.32	30/12/2005	30/12/2006	30/12/2011
Number of DSFH share options									
Hon-Hing Wong (Derek Wong)	1,000,000	-	-	-	1,000,000	51.71	28/8/2005	25/8/2006	25/8/2011
Gary Pak-Ling Wang	400,000	-	-	-	400,000	51.71	25/8/2005	25/8/2006	25/8/2011
Harold Tsu-Hing Wong	250,000	-	-	-	250,000	51.71	25/8/2005	25/8/2006	25/8/2011
	100,000	-	-	-	100,000	61.93	28/9/2007	28/9/2008	28/9/2013

Apart from the above, at no time during the year was the Bank, its subsidiary, its fellow subsidiaries or its holding companies a party to any arrangements to enable the Directors of the Bank or their spouse or children under 18 years of age to acquire benefits by means of the acquisition of shares in, or debentures of, the Bank or any other body corporate.

The Directors do not have any service contracts with the Bank.

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

Management Contracts

Pursuant to a services agreement between the Bank and Dah Sing Bank, Limited ("DSB"), a fellow subsidiary, the Bank has outsourced the management and administration of most of its banking operations, credit risk management, information technology and other support services to DSB at a service fee agreed on an annual basis. This services agreement can be terminated by either party by giving the other party not less than 9 months' written notice.

MEVAS Bank Limited

Report of the Directors

Statement of Compliance

In preparing the financial statements for the year ended 31 December 2008, the Bank has fully complied with the requirements set out in the Banking (Disclosure) Rules issued by the Hong Kong Monetary Authority under section 60A of the Hong Kong Banking Ordinance. The Bank has fully complied with such disclosure requirements.

Auditors

The financial statements have been audited by PricewaterhouseCoopers who retire and, being eligible, offer themselves for re-appointment.

On behalf of the Board

David Shou-Yeh Wong
Chairman

Hong Kong, 20 April 2009

MEVAS Bank Limited**Income Statement****For the year ended 31 December 2008****(Expressed in thousands of Hong Kong dollars)**

	Note	2008	2007
Interest income		232,908	350,229
Interest expense		(146,476)	(251,973)
Net interest income	6	86,432	98,256
Fee and commission income		31,193	34,543
Fee and commission expense		(2,264)	(2,945)
Net fee and commission income	7	28,929	31,598
Net trading income	8	1,273	1,115
Other operating income	9	3,760	3,562
Operating income		120,394	134,531
Operating expenses	10	(94,195)	(67,016)
Operating profit before impairment losses		26,199	67,515
Impairment losses on loans and advances	13	(14,730)	(4,350)
Operating profit before gains or losses on certain investments and fixed assets		11,469	63,165
Net gain on disposal of furniture and equipment		1	-
Net loss from fair value adjustment on investment properties		(8,000)	-
Net gain on disposal of available-for-sale securities		62	1,070
Profit before income tax		3,532	64,235
Income tax expense	14	(547)	(10,788)
Profit attributable to shareholders of the Bank		2,985	53,447
Dividend			
Interim dividend paid		30,000	-

The notes on pages 8 to 66 are an integral part of these financial statements.

MEVAS Bank Limited**Balance Sheet
As at 31 December 2008
(Expressed in thousands of Hong Kong dollars)**

	Note	2008	2007
ASSETS			
Cash and balances with banks	15	4,327,407	4,650,918
Derivative financial instruments	16	2,717	45
Financial assets at fair value through profit or loss	17	82,721	245,949
Advances and other accounts	18,23	1,851,267	2,088,205
Available-for-sale securities	19	11,450	12,037
Furniture and equipment	20	8,384	10,640
Investment properties	21	63,000	-
Current income tax assets		2,607	-
Deferred income tax assets	27	1,847	204
Total assets		6,351,400	7,007,998
LIABILITIES			
Deposits from banks		14,088	37,090
Derivative financial instruments	16	2,733	1,222
Deposits from customers	24	5,747,294	6,114,487
Deposits from customers designated at fair value through profit or loss	25	82,721	345,171
Other accounts and accruals	26	83,363	56,374
Current income tax liabilities		-	5,922
Total liabilities		5,930,199	6,560,266
EQUITY			
Share capital	30	400,000	400,000
Reserves			
Retained earnings	31	20,673	47,688
Investment revaluation reserve	31	528	44
Total equity		421,201	447,732
Total equity and liabilities		6,351,400	7,007,998

Approved and authorised for issue by the Board of Directors on 20 April 2009.

David Shou-Yeh Wong
Director

Frederic Suet-Chiu Lau
Director

Gary Pak-Ling Wang
Director

Harold Tsu-Hing Wong
Chief Executive

The notes on pages 8 to 66 are an integral part of these financial statements.

MEVAS Bank Limited

**Statement of Changes in Equity
For the year ended 31 December 2008
(Expressed in thousands of Hong Kong dollars)**

	<u>Attributable to the shareholders of the Bank</u>			Total equity
	Share capital	Investment revaluation reserve	Retained earnings	
Balance at 1 January 2008	400,000	44	47,688	447,732
Fair value gains on available-for-sale securities	-	650	-	650
Deferred income tax liabilities recognised on fair value gains on available-for-sale securities	-	(104)	-	(104)
Disposal of available-for-sale securities	-	(62)	-	(62)
Net income recognised directly in equity	-	484	-	484
Profit for the year	-	-	2,985	2,985
Total recognised income for 2008	-	484	2,985	3,469
2008 interim dividend	-	-	(30,000)	(30,000)
Balance at 31 December 2008	400,000	528	20,673	421,201

	<u>Attributable to the shareholders of the Bank</u>			Total equity
	Share capital	Investment revaluation reserve	(Accumulated losses)/ Retained earnings	
Balance at 1 January 2007	400,000	693	(5,759)	394,934
Fair value gains on available-for-sale securities	-	421	-	421
Disposal of available-for-sale securities	-	(1,070)	-	(1,070)
Net loss recognised directly in equity	-	(649)	-	(649)
Profit for the year	-	-	53,447	53,447
Total recognised (expense)/income for 2007	-	(649)	53,447	52,798
Balance at 31 December 2007	400,000	44	47,688	447,732

The notes on pages 8 to 66 are an integral part of these financial statements.

MEVAS Bank Limited**Cash Flow Statement****For the year ended 31 December 2008****(Expressed in thousands of Hong Kong dollars)**

	Note	2008	2007
Cash flows from operating activities			
Cash (absorbed by) / generated from operations		(211,032)	57,381
Hong Kong profits tax paid		(10,823)	(1,693)
Net cash flow (used in) / from operating activities	32(a)	<u>(221,855)</u>	<u>55,688</u>
Cash flows from investing activities			
Purchase of investment properties		(71,000)	-
Purchase of furniture and equipment		(656)	(5,119)
Net cash flow used in investing activities		<u>(71,656)</u>	<u>(5,119)</u>
Cash flows from financing activities			
Dividend paid on ordinary shares		(30,000)	-
Net cash flow used in financing activities		<u>(30,000)</u>	<u>-</u>
Net (decrease) / increase in cash and cash equivalents		(323,511)	50,569
Cash and cash equivalents at beginning of the year		<u>4,650,918</u>	<u>4,600,349</u>
Cash and cash equivalents at end of the year	32(b)	<u>4,327,407</u>	<u>4,650,918</u>

The notes on pages 8 to 66 are an integral part of these financial statements.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

1. General information

MEVAS Bank Limited (the "Bank") provides retail and commercial banking and related financial services in Hong Kong.

The Bank is a financial institution incorporated in Hong Kong. The address of its registered office is 36th Floor, Dah Sing Financial Centre, 108 Gloucester Road, Wanchai, Hong Kong.

The ultimate holding company is Dah Sing Financial Holdings Limited, a listed company incorporated in Hong Kong.

These financial statements are presented in thousands of units of Hong Kong dollars (HK\$'000), unless otherwise stated. These financial statements have been approved for issue by the Board of Directors on 20 April 2009.

2. Summary of significant accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

2.1 Basis of preparation

Consolidated financial statements have not been prepared as the Bank is a wholly owned subsidiary of another body corporate, Dah Sing Banking Group Limited. The financial statements of the Bank have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs" is a collective term which includes all applicable individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), accounting principles generally accepted in Hong Kong and the requirements of the Hong Kong Companies Ordinance.

These financial statements have been prepared under the historical cost convention, as modified by the revaluation of investment properties, available-for-sale financial assets and financial assets and financial liabilities (including derivative instruments) at fair value through profit or loss.

The preparation of financial statements in conformity with HKFRSs requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Bank's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Note 4.

(a) Amendments and interpretations to existing standards effective in 2008

- HKAS 39 Financial Instruments: Recognition and Measurement amendment on reclassification of financial assets permits reclassification of certain financial assets out of the held-for-trading and available-for-sale categories if specified conditions are met. The related amendment to HKFRS 7 - Financial Instruments: Disclosures, introduces disclosure requirements with respect to financial assets reclassified out of the held-for-trading and available-for-sale categories. The amendment is effective prospectively from 1 July 2008. The Bank did not make any reclassification of financial assets pursuant to this amendment.
- HK(IFRIC) Int 11 - HKFRS 2 Group and treasury share transactions, provides guidance on whether share-based transactions involving treasury shares or involving group entities (for example, options over a parent's shares) should be accounted for as equity-settled or cash-settled share-based payment transactions in the standalone accounts of the parent and group companies. This interpretation does not have a significant impact on the Bank's financial statements.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

2. Summary of significant accounting policies (Continued)

2.1 Basis of preparation (Continued)

- (b) Interpretations to existing standards effective in 2008 but not relevant to the Bank's operations
- HK(IFRIC) - Int 14 - HKAS 19 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and Their Interaction.
 - HK(IFRIC) - Int 12 Service Concession Arrangements.
- (c) Standards, amendments and interpretations to existing standards that are not yet effective and have either not been early adopted by the Bank

The Bank has chosen not to early adopt the following standards, amendments and interpretations to existing standards that were issued but not yet effective for accounting periods beginning on 1 January 2008:

- HKAS 1 (Revised) - Presentation of Financial Statements (effective from 1 January 2009)
- HKAS 23 (Revised) Borrowing Costs (effective from 1 January 2009).
- HKAS 27 (Revised) Consolidated and Separate Financial Statements (effective from 1 July 2009).
- HKAS 32 (Amendment) - Financial Instruments: Presentation and HKAS 1 (Amendment) - Presentation of Financial Statements - Puttable Financial Instruments and Obligations Arising on Liquidation (effective from 1 January 2009).
- HKFRS 2 (Amendment) - Share-based Payment (effective from 1 January 2009).
- HKFRS 3 (Revised) Business Combinations (effective from 1 July 2009).
- HKFRS 8 Operating Segment (effective from 1 January 2009).
- HK(IFRIC) - Int 13 - Customer Loyalty Programmes Statements (effective from 1 July 2008).
- HKICPA's improvements to HKFRS published in October 2008
 - (1) HKAS 1 (Amendment) - Presentation of Financial Statements (effective from 1 January 2009).
 - (2) HKAS 16 (Amendment) - Property, Plant and Equipment (and consequential amendment to HKAS 7 Statement of Cash Flows) (effective from 1 January 2009).
 - (3) HKAS 19 (Amendment) - Employee Benefits (effective from 1 January 2009).
 - (4) HKAS 20 (Amendment) - Accounting for Government Grants and Disclosure of Government Assistance (effective from 1 January 2009).
 - (5) HKAS 23 (Amendment) - Borrowing Costs (effective from 1 January 2009).
 - (6) HKAS 27 (Amendment) - Consolidated and Separate Financial Statements (effective for annual periods beginning from 1 January 2009).
 - (7) HKAS 28 (Amendment) - Investments in Associates (and consequential amendments to HKAS 32 - Financial Instruments: Presentation and HKFRS 7 - Financial Instruments: Disclosures (effective from 1 January 2009).
 - (8) HKAS 31 (Amendment) - Interests in Joint Ventures (and consequential amendments to HKAS 32 and HKFRS 7) (effective from 1 January 2009).
 - (9) HKAS 36 (Amendment) - Impairment of Assets (effective from 1 January 2009).
 - (10) HKAS 38 (Amendment) - Intangible Assets (effective from 1 January 2009).
 - (11) HKAS 39 (Amendment) - Financial Instruments: Recognition and Measurement (effective from 1 January 2009).
 - (12) HKAS 40 (Amendment) - Investment Property (and consequential amendments to HKAS 16) (effective from 1 January 2009).
 - (13) HKFRS 5 (Amendment) - Non-current Assets Held for Sale and Discontinued Operations (and consequential amendment to HKFRS 1, "First-time adoption") (effective from 1 July 2009).
 - (14) Other minor amendments to HKFRS 7 Financial Instruments: Disclosures, HKAS 8 Accounting Policies, Changes in Accounting Estimates and Errors, HKAS 10 Events after the Reporting Period, HKAS 18 Revenue and HKAS 34 Interim Financial Reporting.

The adoption of the above amendments is not expected to have significant impact on the Bank's financial position.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

2. Summary of significant accounting policies (Continued)

2.1 Basis of preparation (Continued)

- (d) Standards, amendments and interpretations to existing standards that are not yet effective and not relevant to the Bank's operations
- HKFRS 1 (Amendment) - First Time Adoption of HKFRS and HKAS 27 - Consolidated and Separate Financial Statements (effective from 1 January 2009).
 - HK(IFRIC) - Int 15 - Agreements for Construction of Real Estates (effective from 1 January 2009).
 - HK(IFRIC) - Int 16 - Hedges of a Net Investment in a Foreign Operation (effective from 1 October 2008).
 - HKICPA's improvements to HKFRS published in October 2008
 - (1) HKAS 29 (Amendment) - Financial Reporting in Hyperinflationary Economies (effective from 1 January 2009).
 - (2) HKAS 41 (Amendment) - Agriculture (effective from 1 January 2009).
 - (3) Other minor amendments to HKAS 20 Accounting for Government Grants and Disclosure of Government Assistance, HKAS 29 Financial Reporting in Hyperinflationary Economies, HKAS 40 Investment Property and HKAS 41 Agriculture.

2.2 Consolidation

Consolidated financial statements have not been prepared as the Bank is a wholly owned subsidiary of another body corporate, Dah Sing Banking Group Limited.

2.3 Interest income and expenses

Interest income and expense are recognised in the income statement for all instruments measured at amortised cost, available-for-sale securities and certain financial assets/liabilities designated at fair value through profit or loss using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument (for example, prepayment options) but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

2. Summary of significant accounting policies (Continued)

2.4 Fee and commission income and expense

Fees and commissions are generally recognised on an accrual basis when the service has been provided. Loan syndication fees are recognised as revenue when the syndication has been completed and the Bank retained no part of the loan package for itself or retained a part at the same effective interest rate for the other participants. Wealth management, financial planning and custody services that are continuously provided over an extended period of time are recognised rateably over the period the service is provided.

2.5 Financial assets

2.5.1 Classification

The Bank classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables and available-for-sale financial assets. The classification depends on the purpose for which the investments were acquired. Management determines the classification of its investments at initial recognition, except for subsequent reclassification meeting specified definition of relevant asset reclassification.

(a) Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified as held for trading if it is acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives are also categorised as held for trading unless they are designated as hedges. Assets in this category are measured at fair value with all holding gains and loss recognised in the income statement.

A financial asset is typically classified as fair value through profit or loss at inception if it meets the following criteria:

- (i) It eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as “an accounting mis-match”) that would otherwise arise from measuring the financial assets or recognising the gains and losses on them on different bases; or
- (ii) A group of financial assets is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and this is the basis on which information about the assets is provided internally to the key management personnel such as the Board of Directors and Chief Executive Officer; or
- (iii) Financial assets with embedded derivatives where the characteristics and risks of the embedded derivatives are not closely related to the host contracts.

(b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than: (a) those that the Bank intends to sell immediately or in the short term, which are classified as held for trading, and those that the Bank upon initial recognition designates as at fair value through profit or loss; (b) those that the Bank upon initial recognition designates as available-for-sale; or (c) those for which the Bank may not recover substantially all of its initial investment, other than because of credit deterioration. Assets in this category are carried at amortised cost less any impairment loss.

(c) Available-for-sale

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

2. Summary of significant accounting policies (Continued)

2.5 Financial assets (Continued)

2.5.2 Recognition and measurement

Purchases and sales of financial assets are recognised on the trade date – the date on which the Bank commits to purchase or sell the asset. Financial assets are initially recognised at fair value plus transaction costs. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Bank has transferred substantially all risks and rewards of ownership.

Available-for-sale financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables are carried at amortised cost using the effective interest method. Gains or losses arising from changes in the fair value of the “financial assets at fair value through profit or loss” category are included in the income statement in the period in which they arise. Unrealised gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised directly in equity, until the financial asset is derecognised or impaired at which time the cumulative gain or loss previously recognised in equity should be recognised in the income statement. However, interest calculated using the effective interest method is recognised in the income statement. Dividends on available-for-sale equity instruments are recognised in the income statement when the Bank’s right to receive payments is established.

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Bank establishes fair value by using valuation techniques. These include the use of recent arm’s length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, and option pricing models refined to reflect the issuer’s specific circumstances.

2.6 Impairment of financial assets

(a) Assets carried at amortised cost

The Bank assesses at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a ‘loss event’) and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Bank about the following loss events:

- (i) significant financial difficulty of the issuer or obligor;
- (ii) a breach of contract, such as a default or delinquency in interest or principal payments;
- (iii) the Bank granting to the borrower, for economic or legal reasons relating to the borrower’s financial difficulty, a concession that the lender would not otherwise consider;
- (iv) it becoming probable that the borrower will enter into bankruptcy or other financial reorganisation;
- (v) the disappearance of an active market for that financial asset because of financial difficulties; or
- (vi) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:
 - adverse changes in the payment status of borrowers in the group; or
 - national or local economic conditions that correlate with defaults on the assets in the group.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

2. Summary of significant accounting policies (Continued)

2.6 Impairment of financial assets (Continued)

(a) Assets carried at amortised cost (Continued)

The estimated period between a loss occurring and its identification is determined by management for each identified portfolio. In general, the periods used vary between 3 months and 12 months; in exceptional cases, longer periods are warranted.

The Bank first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes that asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Bank may measure impairment on the basis of an instrument's fair value using an observable market price.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e. on the basis of the Bank's grading process that considers asset type, collateral type, overdue status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the group and historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is 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 cash flows for groups of assets should reflect and be directionally consistent with changes in related observable data from period to period (for example, changes in unemployment rates, property prices, payment status, or other factors indicative of changes in the probability of losses in the group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Bank to reduce any differences between loss estimates and actual loss experience.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

2. Summary of significant accounting policies (Continued)

2.6 Impairment of financial assets (Continued)

(a) Assets carried at amortised cost (Continued)

When a loan is uncollectable, it is written off against the related allowances for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

(b) Assets classified as available-for-sale

The Bank assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss measured as the difference between the acquisition cost (net of any principal repayment and amortisation) 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 the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement. 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 the income statement, the impairment loss is reversed through the income statement.

(c) Renegotiated loans

Loans that are either subject to collective impairment assessment or individually significant and whose terms have been renegotiated are no longer considered to be past due but are treated as new loans. In subsequent periods, the asset if past due again is considered to be and disclosed as past due loans.

2.7 Financial liabilities

Financial liabilities are classified into two categories: financial liabilities at fair value through profit or loss and other financial liabilities. All financial liabilities are classified at inception and recognised initially at fair value.

(a) Financial liabilities at fair value through profit or loss

This category has two sub-categories: financial liabilities held for trading, and those designated at fair value through profit or loss at inception.

A financial liability is classified as held for trading if it is incurred principally for the purpose of repurchasing in the short term. It is carried at fair value and any gains and losses from changes in fair value are recognised in the income statement.

A financial liability is typically classified as fair value through profit or loss at inception if it meets the following criteria:

- (i) It eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as "an accounting mis-match") that would otherwise arise from measuring liabilities or recognising the gains and losses on them on different bases; or

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

2. Summary of significant accounting policies (Continued)

2.7 Financial liabilities (Continued)

(a) Financial liabilities at fair value through profit or loss (Continued)

- (ii) A group of financial liabilities is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and this is the basis on which information about the liabilities is provided internally to the key management personnel such as the Board of Directors and Chief Executive Officer; or
- (iii) Financial liabilities with embedded derivatives where the characteristics and risks of the embedded derivatives are not closely related to the host contracts.

Financial liabilities designated at fair value through profit or loss and deposits received from customers that are embedded with certain derivatives, are designated as such at inception or date of transition to the new HKFRS. Financial liabilities designated at fair value through profit or loss are carried at fair value and any gains and losses from changes in fair value are recognised in the income statement.

(b) Other financial liabilities

Other financial liabilities are recognised initially at fair value net of transaction costs incurred and are subsequently carried at amortised cost. Any difference between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period of the other financial liabilities using the effective interest method.

2.8 Derivative financial instruments

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently re-measured at their fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models and options pricing models, as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e. the fair value of the consideration given or received).

Changes in the fair value of derivative instrument are recognised immediately in the income statement under net trading income.

2.9 Offsetting financial instruments

Financial assets and liabilities are offset and the net amount 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.

2.10 Repossessed assets

Loans on which collateral assets have been repossessed are not derecognised and are carried in the balance sheet with appropriate amounts of impairment allowances made.

2.11 Segment reporting

In accordance with the Bank's internal financial reporting policy, the Bank has determined that its segment reporting should be presented based on business segments.

Business segments are distinguishable business divisions of the Bank that provide products and services to customer base or dealing with the market that are different to those of other business segments.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

2. Summary of significant accounting policies (Continued)

2.11 Segment Reporting (Continued)

For the purposes of segment reporting, revenue derived from customers, products and services directly identifiable with individual business are reported directly under respective segment, while revenue and funding cost arising from inter-segment funding operation and funding resources are allocated to the business segments with reference to market interest rates. Transactions within segments are priced based on similar terms offered to or transacted with external parties. Inter-segment income or expenses are eliminated.

All direct costs incurred by different segments are grouped under respective segments. Indirect costs and support functions' costs are allocated to various business segments and products based on effort and time spent as well as segments' operating income depending on the nature of costs incurred. Costs related to corporate activities that cannot be reasonably allocated to business segments, products and support functions are grouped under unallocated items.

2.12 Foreign currency translation

(a) Functional and presentation currency

Items included in the financial statements of the Bank are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The financial statements are presented in HK dollars, which is the Bank's presentation currency and functional currency.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

Translation differences on non-monetary items, such as investment in equity instruments held at fair value through profit or loss, are recognised in the income statement as part of the fair value gain or loss. Translation difference on certain other non-monetary items, such as equities classified as available-for-sale financial assets, are included in the fair value reserve in equity.

2.13 Furniture and equipment

All furniture and equipment are stated at historical cost less depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance are expensed in the income statement during the financial period in which they are incurred.

Depreciation is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives, as follows:

- | | |
|-------------------------------------|--|
| - Furniture, fixtures and equipment | Over the estimated useful lives generally between 5 and 10 years |
|-------------------------------------|--|

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

2. Summary of significant accounting policies (Continued)

2.14 Investment properties

Property that is held for long-term rental yields or for capital appreciation or both, and that is not occupied by the Bank, is classified as investment property.

Investment property comprises land held under operating lease and buildings held under finance lease.

Land held under operating lease is classified and accounted for as investment property when the rest of the definition of investment property is met. The operating lease is accounted for as if it were a finance lease.

Investment property is measured initially at its cost, including related transaction costs.

After initial recognition, investment property is carried at fair value. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset. If this information is not available, the Bank uses alternative valuation methods such as recent prices on less active markets or discounted cash flow projections. These valuations are performed in accordance with the guidance issued by the International Valuation Standards Committee. These valuations are reviewed annually by external valuers. Investment property that is being redeveloped for continuing use as investment property, or for which the market has become less active, continues to be measured at fair value.

The fair value of investment property reflects, among other things, rental income from current leases and assumptions about rental income from future leases in the light of current market conditions.

Subsequent expenditure is charged to the asset's carrying amount only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance costs are expensed in the income statement during the financial period in which they are incurred.

Changes in fair values are recognised in the income statement.

If an investment property becomes owner-occupied, it is reclassified as property, plant and equipment, and its fair value at the date of reclassification becomes its cost for accounting purposes.

If an item of premises and other fixed assets becomes an investment property because its use has changed, any difference resulting between the carrying amount and the fair value of this item at the date of transfer is recognised in equity as a revaluation of premises and other fixed assets under HKAS 16. However, if a fair value gain reverses a previous impairment loss, the gain is recognised in the income statement.

2.15 Current and deferred income tax

The tax expense for the period comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised directly in equity. In this case, the tax is recognised in equity.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the Bank's subsidiaries and associates operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

2. Summary of significant accounting policies (Continued)

2.15 Current and deferred income tax (Continued)

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, if the deferred income tax arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit nor loss, it is not accounted for. Deferred income tax is determined using tax rates that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

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

Income tax payable on profits, based on the applicable tax law, is recognised as an expense in the period in which profits arise. The tax effects of income tax losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

Deferred income tax related to fair value re-measurement of available-for-sale investments, which is charged or credited directly to equity, is also credited or charged directly to equity and is subsequently recognised in the income statement together with the deferred gain or loss.

2.16 Employee benefits

(a) Pension obligations

The Bank offers a mandatory provident fund scheme and a number of defined contribution plans, the assets of which are generally held in separate trustee-administered funds. These pension plans are funded by payments from employees and by the Bank.

The Bank's contributions to the mandatory provident fund schemes and defined contribution retirement schemes are expensed as incurred. Other than mandatory provident fund contribution, the Bank's contributions may be reduced by contributions forfeited by those employees who leave prior to vesting fully in the contributions.

(b) Employee leave entitlements

Employee entitlements to annual leave and long service leave are recognised when they accrue to employees. An accrual is made for the estimated liability for annual leave and long service leave as a result of services rendered by employees up to the balance sheet date.

(c) Bonus plans

Liabilities for bonus plans due wholly within twelve months after the balance sheet date are recognised when the Bank has a present or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made.

2.17 Provisions

Provisions for restructuring costs and legal claims are recognised when: the Bank has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Restructuring provisions comprise lease termination penalties and employee termination payments. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

2. Summary of significant accounting policies (Continued)

2.18 Leases

(a) Operating lease

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are expensed in the income statement on a straight-line basis over the period of the lease.

Where the Bank is a lessor under operating leases, assets leased out are included in fixed assets in the balance sheet. They are depreciated over their expected useful lives on a basis consistent with similar owned fixed assets. Rental income (net of any incentives given to lessees) is recognised on a straight-line basis over the lease term.

(b) Finance lease

Leases of assets where the Bank has substantially retained all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalised at the lease's commencement at the lower of the fair value of the leased property and the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included as liabilities. The investment properties acquired under finance leases are carried at their fair value.

Where the Bank is a lessor under finance leases, the amounts due under the leases, net of unearned finance income, are recognised as a receivable and are included in "Advances and other accounts". Finance income implicit in rentals receivable is credited to the income statement over the lease period so as to produce a constant periodic rate of return on the net investment outstanding for each accounting period.

2.19 Fiduciary activities

The Bank commonly acts as trustees and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, trusts and other institutions. These assets and income arising thereon are excluded from the Bank's financial statements, as they are not assets of the Bank.

2.20 Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds.

Dividends on ordinary shares are recognised as a liability in the Bank's financial statements in the period in which they are approved by the Bank's shareholders.

2.21 Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including: cash, balances with banks and other financial institutions, treasury bills, other eligible bills and certificates of deposit and investment securities which are readily convertible to cash and are subject to an insignificant risk of changes in value.

2.22 Financial guarantee contracts

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Such financial guarantees are given to banks, financial institutions and other bodies on behalf of customers to secure loans, overdrafts and other banking facilities, and to other parties in connection with the performance of customers under obligations related to contracts, advance payments made by other parties, tenders, retentions and the payment of import duties.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

2. Summary of significant accounting policies (Continued)

2.22 Financial guarantee contracts (Continued)

Financial guarantees are initially recognised in the financial statements at fair value on the date the guarantee was given. Subsequent to initial recognition, the Bank's liabilities under such guarantees are measured at the higher of the amount determined in accordance with HKAS 37 Provisions, Contingent Liabilities and Contingent Assets and the amount initially recognised less cumulative amortisation recognised. Any changes in the liability relating to financial guarantees are taken to the income statement.

2.23 Contingent liabilities and contingent assets

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Bank. It can also be a present obligation arising from past events that is not recognised because it is not probable that an outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised but is disclosed in the notes to the financial statements. When a change in the probability of an outflow occurs so that outflow is probable, it will then be recognised as a provision.

A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain events not wholly within the control of the Bank.

A contingent asset is not recognised but is disclosed in the notes to the financial statements when an inflow of economic benefits is probable. When such inflow is virtually certain, an asset is recognised.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management

The Bank's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. Taking risk is core to the financial business, and the operational risks are an inevitable consequence of being in business. The Bank's aim is therefore to achieve an appropriate balance between risk and return and minimise potential adverse effects on the Bank's financial performance.

The Bank's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls, and to monitor the risks and adherence to limits by means of reliable and up-to-date information systems. The Bank regularly reviews its risk management policies and systems to reflect changes in markets, products and emerging best practice.

Risk management is carried out pursuant to the overall strategy and policies approved by the Board of Directors. The Executive Committee under the authority delegated by the Board oversees and guides the management of different risks which are more particularly managed and dealt with by the Bank's risk and different functional committees. In addition, Internal Audit is responsible for the independent review of risk management and the control environment.

The most important types of risk are credit risk, liquidity risk, market risk and operational risk.

3.1 Strategy in using financial instruments

The Bank accepts deposits from customers at both fixed and floating rates, and for various periods, and seeks to earn positive interest margins by investing these funds in high-quality assets. The Bank seeks to increase these margins by consolidating short-term funds and lending for longer periods at higher rates, while maintaining sufficient liquidity to meet all claims that might fall due.

The Bank also seeks to apply its interest margins through its lending to commercial and retail borrowers and to charge customers appropriate fees and commission, taking into consideration credit risk and market conditions. Such exposures involve not just on-balance sheet loans and advances, as the Bank also enters into guarantees and other commitments such as letters of credit performance and other bonds.

Apart from specific hedging arrangements, foreign exchange and interest rate exposures are normally offset by entering into counterbalancing positions (including transactions with customers or market counterparties), or by the use of derivatives thereby controlling the variability in the net cash amounts required to liquidate market positions.

Pursuant to a services agreement entered into between the Bank and Dah Sing Bank, Limited ("DSB"), a fellow subsidiary, the management of risks of the Bank, including the management of different types of financial risks, is outsourced to DSB. The development of risk policies and control, ongoing risk monitoring and management review are carried out by DSB for the Bank with the participation of the Bank's Chief Executive.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk

The Bank's main credit risk is that borrowers or counterparties may default on their payment obligations due to the Bank. These obligations arise from the Bank's lending and investment activities, and trading of financial instruments (including derivatives).

The Bank has a Credit Committee made up of certain Executive Directors and senior credit officers and chaired by the Chief Executive. The Credit Committee has the responsibility for formulating and revising credit policies and procedures within the parameters of the Bank's Risk Policy and regulatory framework. Credit policies and procedures define the credit assessment and approval criteria and guidelines, use of scoring, review and monitoring process and the systems of loan classification and impairment.

The Bank manages all types of credit risk on a prudent basis, in accordance with the credit approval and review policies, by evaluating the credit-worthiness of different types of customers and counterparties based on assessment of business, financial, market and industry risks applicable to the types of loans, collateral and counterparty dealings including dealing in or use of derivative financial instruments. Credits are extended within the parameters set out in the credit policies and are approved by different levels of management based upon established guidelines. Credit exposures, limits and asset quality are regularly monitored and controlled by management, Credit Committee and Group Risk function of the immediate holding company. The Bank's internal auditors conduct regular reviews and audits to ensure compliance with credit policies and procedures and regulatory guidelines.

The Bank's credit policies also establish policies and processes for the approval and review of new products and activities, together with details of the loan grading, or credit scoring, processes and impairment policies.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk (Continued)

3.2.1 Credit risk measurement

(a) Loans and advances

In measuring credit risk of loans and advances to customers and to banks and other financial institutions at a counterparty level, the Bank reflects three components (i) the differentiation of credit risk of the client or counterparty on its contractual obligations; (ii) current exposures to the counterparty and its likely future development, from which the Bank derive the “exposure at default”; and (iii) the likely loss on the defaulted obligations after considering recovery and collateral realisation.

These credit risk measurements, which operate to control and monitor credit performance of individual and pools of borrowers through on-going credit review, loan classification, collection, credit risk mitigation including realisation of collateral, and provision of impairment on problem loans as required by the Bank’s credit policies and procedures, and regulatory guidelines, are embedded in the Bank’s daily operational management. Based on the Banking (Capital) Rules of the Hong Kong Banking Ordinance, the Bank is also required to assess expected loss of individual and portfolios of credits, and to set aside sufficient loan loss reserve against any expected loss. The operational measurements to also cover expected losses can be contrasted with impairment allowances required under HKAS 39, which are based on losses that have been incurred at the balance sheet date (the “incurred loss model”) rather than expected loss (Note 3.2.3).

- (i) The Bank assesses the credit quality of individual counterparties using internal rating tools tailored to the various categories of counterparty. They have been developed internally and combine general analysis and judgements of credit officers, and are reviewed, where appropriate, by comparison with externally available data. Clients of the Bank are segmented into three broad rating classes. The Bank’s rating scale, which is shown in Note 3.2.3, differentiates credit quality for each rating class. This means that, in principle, exposures migrate between classes as the assessment of credit quality and business environment changes. The rating tools are kept under review and upgraded as necessary. The Bank regularly reviews the performance of the rating and their predictive power with regard to default events.

The Bank uses both internal data and market information (e.g. credit rating migration, credit scoring) for internal credit risk assessment. Observed migration data per rating category vary year on year, especially over an economic cycle.

- (ii) Exposure at default is based on the amounts the Bank expects to be owed at the time of default. For example, for a loan, exposure at default is the face value. For a commitment, the Bank includes any amount already drawn plus the further amount that may have been drawn by the time of default, should it occur.
- (iii) Estimated credit loss or loss severity represents the Bank’s expectation of the extent of loss on a claim should default occur. It is based on actual loss experience and typically varies by type of counterparty, type and seniority of claim and availability of collateral or other credit risk mitigation.

(b) Credit-related commitments

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit - which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties - carry the same credit risk as loans.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk (Continued)

3.2.1 Credit risk measurement (Continued)

(b) Credit-related commitments (Continued)

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

(c) Debt securities

For debt securities, external ratings such as Standard & Poor's rating or their equivalents are used by Group Risk for managing the credit risk exposures. The investments in debt securities are made to gain a better credit quality, to diversify risk exposures and income streams, and to maintain a readily available source of funds to meet the funding and liquidity requirement of the Bank from time to time.

(d) Derivatives

The Bank uses the following derivative instruments for trading purposes:

- (i) Currency forwards represent commitments to purchase foreign and domestic currency, including undelivered spot transactions. Foreign currency and interest rate futures are contractual obligations to receive or pay a net amount based on changes in currency rates or interest rates or to buy or sell foreign currency or a financial instrument on a future date at a specified price, established in an organised financial market. The credit risk is negligible, as futures contracts are collateralised by cash or marketable securities, and changes in the futures contract value are settled daily with the exchange.
- (ii) Currency and interest rate swaps are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of currencies or interest rates (for example, fixed rate for floating rate) or a combination of all these (i.e., cross-currency interest rate swaps). No exchange of principal takes place, except for certain currency swaps. The Bank's credit risk represents the potential cost to replace the swap contracts if counterparties fail to perform their obligation. This risk is monitored on an ongoing basis with reference to the current fair value, a proportion of the notional amount of the contracts and the liquidity of the market. To control the level of credit risk taken, the Bank assesses counterparties using the same techniques as for its lending activities.
- (iii) Foreign currency and interest rate options are contractual agreements under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, either to buy (a call option) or sell (a put option) at or by a set date or during a set period, a specific amount of a foreign currency or a financial instrument at a predetermined price. The seller receives a premium from the purchaser in consideration for the assumption of foreign exchange or interest rate risk. Options may be either exchange-traded or negotiated between the Bank and a customer. The Bank is exposed to credit risk on purchased options only, and only to the extent of their carrying amount, which is their fair value.

The Bank may be exposed to counterparty risk arising from its positions in derivative financial instruments, which is either "valuation risk" for the credit risk on receiving mark-to-market gains upon the default of a counterparty prior to scheduled settlement, or "settlement risk" for the possibility of not receiving the expected cash value of a derivative transaction or upon the expiry of a derivative contract on the settlement date.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk (Continued)

3.2.1 Credit risk measurement (Continued)

(d) Derivatives (Continued)

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the balance sheet but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and, therefore, do not indicate the Bank's exposure to credit or price risks. The derivative instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in market interest rates or foreign exchange rates relative to their terms. The aggregate contractual or notional amount of derivative financial instruments on hand, the extent to which instruments are favourable or unfavourable, and thus the aggregate fair values of derivative financial assets and liabilities, can fluctuate significantly from time to time.

The Bank maintains strict control limits on net open derivative positions (i.e., the difference between purchase and sale contracts), by both amount and term. At any one time, the amount subject to credit risk is limited to the current fair value of instruments that are favourable to the Bank (i.e., assets where their fair values are positive), which in relation to derivatives is only a small fraction of the contract, or notional values used to express the volume of instruments outstanding.

3.2.2 Risk limit control and mitigation policies

The Bank manages, controls and limits concentrations of credit risk wherever they are identified - in particular, to individual counterparties and groups, and to industries and countries.

The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored on a revolving basis and are subject to an annual or more frequent review, when considered necessary. Limits on the level of credit risk by product, industry sector and by country are approved by the Credit Committee and Group Risk.

The exposure to any one borrower or counterparty including banks and brokers is further restricted by sub-limits covering on- and off- balance sheet exposures, and daily delivery risk limits in relation to trading items such as forward foreign exchange contracts. Actual exposures against limits are monitored daily.

Exposures to credit risk is also managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by regular review and revision of these limits where appropriate.

To avoid concentration of risk, large exposures to individual customers or related groups are limited to a percentage of the capital base, and exposures to industry sectors and countries/regions are managed within approved limits to achieve a balanced portfolio.

(a) Loans and advances

In order to mitigate the credit risk and where appropriate, the Bank will obtain collateral to support the credit facility. To control credit risk exposure to counterparty arising from derivative positions, the Bank limits its derivative dealings with approved financial institutions, and uses established market practices on credit support and collateral settlement to reduce credit risk exposure to derivative counterparties. Overall credit risk limit for each financial institution counterparty, including valuation limit for derivatives, is approved by the Credit Committee with reference to the financial strength and credit rating of each counterparty. The acceptable types of collateral and their characteristics are established within the credit policies, as are the respective margins of finance.

Irrespective of whether collateral is taken, all credit decisions are based upon the customer's or counterparty's credit profile, cashflow position and ability to repay.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk (Continued)

3.2.2 Risk limit control and mitigation policies (Continued)

(a) Loans and advances (Continued)

The Bank employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for funds advanced, which is a common practice. The Bank implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation. The principal collateral types for loans and advances are:

- Mortgages over residential properties;
- Charges over business assets such as premises, inventory and accounts receivable; and
- Charges over financial instruments such as debt securities and equities.

Longer-term finance and lending to corporate entities are generally secured; revolving individual credit facilities are generally unsecured. In addition, in order to minimise credit loss, the Bank will seek additional collateral from the counterparty as soon as impairment indicators are noticed on relevant individual loans and advances.

(b) Debt securities

Debt securities and treasury bills are generally unsecured, with the exception of asset-backed securities and similar instruments, which are secured by portfolios of financial instruments.

(c) Derivatives

Since all counterparties are financial institutions, the risk is managed as part of the credit risk control and monitoring process in respect of financial institutions including credit controls such as setting individual limit for valuation risk, daily settlement limits and performing periodic credit assessment for each counterparty. Moreover, the Bank requires all derivative contract counterparties to enter into International Swaps and Derivatives Association ("ISDA") Agreement in order to follow the standardised market practice of close-out arrangement in the event of default, settlement procedure, valuation/pricing methods.

Collateral or other security is not usually obtained for credit risk exposures on these instruments, except where the Bank requires margin deposits from counterparties.

The Bank further restricts its exposure to credit losses by entering into master netting arrangements with counterparties with which it undertakes a significant volume of transactions. Master netting arrangements do not generally result in an offset of balance sheet assets and liabilities, as transactions are usually settled on a gross basis. However, the credit risk associated with favourable contracts is reduced by a master netting arrangement to the extent that if an event of default occurs, all amounts with the counterparty are terminated and settled on a net basis.

The Bank's overall exposure to credit risk on derivative instruments subject to master netting arrangements can change substantially within a short period, as it is affected by each transaction subject to the arrangement.

3.2.3 Impairment and provisioning policies

The internal rating system described in Note 3.2.1 focuses more on credit-quality assessment from the inception of the lending and investment activities. In contrast, impairment allowances are recognised for financial reporting purposes only for losses that have been incurred at the balance sheet date based on objective evidence of impairment (see Note 2.6). Due to the different approaches applied, the amount of incurred credit losses provided for in the financial statements may be different from the amount determined from other loss estimation approach that is used for internal operational management and banking regulation purposes.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk (Continued)

3.2.3 Impairment and provisioning policies (Continued)

The impairment allowance shown in the balance sheet at year-end is derived from each of the three broad internal rating grades. However, the majority of the impairment allowance comes from the bottom two gradings. The table below shows the percentage of the Bank's on-balance sheet items relating to loans and advances and the associated impairment allowance covering on- and off-balance sheet amounts for each of these broad internal rating categories.

	2008		2007	
Grades	Loans and advances %	Impairment allowance as a % of loan balance %	Loans and advances %	Impairment allowance as a % of loan balance %
1 - satisfactory	99.4	0.3	99.5	0.3
2 - special mention	0.1	0.8	0.1	0.8
3 - sub-standard or below	0.5	70.2	0.4	46.2
	<u>100.0</u>		<u>100.0</u>	

As far as the commercial banking business of the Bank is concerned, the credit ratings are broadly categorised as follows.

Grade 1 "satisfactory", which covers Grade 1 to 9 of the Bank's internal loan grading system, represents loans for which borrowers are current in meeting commitments and for which the full repayment of interest and principal is not in doubt.

Grade 2 "special mention", which covers Grade 10 of the Bank's internal loan grading system, represents loans with which borrowers are experiencing difficulties and which may lead to credit losses to the Bank if the deterioration in loan quality cannot be contained.

Grade 3 "sub-standard or below", which covers Grade 11 to 13 of the Bank's internal loan grading system, represents loans in which borrowers are displaying a definable weakness that is likely to jeopardise repayment; or collection in full is improbable and the Bank expects to sustain a loss of principal and/or interest, taking into account the fair value of collateral less cost to sell; or loans that are considered uncollectible after all collection options have been exhausted.

The internal rating tool assists management to determine whether objective evidence of impairment exists under HKAS 39, which is based on the following criteria set out by the Bank:

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower (e.g. equity to debt ratio, net income percentage of sales);
- Breach of loan covenants or conditions;
- Initiation of bankruptcy proceedings;
- Deterioration of the borrower's competitive position; and
- Deterioration in the value of collateral.

The Bank's policy requires the review of individual financial assets that are above certain preset thresholds at least annually or more regularly when individual circumstances require. Impairment allowances on individually assessed accounts are determined by an evaluation of the incurred loss at balance sheet date on a case-by-case basis, and are applied to all individually significant accounts. The assessment normally encompasses collateral held (including re-confirmation of its enforceability) and the anticipated receipts on liquidating collaterals for that individual account.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk (Continued)

3.2.3 Impairment and provisioning policies (Continued)

Collectively assessed impairment allowances are provided for: (i) portfolios of homogenous assets that are individually below certain preset thresholds; and (ii) losses that have been incurred but have not yet been identified, by using the available historical experience, experienced judgement and statistical techniques.

3.2.4 Maximum exposure to credit risk before collateral held or other credit enhancements

	2008	2007
Credit risk exposures relating to on-balance sheet assets are as follows:		
Cash and balances with banks	4,327,407	4,650,918
Derivative financial instruments	2,717	45
Financial assets at fair value through profit or loss	82,721	245,949
Loans and advances to customers		
Loans to individuals:		
- Credit cards	330,921	296,806
- Mortgages	778,211	792,396
- Others	226,272	235,125
Loans to corporate entities:		
- Term loans	509,917	732,252
Other assets	18,046	31,626
Available-for-sale securities		
- Debt securities	325	325
	<u>6,276,537</u>	<u>6,985,442</u>
Credit risk exposures relating to off-balance sheet items are as follows:		
Financial guarantees and other credit related contingent liabilities	269	269
Loan commitments and other credit related commitments	2,443,558	2,265,611
	<u>2,443,827</u>	<u>2,265,880</u>
At 31 December	<u>8,720,364</u>	<u>9,251,322</u>

The above table represents a worse case scenario of credit risk exposure to the Bank at 31 December 2008 and 2007, without taking into account of any collateral held or other credit enhancements attached.

The results of credit performance of the Bank can be further assessed with reference to the following:

- 3% of the loans and advances portfolio is categorised in the top three grades of the internal rating system (2007: 10%);
- Mortgage loans, which represent the biggest group in the portfolio, are backed by collateral;
- 98% of the loans and advances portfolio are considered to be neither past due nor individually impaired (2007: 98%).

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk (Continued)

3.2.5 Loans and advances

Loans and advances are summarised as follows:

	2008	2007
Loans and advances to customers		
Neither past due nor impaired	1,813,535	2,022,139
Past due but not impaired (Note (a))	30,004	32,029
Past due and collectively assessed as impaired	1,782	2,411
Gross	<u>1,845,321</u>	<u>2,056,579</u>
Less: allowance for collective impairment	<u>(12,100)</u>	<u>(8,606)</u>
Net	<u>1,833,221</u>	<u>2,047,973</u>
Impairment allowances made in respect of loans collectively assessed as impaired (Note (b))	<u>1,782</u>	<u>2,411</u>
Impaired loans and advances as a % of total loans and advances to customers	<u>0.10%</u>	<u>0.12%</u>

Note:

- (a) The Bank did not have any individually impaired loans and advances as at 31 December 2008 and 31 December 2007.
- (b) Collectively impaired loans and advances refer to those unsecured loans and advances assessed for impairment on a collectively basis and which have become overdue for more than 90 days as at the reporting date. The collective impairment allowance for these impaired loans, which is a part of the overall collective impairment allowances, is shown above

The total collective impairment allowance for loans and advances is HK\$12,100,000 (2007: HK\$8,606,000). Further information on the impairment allowance for loans and advances to customers is provided in Note 18.

During the year ended 31 December 2008, the Bank's total loans and advances decreased by 10%. When entering into new markets or expanding business focus or allocation to different loan segments, the Bank undertakes proper risk assessment in accordance with credit policies and procedures, review and approval of new risk limits, financial and credit reviews with an emphasis on proper risk and return balance. In order to minimise the potential increase of credit risk exposure, the Bank focused more on the business with large corporate enterprises or banks with good credit rating or retail customers providing sufficient collateral.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk (Continued)

3.2.5 Loans and advances (Continued)

(a) Loans and advances neither past due nor impaired

The credit quality of the portfolio of loans and advances that were neither past due nor impaired can be assessed by reference to the internal rating system adopted by the Bank.

At 31 December 2008

	Individual (retail customers)			Corporate entities	Total loans and advances to customers
	Credit cards	Mortgages	Others	Term loans	
Grades:					
1 - satisfactory	324,491	767,751	211,246	509,917	1,813,405
2 - special mention	-	-	-	-	-
3 - sub-standard or below	130	-	-	-	130
Total	324,621	767,751	211,246	509,917	1,813,535

At 31 December 2007

	Individual (retail customers)			Corporate entities	Total loans and advances to customers
	Credit cards	Mortgages	Others	Term loans	
Grades:					
1 - satisfactory	287,815	774,140	227,871	732,252	2,022,078
2 - special mention	-	-	-	-	-
3 - sub-standard or below	61	-	-	-	61
Total	287,876	774,140	227,871	732,252	2,022,139

Mortgage loans in the sub-standard or below class were assessed as not impaired after taking into consideration the value and recoverability of collaterals.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk (Continued)

3.2.5 Loans and advances (Continued)

(b) Past due loans and advances

At 31 December 2008

	Individual (retail customers)			Total loans and advances to customers
	Credit cards	Mortgages	Others	
Past due up to 1 month	2,957	7,894	12,536	23,387
Past due more than 1 month and up to 3 months	2,090	2,566	1,961	6,617
Past due more than 3 months and up to 6 months	1,253	-	529	1,782
Past due more than 6 months	-	-	-	-
Total	6,300	10,460	15,026	31,786
Fair value of collaterals*	-	10,460	-	10,460

At 31 December 2007

	Individual (retail customers)			Total loans and advances to customers
	Credit cards	Mortgages	Others	
Past due up to 1 month	3,771	15,596	5,967	25,334
Past due more than 1 month and up to 3 months	2,984	-	1,051	4,035
Past due more than 3 months and up to 6 months	2,175	-	236	2,411
Past due more than 6 months	-	2,660	-	2,660
Total	8,930	18,256	7,254	34,440
Fair value of collaterals*	-	18,256	-	18,256

* Fair value of collateral is determined as the lower of the market value of collateral and outstanding loan balance.

As at 31 December 2008 and 2007, there were no loans and advances extended to corporate entities that were past due.

Upon initial recognition of loans and advances, the fair value of collateral is based on valuation techniques commonly used for the corresponding assets. In subsequent periods, the fair value is updated with reference to market price or indexes of similar assets.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk (Continued)

3.2.5 Loans and advances (Continued)

(c) Loans and advances overdue for more than 3 months

(i) Gross amount of overdue loans

	2008		2007	
	Gross amount of overdue loans	% of total	Gross amount of overdue loans	% of total
Gross advances to customers which have been overdue for:				
- six months or less but over three months	1,782	0.10	2,411	0.12
- one year or less but over six months	-	-	2,660	0.13
	<u>1,782</u>	<u>0.10</u>	<u>5,071</u>	<u>0.25</u>

(ii) Value of collateral held and impairment allowances against overdue loans and advances

At 31 December 2008

	Outstanding amount of loans and advances	Current market value of collateral	Covered portion by collateral	Uncovered portion by collateral	Other credit risk mitigation	Impairment allowances - individual assessment
Overdue loans and advances to customers	<u>1,782</u>	<u>-</u>	<u>-</u>	<u>1,782</u>	<u>-</u>	<u>-</u>

At 31 December 2007

	Outstanding amount of loans and advances	Current market value of collateral	Covered portion by collateral	Uncovered portion by collateral	Other credit risk mitigation	Impairment allowances - individual assessment
Overdue loans and advances to customers	<u>5,071</u>	<u>2,660</u>	<u>2,660</u>	<u>2,411</u>	<u>-</u>	<u>-</u>

Collateral held against such loans mainly include mortgages over properties.

(d) Rescheduled advances net of amounts included in advances overdue for more than 3 months

	2008	% of total	2007	% of total
Advances to customers	<u>4,434</u>	<u>0.24</u>	<u>860</u>	<u>0.04</u>

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk (Continued)

3.2.6 Repossessed collateral

As at 31 December 2008 and 31 December 2007, the Bank did not hold any repossessed collateral.

3.2.7 Debt securities

The table below presents an analysis of debt securities by rating agency designation at 31 December 2008.

At 31 December 2008

	Available-for-sale investments	Designated at fair value	Total
Rated at or higher than BBB+	-	82,721	82,721
Unrated	325	-	325
Total	325	82,721	83,046

At 31 December 2007

	Available-for-sale investments	Designated at fair value	Total
Rated at or higher than BBB+	-	245,949	245,949
Unrated	325	-	325
Total	325	245,949	246,274

There were no overdue debt securities in the year (2007: Nil).

3.2.8 Concentration of risks of financial assets with credit risk exposure

(a) Geographical sectors

Advances to customers by geographical area are classified according to the location of the counterparties after taking into account the transfer of risk. In general, risk transfer applies when an advance is guaranteed by a party located in an area which is different from that of the counterparty.

The following table analyses gross advances to customers and overdue loans by geographical area

	As at 31 Dec 2008	As at 31 Dec 2007
Gross advances to customers		
- Hong Kong	1,504,420	1,687,383
- China	75,000	76,135
- Others	265,901	293,061
	1,845,321	2,056,579
Gross advances overdue for over 3 months		
- Hong Kong	1,782	5,071

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk (Continued)

3.2.8 Concentration of risks of financial assets with credit risk exposure (Continued)

(a) Geographical sectors (Continued)

The following table analyses the cross-border claims of the Bank in relation to loans and advances, investments in securities, and balances and placements with banks.

As at 31 December 2008	Banks	Others	Total
Asia Pacific excluding Hong Kong	123,427	215,519	338,946
North and South America	557	2,007	2,564
Caribbean	-	127,416	127,416
Europe	349,560	-	349,560
	<u>473,544</u>	<u>344,942</u>	<u>818,486</u>

As at 31 December 2007	Banks	Others	Total
Asia Pacific excluding Hong Kong	1,569	215,063	216,632
North and South America	4,562	4,844	9,406
Caribbean	-	151,293	151,293
	<u>6,131</u>	<u>371,200</u>	<u>377,331</u>

The above information of cross-border claims discloses exposures to foreign counterparties on which the ultimate risk lies, and is derived according to the location of the counterparties after taking into account any transfer of risk. In general, transfer of risk from one country to another is recognised if the claims against a counterparty are guaranteed by another party in a different country or if the claims are on an overseas branch of a bank whose head office is located in a different country. Only regions constituting 10% or more of the aggregate cross-border claims are disclosed.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.2 Credit risk (Continued)

3.2.8 Concentration of risks of financial assets with credit risk exposure (Continued)

(b) Industry sectors

Gross advances to customers by industry sector classified according to the usage of loans

	2008	2007
Loans for use in Hong Kong		
Industrial, commercial and financial		
- Property investment	81,270	75,326
- Financial concerns	30,303	67,562
- Stockbrokers	4,400	22,000
- Wholesale and retail trade	-	3,519
- Manufacturing	26,641	66,691
- Transport and transport equipment	89,454	122,365
- Recreational activities	-	50,030
	<u>232,068</u>	<u>407,493</u>
Individuals		
-Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	25,820	22,655
- Loans for the purchase of other residential properties	535,716	583,720
- Credit card advances	330,921	296,806
- Others	361,678	342,301
	<u>1,254,135</u>	<u>1,245,482</u>
Loans for use in Hong Kong	1,486,203	1,652,975
Loans for use outside Hong Kong (Note)	359,118	403,604
	<u>1,845,321</u>	<u>2,056,579</u>

Note: Loans for use outside Hong Kong include loans extended to customers located in Hong Kong with the finance used outside Hong Kong.

3.3 Market risk

Market risk is the risk of losses in assets, liabilities and off-balance sheet positions arising from movements in market rates and prices. Market risk includes currency risk, interest rate and other price risk. Generally, the Bank's market risk is associated with its positions in foreign exchange, debt securities, equity securities and derivatives in the trading book.

Market risk exposure for different types of transactions is managed within risk limits and guidelines approved by the Board, Executive Committee ("EXCO"), Asset and Liability Management Committee ("ALCO") and Treasury Risk Committee ("TRC"). The overall risk limits comprise sub-limits for each of the different risk categories which are interest rate and foreign exchange.

3.3.1 Market risk arising from trading book

The Bank has very limited foreign exchange exposures, as such exposures are normally offset against other transactions with the market. The Bank does not engage in trading of any on-balance sheet or off-balance sheet financial instruments. The Bank considers that its business and activities in the trading book do not give rise to any material market risk.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.3 Market risk (Continued)

3.3.2 Market risk arising from the banking book

In the Bank's banking book, market risk is predominantly associated with positions in debt and equity securities.

(a) Market risk measurement technique

Within the risk management framework and policies established by the Board, EXCO and TRC, various management action triggers ("MATs") are established to provide early alert to management on the different levels of exposures of the Bank's banking book activities to foreign exchange risk, interest rate risk, and liquidity risk. Sensitivity analysis and stress testing covering shocks and shifts in interest rates on the Bank's on- and off- balance sheet positions, liquidity drift under institution-specific and general market crisis scenarios are regularly performed to gauge and forecast the market risk inherent in the Bank's banking book portfolios against these MATs.

(b) Sensitivity analysis of non-trading portfolio

(i) Foreign exchange risk

The Bank has limited net foreign exchange exposure (except for USD) as foreign exchange positions and foreign currency balances arising from customer transactions are normally matched against other customer transactions or transactions with the market. The net exposure positions, both by individual currency and in aggregate, are managed by the Treasury of the Bank on a daily basis within established foreign exchange limits.

Long-term foreign currency funding, to the extent that this is used to fund Hong Kong dollar assets, is normally matched using forward exchange forward contracts to reduce exposure to foreign exchange risk.

At 31 December 2008, if HK\$ had weakened by 1% against US\$ with all other variable held constant, the profit after taxation for the year would have been HK\$59,000 lower (2007: HK\$11,000 lower), mainly as a result of foreign exchange losses on translation of US\$ denominated financial liabilities compensated by foreign exchange gains on translation of US\$ denominated financial assets.

Conversely, if HK\$ had strengthened by 1% against US\$ with all other variables held constant, profit after taxation for the year would have been HK\$59,000 higher (2007: HK\$11,000 higher).

(ii) Interest rate risk

The Bank's interest rate risk mainly arises from the funding of fixed-rate loans and investments in fixed income securities by floating rate deposits. When interest rates rise or fall, the interest spread and net interest income will be affected as interest income generated by the existing fixed-rate loans or securities will not change. In addition to changes in earnings, the variations in market interest rates will also affect the economic values of the Bank's assets, liabilities and off-balance sheet positions, which can, in turn affect the net worth of the Bank. The Board sets limit on the level of mismatch of interest rate repricing that may be undertaken, which is monitored monthly by the Risk Management and Control Department.

At 31 December 2008, if HK\$ market interest rates had been 200 basis points higher and US\$ market interest rates had been 200 basis points higher with other variables held constant, profit after taxation over the next 12 months and economic value would have been HK\$11,000,000 higher (2007: HK\$7,000,000 higher) and HK\$3,000,000 higher (2007: HK\$2,000,000 lower) respectively.

The method and assumptions used in the above sensitivity analysis on foreign exchange and interest rate risk are on the same basis for both 2008 and 2007.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.3 Market risk (Continued)

3.3.2 Market risk arising from the banking book (Continued)

(b) Sensitivity analysis of non-trading portfolio (Continued)

In addition to foreign exchange risk and interest rate risk, the Bank's investments in debt securities are also exposed to other price risks. Consequently, the value of such investments could change significantly depending on a variety of factors including liquidity risk, market sentiment and other events that might affect individual or portfolios of exposures.

3.3.3 Currency risk

The table below summarises the Bank's financial assets and liabilities translated into equivalent HK dollar, categorised by currency.

Concentration of currency risk - on and off-balance sheet financial instruments

	HKD	USD	Others	Total
As at 31 December 2008				
Assets				
Cash and balances with banks	2,883,446	1,043,996	399,965	4,327,407
Derivative financial instruments	2,709	8	-	2,717
Financial assets at fair value through profit or loss	74,274	8,447	-	82,721
Advances and other accounts	1,689,762	161,275	230	1,851,267
Available-for-sale securities	9,443	2,007	-	11,450
Total financial assets	4,659,634	1,215,733	400,195	6,275,562
Liabilities				
Deposits from banks	14,082	-	6	14,088
Derivative financial instruments	2,725	8	-	2,733
Deposits from customers	4,142,012	1,207,058	398,224	5,747,294
Deposits from customers designated at fair value through profit or loss	74,274	8,447	-	82,721
Other accounts and accruals	74,564	6,316	2,483	83,363
Total financial liabilities	4,307,657	1,221,829	400,713	5,930,199
Net on-balance sheet positions	351,977	(6,096)	(518)	345,363
Off-balance sheet net notional positions *	(1,415)	1,938	(530)	(7)
Credit commitments	2,429,847	13,980	-	2,443,827

* Off-balance sheet net notional positions represent the net notional amounts of foreign currency derivative financial instruments which are principally used to reduce the Bank's exposure to currency movements.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.3 Market risk (Continued)

3.3.3 Currency risk (Continued)

Concentration of currency risk - on and off-balance sheet financial instruments (Continued)

	HKD	USD	Others	Total
As at 31 December 2007				
Assets				
Cash and balances with banks	3,891,715	417,607	341,596	4,650,918
Derivative financial instruments	7	10	28	45
Financial assets at fair value through profit or loss	185,161	60,788	-	245,949
Advances and other accounts	1,871,448	214,914	1,843	2,088,205
Available-for-sale securities	9,446	2,591	-	12,037
Total financial assets	5,957,777	695,910	343,467	6,997,154
Liabilities				
Deposits from banks	37,090	-	-	37,090
Derivative financial instruments	1,214	8	-	1,222
Deposits from customers	5,146,372	628,701	339,414	6,114,487
Deposits from customers designated at fair value through profit or loss	284,383	60,788	-	345,171
Other accounts and accruals	50,855	3,868	1,651	56,374
Total financial liabilities	5,519,914	693,365	341,065	6,554,344
Net on-balance sheet positions	437,863	2,545	2,402	442,810
Off-balance sheet net notional positions *	1,153	(260)	(891)	2
Credit commitments	2,261,887	3,993	-	2,265,880

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.3 Market risk (Continued)

3.3.4 Interest rate risk

The table below summarises the Bank's exposure to interest rate risks. Included in the table are the Bank's financial assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

At 31 December 2008	3 months or less	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	Non- interest bearing	Total
Assets						
Cash and balances with banks	4,244,313	-	-	-	83,094	4,327,407
Derivative financial instruments	-	-	-	-	2,717	2,717
Financial assets at fair value through profit or loss	40,423	42,298	-	-	-	82,721
Advances and other accounts	1,568,802	184,048	87,028	1,259	10,130	1,851,267
Available-for-sale securities	-	-	-	-	11,450	11,450
Total financial assets	5,853,538	226,346	87,028	1,259	107,391	6,275,562
Liabilities						
Deposits from banks	-	-	-	-	14,088	14,088
Derivative financial instruments	-	-	-	-	2,733	2,733
Deposits from customers	5,269,468	427,880	44,306	-	5,640	5,747,294
Deposits from customers designated at fair value through profit or loss	40,423	42,298	-	-	-	82,721
Other accounts and accruals	-	-	-	-	83,363	83,363
Total financial liabilities	5,309,891	470,178	44,306	-	105,824	5,930,199
Total interest sensitivity gap (unadjusted)*	543,647	(243,832)	42,722	1,259	1,567	345,363
Effect of interest rate derivative contracts	-	-	-	-	-	-
Total interest sensitivity gap (adjusted)*	543,647	(243,832)	42,722	1,259	1,567	345,363

* Unadjusted interest sensitivity gap is determined based on positions of on-balance sheet assets and liabilities. Adjusted interest sensitivity gap takes into account the effect of interest rate derivative contracts entered into to mitigate interest rate risk.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.3 Market risk (Continued)

3.3.4 Interest rate risk (Continued)

	3 months or less	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	Non- interest bearing	Total
At 31 December 2007						
Assets						
Cash and balances with banks	4,530,463	-	-	-	120,455	4,650,918
Derivative financial instruments	-	-	-	-	45	45
Financial assets at fair value through profit or loss	90,067	103,833	52,049	-	-	245,949
Advances and other accounts	1,689,050	289,205	77,083	1,241	31,626	2,088,205
Available-for-sale securities	-	-	-	-	12,037	12,037
Total financial assets	6,309,580	393,038	129,132	1,241	164,163	6,997,154
Liabilities						
Deposits from banks	-	-	-	-	37,090	37,090
Derivative financial instruments	-	-	-	-	1,222	1,222
Deposits from customers	5,936,348	170,962	452	-	6,725	6,114,487
Deposits from customers designated at fair value through profit or loss	153,968	129,506	61,697	-	-	345,171
Other accounts and accruals	-	-	-	-	56,374	56,374
Total financial liabilities	6,090,316	300,468	62,149	-	101,411	6,554,344
Total interest sensitivity gap (unadjusted)*	219,264	92,570	66,983	1,241	62,752	442,810
Effect of interest rate derivative contracts	(35,350)	25,700	9,650	-	-	-
Total interest sensitivity gap (adjusted)*	183,914	118,270	76,633	1,241	62,752	442,810

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.4 Liquidity risk

Liquidity risk is the risk that the Bank is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfill commitments to lend.

3.4.1 Liquidity risk management process

The Bank manages its liquidity on a prudent basis to ensure that a sufficiently high liquidity ratio relative to the statutory minimum is maintained throughout the year. The average liquidity ratio of the Bank during the period was well above the 25% minimum ratio set by the Hong Kong Banking Ordinance.

Asset and Liability Management Committee ("ALCO") of the Bank's immediate holding company, Dah Sing Banking Group Limited, regularly reviews the Bank's current loan and deposit mix and changes, funding requirements and projections, and monitors the liquidity ratio and maturity mismatch on an ongoing basis. Appropriate limits on liquidity ratio and maturity mismatch are set and sufficient liquid assets are held to ensure that the Bank can meet all short-term funding requirements.

The Bank's funding comprises mainly deposits of customers. Short-term interbank deposits are taken on a limited basis and the Bank is a net lender to the interbank market.

Monitoring and reporting take the form of cash flow measurement and projections for the next day, week and month respectively, as these are key periods for liquidity management. The starting point for those projections is an analysis of the contractual maturity of the financial liabilities and the expected collection date of the financial assets.

ALCO also monitors unmatched medium-term assets, the level and type of undrawn lending commitments, the usage of overdraft facilities and the impact of contingent liabilities such as standby letters of credit and guarantees.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.4 Liquidity risk (Continued)

3.4.2 Maturity analysis

The table below analyses the Bank's assets and liabilities into relevant maturity groupings based on the remaining period at balance sheet date to the contractual maturity date or, where applicable, the earliest callable date.

At 31 December 2008

	Repayable on demand	Up to 1 month	3 months or less but over 1 month	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	Indefinite	Total
Assets								
Cash and balances with banks	83,094	4,244,313	-	-	-	-	-	4,327,407
Derivative financial instruments	-	2	1	2	2,712	-	-	2,717
Financial assets at fair value through profit or loss	-	30,487	9,935	42,299	-	-	-	82,721
Advances and other accounts	391,557	21,878	28,829	114,645	724,382	568,960	1,016	1,851,267
Available-for-sale securities	-	-	-	-	-	-	11,450	11,450
Furniture and equipment	-	-	-	-	-	-	8,384	8,384
Investment properties	-	-	-	-	-	-	63,000	63,000
Current income tax assets	-	-	-	2,607	-	-	-	2,607
Deferred income tax assets	-	-	-	-	1,847	-	-	1,847
Total assets	474,651	4,296,680	38,765	159,553	728,941	568,960	83,850	6,351,400
Liabilities								
Deposit from banks	14,088	-	-	-	-	-	-	14,088
Derivative financial instruments	-	9	1	2	2,721	-	-	2,733
Deposits from customers	1,022,636	2,408,532	1,889,600	426,075	451	-	-	5,747,294
Deposits from customers designated at fair value through profit or loss	-	30,487	9,935	42,299	-	-	-	82,721
Other accounts and accruals	-	30,709	6,997	32,896	1,401	-	11,360	83,363
Total liabilities	1,036,724	2,469,737	1,906,533	501,272	4,573	-	11,360	5,930,199
Net liquidity gap	(562,073)	1,826,943	(1,867,768)	(341,719)	724,368	568,960	72,490	421,201

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.4 Liquidity risk (Continued)

3.4.2 Maturity analysis (Continued)

At 31 December 2007

	Repayable on demand	Up to 1 month	3 months or less but over 1 month	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	Indefinite	Total
Assets								
Cash and balances with banks	120,455	4,530,463	-	-	-	-	-	4,650,918
Derivative financial instruments	-	45	-	-	-	-	-	45
Financial assets at fair value through profit or loss	-	30,051	60,016	103,833	52,049	-	-	245,949
Advances and other accounts	372,980	36,873	59,006	205,540	763,787	644,761	5,258	2,088,205
Available-for-sale securities	-	-	-	-	-	-	12,037	12,037
Furniture and equipment	-	-	-	-	-	-	10,640	10,640
Deferred income tax assets	-	-	-	204	-	-	-	204
Total assets	493,435	4,597,432	119,022	309,577	815,836	644,761	27,935	7,007,998
Liabilities								
Deposit from banks	37,090	-	-	-	-	-	-	37,090
Derivative financial instruments	-	178	1,044	-	-	-	-	1,222
Deposits from customers	1,390,198	3,377,768	1,175,107	170,962	452	-	-	6,114,487
Deposits from customers designated at fair value through profit or loss	-	51,966	137,323	103,833	52,049	-	-	345,171
Other accounts and accruals	483	35,868	5,862	1,901	1,814	-	10,446	56,374
Current income tax liabilities	-	564	-	5,358	-	-	-	5,922
Total liabilities	1,427,771	3,466,344	1,319,336	282,054	54,315	-	10,446	6,560,266
Net liquidity gap	(934,336)	1,131,088	(1,200,314)	27,523	761,521	644,761	17,489	447,732

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.4 Liquidity risk (Continued)

3.4.2 Maturity analysis (Continued)

In respect of certificates of deposit held for investment purposes and included in financial assets at fair value through profit or loss as at balance sheet date, the applicable balance, analysed based on the remaining period at the balance sheet date to contractual maturity, is shown as follows.

	Repayable on demand	Up to 1 month	3 months or less but over 1 month	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	Undated	Total
As at 31 December 2008								
Certificates of deposit held included in: Financial assets at fair value through profit or loss	<u>-</u>	<u>9,331</u>	<u>9,935</u>	<u>42,299</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>61,565</u>
As at 31 December 2007								
Certificates of deposit held included in: Financial assets at fair value through profit or loss	<u>-</u>	<u>8,998</u>	<u>34,794</u>	<u>98,857</u>	<u>52,049</u>	<u>-</u>	<u>-</u>	<u>194,698</u>

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities are fundamental to the management of the Bank. It is unusual for banks to be completely matched, as businesses transacted are often of uncertain term and of different types. An unmatched position potentially enhances profitability, but also increases the risk of losses.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature are important factors in assessing the liquidity of the Bank and its exposure to changes in interest rates and exchange rates.

The total outstanding contractual amount of commitments to extend credit does not necessarily represent future cash requirements, as many of these commitments will expire or terminate without being funded.

3.4.3 Undiscounted cash flows by contractual maturities

The table below presents the cash flows payable by the Bank under non-derivative financial liabilities, derivative financial liabilities that will be settled on a net basis and derivative financial instruments that will be settled on gross basis by remaining contractual maturities at the balance sheet date. The amounts disclosed in the table are the contractual undiscounted cash flows, whereas the Bank manages the inherent liquidity risk based on expected undiscounted cash inflows.

The Bank's derivatives that normally will be settled on a net basis include:

- Interest rate derivatives: interest rate swaps, over-the-counter (OTC) interest rate options; and
- Foreign exchange derivatives: OTC currency options.

The Bank's derivatives that will be settled on a gross basis include:

- Foreign exchange derivatives: currency forward.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.4 Liquidity risk (Continued)

3.4.3 Undiscounted cash flows by contractual maturities (Continued)

As at 31 December 2008

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Non-derivative cash flow						
Liabilities						
Deposits from banks	14,088	-	-	-	-	14,088
Deposits from customers	3,445,942	1,903,021	435,385	509	-	5,784,857
Deposits from customers designated at fair value through profit or loss	31,645	10,255	42,463	-	-	84,363
Other liabilities	18,212	-	30,000	1,394	-	49,606
Total liabilities (contractual maturity dates)	3,509,887	1,913,276	507,848	1,903	-	5,932,914
Derivative cash flow						
Derivative financial instruments settled on net basis						
	-	-	-	-	-	-
Derivative financial instruments settled on gross basis						
Total outflow	5,559	-	-	-	-	5,559
Total inflow	(5,552)	-	-	-	-	(5,552)
	7	-	-	-	-	7

As at 31 December 2007

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Non-derivative cash flow						
Liabilities						
Deposits from banks	37,090	-	-	-	-	37,090
Deposits from customers	4,787,683	1,185,094	176,536	511	-	6,149,824
Deposits from customers designated at fair value through profit or loss	54,991	144,562	108,356	52,843	-	360,752
Other liabilities	24,254	-	5,154	1,808	-	31,216
Total liabilities (contractual maturity dates)	4,904,018	1,329,656	290,046	55,162	-	6,578,882
Derivative cash flow						
Derivative financial instruments settled on net basis						
	67	-	-	-	-	67
Derivative financial instruments settled on gross basis						
Total outflow	3,576	-	-	-	-	3,576
Total inflow	(3,574)	-	-	-	-	(3,574)
	2	-	-	-	-	2

Assets available to meet all of the liabilities and to cover outstanding loan commitments include cash, central bank balances, items in the course of collection and treasury bills; and loans and advances to customers. In the normal course of business, a proportion of customer loans contractually repayable within one year will be extended.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.4 Liquidity risk (Continued)

3.4.4 Off-balance sheet items

Included in the table below are the following items:

- Loan commitments by reference to the dates of the contractual amounts of the Bank's off-balance sheet financial instruments that commit it to extend credit to customers and other facilities;
- Financial guarantees based on the conditions existing at the reporting date as to what contractual payments are required; and
- The future minimum lease payments under non-cancellable operating leases in respect of operating lease commitments where the Bank is the lessee.

As at 31 December 2008

	No later than 1 year	1-5 years	Total
Loan commitments	2,443,558	-	2,443,558
Guarantees, acceptances and other financial facilities			
- Guarantees and standby letters of credit	269	-	269
Operating lease commitments	7,178	2,946	10,124
Total	<u>2,451,005</u>	<u>2,946</u>	<u>2,453,951</u>

As at 31 December 2007

	No later than 1 year	1-5 years	Total
Loan commitments	2,265,611	-	2,265,611
Guarantees, acceptances and other financial facilities			
- Guarantees and standby letters of credit	269	-	269
Operating lease commitments	8,089	6,278	14,367
Total	<u>2,273,969</u>	<u>6,278</u>	<u>2,280,247</u>

3.5 Fair values of financial assets and liabilities

The fair value of financial instruments traded in active markets (such as publicly traded derivatives, trading and available-for-sale securities) is based on quoted market prices at the balance sheet date. The quoted market price used for financial assets held by the Bank is the current bid price; the appropriate quoted market price for financial liabilities is the current ask price.

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. The Bank uses a variety of methods and makes assumptions that are based on market conditions existing at each balance sheet date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest-rate swaps is calculated as the present value of the estimated future cash flows. The fair value of forward foreign exchange contracts is determined using forward exchange market rates at the balance sheet date.

The fair value of financial assets and financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Bank for similar financial instruments.

(a) Financial instruments measured at fair value using a valuation technique

During 2008 and 2007, there was no financial instrument measured at fair value using a valuation technique which is based on assumptions that are not supported by observable market prices for the same or similar instrument or not based on available observable market data.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.5 Fair values of financial assets and liabilities (Continued)

(b) Financial instruments not measured at fair value

The table below summarises the carrying amounts and fair values of those financial assets and liabilities not presented in the Bank's balance sheet at their fair value.

	Carrying value		Fair value	
	2008	2007	2008	2007
Financial assets				
Cash and balances with banks	4,327,407	4,650,918	4,328,071	4,651,528
Advances and other accounts	1,851,267	2,088,205	1,850,218	2,088,475
Financial liabilities				
Deposits from banks	14,088	37,090	14,088	37,090
Deposits from customers	5,747,294	6,114,487	5,763,211	6,121,925

(i) Placements with banks

The fair value of floating rate placements and overnight deposits is their carrying amount. The estimated fair value of fixed interest bearing deposits is based on discounted cash flows using prevailing money-market interest rates for debts with similar credit risk and remaining maturity.

(ii) Loans and advances to customers

The estimated fair value of loans and advances represents the discounted amount of estimated future cash flows expected to be received. Expected cash flows are discounted at current market rates to determine fair value.

(iii) Deposits from banks and customers

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand. The estimated fair value of fixed interest-bearing deposits not quoted in an active market is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

3.6 Capital management

The Bank's objectives when managing capital are:

- To comply with the capital requirements set by the banking regulator;
- To safeguard the Bank's ability to continue its business as a going concern;
- To maximise returns to shareholders and optimize the benefits to other stakeholders; and
- To maintain a strong capital base to support the development of its business.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

3. Financial risk management (Continued)

3.6 Capital management (Continued)

Capital adequacy of and the use of regulatory capital by the Bank are monitored regularly by the Bank's management, employing techniques based on the guidelines developed by the Basel Committee, as implemented by the Hong Kong Monetary Authority ("HKMA"), for supervisory purposes. The required information is filed with the HKMA on a quarterly basis. The HKMA requires the Bank to maintain a ratio of total regulatory capital to the risk-weighted asset (i.e. the capital adequacy ratio) at or above the internationally agreed minimum of 8%. The Bank's regulatory capital is divided into two tiers:

- Core capital: share capital, profit and loss, and reserves created by appropriations of retained earnings. The book value of goodwill and other intangible assets is deducted in arriving at core capital; and
- Supplementary capital: qualifying perpetual and term subordinated debts, collectively assessed impairment allowances, regulatory reserve, and fair value gains arising on revaluation of holdings of land and buildings and available-for-sale equities and debt securities.

Investment in subsidiaries, significant investments in non-subsidiary companies and shares, exposures to connected companies and investments in other banks' equity are deducted from core and supplementary capital to arrive at the regulatory capital.

Risk-weighted amount is the aggregate of the risk-weighted amounts for credit risk, market risk and operational risk, and covers both on-balance sheet and off-balance sheet exposures. On-balance sheet exposures are classified according to the obligor or the nature of each exposure and risk-weighted based on the credit assessment rating assigned by an external credit assessment institution recognised by the HKMA or other principles as set out in the Banking (Capital) Rules, taking into account the capital effects of credit risk mitigation. Off-balance sheet exposures are converted into credit-equivalent amounts by applying relevant credit conversion factors to each exposure, before being classified and risk-weighted as if they were on-balance sheet exposures.

3.7 Fiduciary activities

The Bank provides custody, trustee, wealth management and advisory services to third parties, which involve the Bank making allocation and purchase and sale decisions in relation to a variety of financial instruments. Those assets that are held in a fiduciary capacity are not included in the Bank's financial statements. These services could give rise to the risk that the Bank will be accused of mal-administration.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

4. Critical accounting estimates, and judgements in applying accounting policies

4.1 Critical accounting estimates and assumptions

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Changes in estimates and assumptions may have a significant impact on the results of the Bank in the periods when changes are made. The application and selection of different estimates and assumptions, and their subsequent changes, could affect the Bank's profit and net asset value in the future. The Bank, based on its high-level assessment of the sensitivity impacts on the reported assets and liabilities of the Bank arising from the changes in critical accounting estimates and assumptions, believes that the estimates and assumptions adopted are appropriate and reasonable, and the financial results and positions presented in the Bank's financial statements are fair and reasonable in all material respects.

Impairment allowances on loans and advances

The Bank reviews its loan portfolios to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the income statement, the Bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when estimating its future cash flows of recoverable amounts. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

4.2 Critical judgments in applying accounting policies

(a) Distinction between investment properties and owner-occupied properties

The Bank determines whether a property qualifies as an investment property. In making its judgment, the Bank considers whether the property generates cash flows largely independently of the other assets held by an entity. Owner-occupied properties generate cash flows that are attributable not only to property but also to other assets used in the production or supply process.

Some properties comprise a portion that is held to earn rentals or for capital appreciation and another portion that is held to supply services or for administrative purposes. If these portions can be sold separately (or leased out separately under a finance lease), the Bank accounts for the portions separately. If the portions cannot be sold separately, the property is accounted for as investment property only if an insignificant portion is held to supply services or for administrative purposes. Judgment is applied in determining whether ancillary services are so significant that a property does not qualify as investment property. The Bank considers each property separately in making its judgment.

(b) Assessment of claims and contingencies

Judgment is needed to determine if provision for compensation to certain customers who had bought structured investments distributed (but not originated or arranged) by the Bank need to be recorded in accordance with the requirements of HKAS 37 "Provisions, Contingent Liabilities and Contingent Assets". In making this judgment, the Bank evaluates the information relating to each or similar cases, and the likelihood and estimated amount of outflow of resources which may be incurred to settle the obligation after considering factors such as recent settlement experiences and advice from legal counsel.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

5. Segment reporting

By business segments

For the year ended 31 December 2008

	Personal Banking	Commercial Banking	Treasury	Unallocated	Elimination	Total
Interest income from:						
- external customers	91,112	24,655	117,141	-	-	232,908
- inter-segments	110,044	-	-	6,681	(116,725)	-
Interest expense to:						
- external customers	(145,616)	-	(860)	-	-	(146,476)
- inter-segments	-	(13,977)	(102,748)	-	116,725	-
Net interest income	55,540	10,678	13,533	6,681	-	86,432
Fee and commission income	30,663	530	-	-	-	31,193
Fee and commission expense	(2,264)	-	-	-	-	(2,264)
Net fee and commission income	28,399	530	-	-	-	28,929
Net trading income	1,273	-	-	-	-	1,273
Other operating income	3,760	-	-	-	-	3,760
Operating income	88,972	11,208	13,533	6,681	-	120,394
Operating expenses	(87,695)	(461)	(1,039)	(5,000)	-	(94,195)
Operating profit before impairment losses	1,277	10,747	12,494	1,681	-	26,199
Impairment losses on loans and advances	(14,730)	-	-	-	-	(14,730)
Operating (loss)/ profit before gains or losses on certain investments and fixed assets	(13,453)	10,747	12,494	1,681	-	11,469
Net gain on disposal of furniture and equipment	-	-	-	1	-	1
Net loss from fair value adjustment on investment properties	-	-	-	(8,000)	-	(8,000)
Net (loss)/gain on disposal of available-for-sale securities	(321)	-	383	-	-	62
(Loss)/profit before income tax	(13,774)	10,747	12,877	(6,318)	-	3,532
As at 31 December 2008						
Total assets	1,426,438	509,342	4,335,341	80,279	-	6,351,400
Total liabilities	5,897,454	-	17,637	15,108	-	5,930,199

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

5. Segment reporting (Continued)

By business segments (Continued)

For the year ended 31 December 2007

	Personal Banking	Commercial Banking	Treasury	Unallocated	Elimination	Total
Interest income from:						
- external customers	102,236	27,627	220,366	-	-	350,229
- inter-segments	226,066	-	-	17,126	(243,192)	-
Interest expense to:						
- external customers	(247,987)	-	(3,986)	-	-	(251,973)
- inter-segments	-	(23,226)	(219,966)	-	243,192	-
Net interest income / (expense)	80,315	4,401	(3,586)	17,126	-	98,256
Fee and commission income	33,685	858	-	-	-	34,543
Fee and commission expense	(2,945)	-	-	-	-	(2,945)
Net fee and commission income	30,740	858	-	-	-	31,598
Net trading income	1,115	-	-	-	-	1,115
Other operating income	3,562	-	-	-	-	3,562
Operating income / (expense)	115,732	5,259	(3,586)	17,126	-	134,531
Operating expenses	(61,123)	(633)	(5,260)	-	-	(67,016)
Operating profit/(loss) before impairment losses	54,609	4,626	(8,846)	17,126	-	67,515
Impairment losses on loans and advances	(4,350)	-	-	-	-	(4,350)
Operating profit/(loss) before gains or losses on certain investments and fixed assets	50,259	4,626	(8,846)	17,126	-	63,165
Net (loss)/gain on disposal of available-for-sale securities	(62)	-	1,132	-	-	1,070
Profit/(loss) before income tax	50,197	4,626	(7,714)	17,126	-	64,235
As at 31 December 2007						
Total assets	1,355,953	732,252	4,663,000	256,793	-	7,007,998
Total liabilities	6,553,122	-	1,222	5,922	-	6,560,266

Personal banking business includes the acceptance of deposits from individual customers and the extension of residential mortgage lending, personal loans, overdraft and credit card services, the provision of insurance sales and investment services.

Commercial banking business includes the provision of finance to commercial, industrial and institutional customers.

Treasury activities are mainly the provision of centralised cash managements for deposit taking and lending.

Unallocated items include results of operations, corporate investments not directly identified under other business divisions.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

6. Net interest income

	2008	2007
Interest income		
Cash and balances with banks	109,765	211,447
Investments in unlisted securities	6,739	7,033
Advances to customers	115,469	129,624
Others	935	2,125
	<u>232,908</u>	<u>350,229</u>
Interest expense		
Deposits from banks / Deposits from customers	<u>146,476</u>	<u>251,973</u>
Included within interest income		
Interest income on financial assets not designated at fair value through profit or loss	<u>226,169</u>	<u>343,204</u>
Included within interest expense		
Interest expense on financial liabilities not designated at fair value through profit or loss	<u>139,002</u>	<u>240,872</u>

7. Net fee and commission income

	2008	2007
Fee and commission income		
Fee and commission income from financial assets and liabilities not designated at fair value through profit or loss		
- Credit related fees and commissions	3,872	5,186
- Credit card	14,129	15,282
Other fee and commission income		
- Securities brokerage and investment services fees	6,517	5,979
- Insurance distribution and related commissions	2,798	3,241
- Retail investment funds and fiduciary services fees and commissions	1,947	3,700
- Other fees	1,930	1,155
	<u>31,193</u>	<u>34,543</u>
Fee and commission expense		
Handling fees and commissions	1,487	2,198
Other fees paid	777	747
	<u>2,264</u>	<u>2,945</u>

8. Net trading income

	2008	2007
Net gain arising from dealing in foreign currencies	<u>1,273</u>	<u>1,115</u>

9. Other operating income

	2008	2007
Dividend income from investments in available-for-sale securities		
- Unlisted investments	1,057	955
Initial fair value recognition of available-for-sale securities	484	2,592
Gross rental income from investment properties	2,050	-
Others	169	15
	<u>3,760</u>	<u>3,562</u>

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

10. Operating expenses

	2008	2007
Employee compensation and benefit expenses (including directors' remuneration) (Note 11)	9,285	10,898
Management fee paid to a fellow subsidiary, Dah Sing Bank, Limited	15,908	16,400
Premises and equipment expense, excluding depreciation		
- Rental of premises	9,632	7,744
- Others	1,994	2,419
Depreciation (Note 20)	1,598	2,154
Advertising costs	9,498	12,447
Auditors' remuneration	573	521
Others	45,707	14,433
	<u>94,195</u>	<u>67,016</u>

11. Employee compensation and benefit expenses

	2008	2007
Salaries and other staff costs	8,906	10,317
Pension costs - defined contribution plans	379	581
	<u>9,285</u>	<u>10,898</u>

Employee benefit expenses included directors' emoluments (Note 12).

12. Directors' emoluments

	2008	2007
Salaries, housing, benefits in kind and other allowances	488	981
Pensions	45	42
	<u>533</u>	<u>1,023</u>

Directors' emoluments represented the attributable emoluments of the Chief Executive borne by the Bank. The Chief Executive of the Bank is an employee of Dah Sing Bank, Limited ("DSB"), a fellow subsidiary. The costs of the Chief Executive were not directly borne by the Bank, but formed part of the annual fee charged to the Bank under the Services Agreement entered into between the Bank and DSB.

The Bank's immediate holding company, Dah Sing Banking Group Limited ("DSBG") and the ultimate holding company, Dah Sing Financial Holdings Limited ("DSFH"), have in place Share Option Schemes (the "Schemes"). Certain directors of the Bank have been granted share options under the Schemes to acquire shares of DSBG or DSFH. None of the share options received by these directors related to services rendered by them in their capacity as directors of the Bank.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

13. Impairment losses on loans and advances

	2008	2007
Net charge of impairment losses on loans and advances		
- Collectively assessed	<u>14,730</u>	<u>4,350</u>
Of which		
- new allowances (including any amount directly written off in the year)	21,066	10,538
- recoveries	<u>(6,336)</u>	<u>(6,188)</u>
Net charge to income statement	<u>14,730</u>	<u>4,350</u>

14. Income tax expense

Hong Kong profits tax has been provided at the rate of 16.5% (2007: 17.5%) on the estimated assessable profit for the year.

	2008	2007
Current income tax	2,294	7,615
Deferred income tax		
- Impact of change of Hong Kong tax rate	12	-
- Origination and reversal of temporary differences	(1,759)	81
- Utilisation of tax losses	-	3,092
Income tax expense	<u>547</u>	<u>10,788</u>

The tax on the Bank's profit before income tax differs from the theoretical amount that would arise using the tax rate applicable to profits of the Bank as follows:

	2008	2007
Profit before income tax	<u>3,532</u>	<u>64,235</u>
Calculated at a taxation rate of 16.5% (2007: 17.5%)	583	11,241
Tax effects of:		
Income not subject to taxation	(255)	(621)
Expenses not deductible for tax purposes	207	168
Remeasurement of deferred tax – change of Hong Kong tax rate	12	-
Income tax expense	<u>547</u>	<u>10,788</u>

15. Cash and balances with banks

	2008	2007
Cash and balances with banks	83,094	120,455
Money at call and short notice	<u>4,244,313</u>	<u>4,530,463</u>
	<u>4,327,407</u>	<u>4,650,918</u>

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

16. Derivative financial instruments

The notional principal amounts of outstanding derivative contracts and their fair values as of 31 December 2008 are as follows:

	Contract/ notional amount	Fair values	
		Assets	Liabilities
Derivatives held for trading			
<i>a) Foreign exchange derivatives</i>			
Currency forwards	5,701	2	(9)
<i>b) Interest rate derivatives</i>			
Interest rate swaps	91,320	1,338	(1,347)
Interest rate options	91,320	1,377	(1,377)
Total recognised derivative financial assets/(liabilities)	188,341	2,717	(2,733)

The notional principal amounts of outstanding derivative contracts and their fair values as of 31 December 2007 are as follows:

	Contract/ notional amount	Fair values	
		Assets	Liabilities
Derivatives held for trading			
<i>a) Foreign exchange derivatives</i>			
Currency forwards	3,577	6	(3)
Currency options purchased and written	14,322	39	(40)
<i>b) Interest rate derivatives</i>			
Interest rate swaps	100,400	-	(1,179)
Total recognised derivative financial assets/(liabilities)	118,299	45	(1,222)

The credit risk weighted amounts of the above off-balance sheet exposures calculated in accordance with Banking (Capital) Rules and without taking into account the effect of bilateral netting arrangements that the Bank entered into, are as follows:

	2008	2007
Derivatives		
Interest rate swaps	1,000	120
Interest rate options	1,596	-
	2,596	120

The above positions taken in financial instruments arose from the execution of trade orders from customers or transactions taken to hedge these positions and funding management of the Bank.

The contract amounts of these instruments indicate the volume of transactions outstanding as at the balance sheet date, they do not represent the amounts at risk.

The credit risk weighted amounts are the amounts that have been calculated with reference to the Banking (Capital) Rules issued by the HKMA. The amounts calculated are dependent upon the status of the counterparty and the maturity characteristics of each type of contract.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

17. Financial assets at fair value through profit or loss

	2008	2007
Debt securities at fair value through profit or loss:		
- unlisted	<u>82,721</u>	<u>245,949</u>
Included within debt securities are:		
- Certificates of deposit held	61,565	194,698
- Other debt securities	<u>21,156</u>	<u>51,251</u>
	<u>82,721</u>	<u>245,949</u>

Financial assets at fair value through profit or loss were securities issued by Dah Sing Bank, Limited (Note 28).

18. Advances and other accounts

(a) Analysis of advances to customers

	2008	2007
Loans and advances to individuals		
- Credit cards	330,921	296,806
- Mortgages	778,211	792,396
- Others	226,272	235,125
Loans and advances to corporate entities		
- Term loans	509,917	732,252
Gross advances to customers	<u>1,845,321</u>	<u>2,056,579</u>
Less: impairment allowances		
- Collectively assessed	(12,100)	(8,606)
Other assets (Note 23)	18,046	40,232
Advances and other accounts	<u>1,851,267</u>	<u>2,088,205</u>

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

18. Advances and other accounts (Continued)

(b) Reconciliation of allowance account for losses on loans and advances to customers

	Impairment allowance - Collective assessment				Total
	Individual (retail customers)			Corporate entities	
	Credit cards	Mortgages	Others	Term loans	
Movement in impairment allowances on loans and advances					
Balance at 1 January 2007	4,771	6,604	2,727	5,078	19,180
Impairment losses charged / (reversed)	12,680	(6,315)	3,063	(5,078)	4,350
Loans written off as uncollectible	(14,509)	-	(6,603)	-	(21,112)
Recoveries of advances written off in previous years	3,215	-	2,973	-	6,188
Balance at 31 December 2007	6,157	289	2,160	-	8,606
Balance at 1 January 2008	6,157	289	2,160	-	8,606
Impairment losses charged / (reversed)	8,579	(259)	5,835	575	14,730
Loans written off as uncollectible	(11,542)	-	(6,030)	-	(17,572)
Recoveries of advances written off in previous years	1,338	-	4,998	-	6,336
Balance at 31 December 2008	4,532	30	6,963	575	12,100

Loans and advances of the Bank are assessed for impairment on a collective basis. The Bank did not have any individually assessed impairment allowances as at 31 December 2008 and 2007.

19. Available-for-sale securities

	2008	2007
Debt securities:		
- unlisted	325	325
Equity securities:		
- listed in Hong Kong	118	121
- unlisted	11,007	11,591
	11,125	11,712
Total available-for-sale securities	11,450	12,037
Available-for-sale securities are analysed by issuers as follows:		
- Corporate entities	11,375	11,962
- Others	75	75
	11,450	12,037

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

20. Furniture and equipment

At 1 January 2007		
Cost		14,485
Accumulated depreciation		<u>(6,810)</u>
Net book amount		<u>7,675</u>
Year ended 31 December 2007		
Opening net book amount		7,675
Additions		5,119
Depreciation charge (Note 10)		<u>(2,154)</u>
Closing net book amount		<u>10,640</u>
At 31 December 2007		
Cost		16,656
Accumulated depreciation		<u>(6,016)</u>
Net book amount		<u>10,640</u>
Year ended 31 December 2008		
Opening net book amount		10,640
Additions		656
Disposals		(1,314)
Depreciation charge (Note 10)		<u>(1,598)</u>
Closing net book amount		<u>8,384</u>
At 31 December 2008		
Cost		15,565
Accumulated depreciation		<u>(7,181)</u>
Net book amount		<u>8,384</u>

21. Investment properties

	2008	2007
At 1 January	-	-
Additions	71,000	-
Fair value losses on revaluation	<u>(8,000)</u>	-
At 31 December	<u>63,000</u>	<u>-</u>

The investment properties were acquired from Dah Sing Bank, Limited, a fellow subsidiary, in June 2008 based on the open market value as at 31 December 2007.

The investment properties were revalued at 31 December 2008. Valuations were made on the basis of open market value by independent, professionally qualified valuer Savills (Valuation and Professional Services) Limited.

The net book value of investment properties comprises:

	2008	2007
Leaseholds		
Held in Hong Kong on medium-term lease (between 10-50 years)	<u>63,000</u>	<u>-</u>

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

22. Investment in a subsidiary

	2008	2007
Investments, at cost		
Unlisted shares	50	50
Amount due to a subsidiary	<u>(50)</u>	<u>(50)</u>
	<u>-</u>	<u>-</u>

The wholly-owned subsidiary at 31 December 2008 and 2007 is as follows:

Name of company	Principal activity	Place of incorporation	Particulars of issued ordinary shares
MEVAS (Nominees) Limited	Nominee services	Hong Kong	500 ordinary shares of HK\$100 each

23. Other assets

	2008	2007
Accrued income	11,828	15,788
Accounts receivable and prepayments	3,702	22,348
Others	<u>2,516</u>	<u>2,096</u>
	<u>18,046</u>	<u>40,232</u>

24. Deposits from customers

	2008	2007
Demand deposits and current accounts	909,120	1,301,186
Savings deposits	113,516	89,012
Time, call and notice deposits	<u>4,724,658</u>	<u>4,724,289</u>
	<u>5,747,294</u>	<u>6,114,487</u>

25. Deposits from customers designated at fair value through profit or loss

	2008	2007
Structured deposits	30,487	193,330
Other deposits from customers designated at fair value through profit or loss	<u>52,234</u>	<u>151,841</u>
	<u>82,721</u>	<u>345,171</u>

During the year, the Bank did not designate on initial recognition any deposits from customers at fair value through profit or loss (2007: deposits from customers totaling HK\$20,750,000 were designated at fair value through profit or loss on initial recognition).

The amount that the Bank would be contractually required to pay at maturity to the holders of these deposits is HK\$99,000 (2007: HK\$8,339,000) higher than the above carrying amount.

MEVAS Bank Limited**Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

26. Other accounts and accruals

	2008	2007
Accruals	25,163	22,188
Others	58,200	34,186
	<u>83,363</u>	<u>56,374</u>

27. Deferred income tax

Deferred income tax assets and liabilities are netted when there is a legally enforceable right to offset current income tax assets against current income tax liabilities and when the deferred income taxes relate to the same fiscal authority. The netted amounts are as follows:

	2008	2007
Deferred income tax assets:		
- Deferred income tax assets to be recovered after more than 12 months	2,821	1,506
Deferred income tax liabilities:		
- Deferred income tax liabilities to be settled after more than 12 months	(974)	(1,302)
	<u>1,847</u>	<u>204</u>

The gross movement on the deferred income tax account is as follows:

	2008	2007
At 1 January	204	3,377
Tax credited/ (charged) to the income statement (Note 14)	1,747	(3,173)
Tax charged to equity	(104)	-
At 31 December	<u>1,847</u>	<u>204</u>

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

27. Deferred income tax (Continued)

The movement in deferred income tax assets and liabilities during the year, without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

Deferred income tax assets:

	Provisions	Unused tax losses	Total
At 1 January 2007	1,151	3,092	4,243
Credited/(charged) to income statement	355	(3,092)	(2,737)
At 31 December 2007 and at 1 January 2008	1,506	-	1,506
Credited to income statement	1,315	-	1,315
At 31 December 2008	2,821	-	2,821

Deferred income tax liabilities:

	Accelerated tax depreciation	Investment revaluation	Total
At 1 January 2007	866	-	866
Charged to income statement	436	-	436
At 31 December 2007 and at 1 January 2008	1,302	-	1,302
Credited to income statement	(432)	-	(432)
Charged to equity	-	104	104
At 31 December 2008	870	104	974

28. Balances with fellow subsidiaries

Included in the following balance sheet captions are balances with fellow subsidiaries detailed as follows:

	2008	2007
Cash and balances with banks	3,781,352	4,578,244
Financial assets at fair value through profit or loss	82,721	245,949
Advances and other accounts	5,940	14,220
Derivative financial instruments	1,344	45
	3,871,357	4,838,458
Deposits from banks	5	-
Deposits from customers	2,161	16,339
Other accounts and accruals	700	2,011
Derivative financial instruments	1,378	1,221
	4,244	19,571

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

29. Contingent liabilities and commitments

(a) Credit commitments

The contract and credit risk weighted amounts of the Bank's off-balance sheet financial instruments that commit it to extend credit to customers are as follows:

	Contract amount	
	2008	2007
Direct credit substitutes	269	269
Commitments that are unconditionally cancellable without prior notice	2,265,225	2,118,164
Other commitments with an original maturity of: - under 1 year	178,333	147,447
	2,443,827	2,265,880

	Credit risk weighted amount	
	2008	2007
Contingent liabilities and commitments	29,478	29,052

(b) Operating lease commitments

Where the Bank is the lessee, the future minimum lease payments under non-cancellable building operating leases are as follows:

	2008	2007
No later than 1 year	7,178	8,089
Later than 1 year and no later than 5 years	2,946	6,278
	10,124	14,367

Where the Bank is the lessor, the future minimum lease payments under non-cancellable building operating leases are as follows:

	2008	2007
No later than 1 year	3,600	-
Later than 1 year and no later than 5 years	5,151	-
	8,751	-

30. Share capital

	2008	2007
Authorised, issued and fully paid: 40,000,000 ordinary shares of HK\$10 each	400,000	400,000

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

31. Reserves

	Investment revaluation reserve	(Accumulated losses)/ Retained earnings	Total
At 1 January 2007	693	(5,759)	(5,066)
Fair value gains on available-for-sale securities	421	-	421
Disposal of available-for-sale securities	(1,070)	-	(1,070)
Profit for the year	-	53,447	53,447
At 31 December 2007 and at 1 January 2008	44	47,688	47,732
Fair value gains on available-for-sale securities	650	-	650
Deferred income tax liabilities recognised on fair value gains on available-for-sale securities	(104)	-	(104)
Disposal of available-for-sale securities	(62)	-	(62)
Profit for the year	-	2,985	2,985
2008 interim dividend	-	(30,000)	(30,000)
At 31 December 2008	528	20,673	21,201

Note: At 31 December 2008, a regulatory reserve amounting to HK\$12,714,000 (2007: HK\$16,798,000) has been earmarked in the retained profits of the Bank. The regulatory reserve is maintained to satisfy the provisions of the Hong Kong Banking Ordinance for prudential supervision purposes. Movements in the regulatory reserve are made directly through retained profits and in consultation with the HKMA.

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

32. Notes to the cash flow statement

(a) Reconciliation of profit before income tax to net cash flow (used in)/ from operating activities

	2008	2007
Profit before income tax	3,532	64,235
Net gain on disposal of furniture and equipment	(1)	-
Net loss from fair value adjustment on investment properties	8,000	-
Net gain on disposal of available-for-sale securities	(62)	(1,070)
Net interest income	(86,432)	(98,256)
Interest received	236,868	349,842
Interest paid	(144,510)	(251,010)
Impairment losses on loans and advances	14,730	4,350
Advances written off net of recoveries	(11,236)	(14,924)
Depreciation	1,598	2,154
Operating profits before changes in operating assets and liabilities	22,487	55,321
Change in financial assets designated at fair value through profit or loss	163,228	11,548
Change in advances and other accounts	229,483	(403,848)
Change in available-for-sale securities	1,237	(838)
Change in deposits from banks	(23,002)	708
Change in derivative financial instruments	(1,161)	(850)
Change in deposits from customers	(367,193)	457,165
Change in deposits from customers designated at fair value through profit or loss	(262,450)	(63,311)
Change in other accounts and accruals	26,339	1,486
Cash (absorbed by) / generated from operating activities	(211,032)	57,381

(b) For the purposes of the cash flow statement, cash and cash equivalents comprise the following balances with less than three months' maturity from the date of acquisition.

	2008	2007
Cash and balances with banks	83,094	120,455
Money at call and short notice	4,244,313	4,530,463
	4,327,407	4,650,918

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

33. Loans to officers

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

	Balance outstanding at 31 December	
	2008	2007
Aggregate amount outstanding in respect of principal and interest	3	3
	Maximum balance during the year	
	2008	2007
Aggregate amount outstanding in respect of principal and interest	3	10

34. Related-party transactions

The Bank's immediate holding company is Dah Sing Banking Group Limited and the ultimate holding company is Dah Sing Financial Holdings Limited. Both holding companies are listed companies incorporated in Hong Kong.

During 2008 and 2007, the Bank entered into various transactions with its fellow subsidiaries on normal commercial terms. These transactions include interbank placements and deposit taking, marketing and distribution of life and general insurance products and the provision of other banking services.

Details of the significant related party transactions are as follows:

(a) Transactions and balances with fellow subsidiaries

Various treasury, operational, administrative and other functions of the Bank are provided by DSB, a fellow subsidiary of the Bank. In addition, the property acquired from DSB in 2008 as shown in Note 21 has been leased back to DSB at market rate.

In 2008, the Bank did not sub-participate in any additional syndicated loans with DSB (2007: syndicated loans with a total principal value of HK\$257 million were sub-participated). DSB is engaged by the Bank to perform loan administration and operation support and processing in respect of its participation in such loans.

(i) Income and expense

	Fellow subsidiaries	
	2008	2007
Interest expense incurred	(44)	(304)
Interest income earned	115,649	218,121
Commission income	1,023	1,597
Service fee incurred	(15,908)	(16,400)
Rental income	2,050	-

MEVAS Bank Limited

Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

34. Related-party transactions (Continued)

(a) Transactions and balances with fellow subsidiaries (Continued)

(ii) Inter-company balances

Inter-company balances with fellow subsidiaries are shown under Note 28.

(iii) Derivative financial instruments - Outstanding notional principal at year-end

Fellow subsidiaries

	2008	2007
Foreign exchange forward contracts	4,686	3,538
Interest rate contracts	<u>91,320</u>	<u>100,400</u>

(b) Key management personnel

(i) Material transactions and balances with directors and key management personnel

During the year, the Bank had banking transactions with the directors and key management personnel of the Bank and its holding companies, including deposit taking, loans, credit card facilities and investment services. These transactions were provided in the ordinary course of business and on the same terms offered to other employees.

Income and expenses arising from the transactions with key management personnel are immaterial and the loans and deposits balances with them as at 31 December are shown below.

	2008	2007
Loans and advances	3	3
Deposits	<u>1,014</u>	<u>1,971</u>

(ii) Remuneration of key management personnel

Key management personnel of the Bank comprise only executive directors and information on their remuneration is described in Note 12 to the financial statements.

(c) Related companies

The Bank has no loans and advances balances and deposits balances with related companies controlled or significantly influenced by Bank's shareholders and directors as at 31 December 2008 and 31 December 2007.

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

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

1. Capital adequacy ratios

	As at 31 Dec 2008	As at 31 Dec 2007
Capital adequacy ratio		
- Core	16.0%	15.4%
- Overall	17.0%	16.3%

The capital adequacy ratio of the Bank is computed in accordance with the Banking (Capital) Rules. This capital adequacy ratio takes into account the capital charge for operational risk.

The Bank has been exempted by the Hong Kong Monetary Authority ("HKMA") to maintain capital against market risk as it met all the relevant criteria specified in the Banking (Capital) Rules.

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

	As at 31 Dec 2008	As at 31 Dec 2007
Core capital:		
Paid up ordinary share capital	400,000	400,000
Reserves	34,974	(5,759)
Profit and loss account	(27,015)	36,649
Less: net deferred tax assets	(1,847)	(204)
	406,112	430,686
Less: 50% of total amount of deductible items	(150)	(150)
Core capital	405,962	430,536
Supplementary capital:		
Reserves attributable to fair value gains on revaluation of holdings of available-for-sale equities and debt securities	237	20
Regulatory reserve	12,714	16,798
Collective impairment allowances for impaired assets	12,100	8,606
	25,051	25,424
Less: 50% of total amount of deductible items	(150)	(150)
Supplementary capital	24,901	25,274
Total capital base	430,863	455,810

In calculating its capital adequacy ratio, the Bank has deducted the cost of investment in the subsidiary, MEVAS Nominees Limited, which is a "regulated financial entity" as defined by the Banking (Capital) Rules, from its capital base.

Consolidated financial statements have not been prepared as the Bank is a wholly owned subsidiary of another body corporate, Dah Sing Banking Group Limited.

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

2. Liquidity ratio

	2008	2007
Liquidity ratio	<u>105.2%</u>	<u>101.9%</u>

The liquidity ratio is calculated as the simple average of each calendar month's average liquidity ratio for the twelve months of the financial year. The liquidity ratio is computed with reference to the methods set out in the Fourth Schedule of the Hong Kong Banking Ordinance.

3. Currency concentrations

The following sets out the Bank's net foreign exchange position in currencies that constitute more than 10% of the total net position in all foreign currencies as at 31 December 2008 and the corresponding comparative balances.

	As at 31 December 2008			
	USD	RMB	AUD	NZD
Equivalent in HK\$'000				
Spot assets	1,215,557	56,135	123,958	131,840
Spot liabilities	(1,222,321)	(54,473)	(124,642)	(132,758)
Forward purchases	2,682	-	175	319
Forward sales	(744)	(1,023)	(142)	(136)
Net (short) / long position	<u>(4,826)</u>	<u>639</u>	<u>(651)</u>	<u>(735)</u>
	As at 31 December 2007			
	USD	RMB	AUD	NZD
Equivalent in HK\$'000				
Spot assets	693,160	33,418	124,615	101,025
Spot liabilities	(690,615)	(32,408)	(124,471)	(100,273)
Forward purchases	39	-	605	520
Forward sales	(299)	-	(630)	(1,083)
Net long position	<u>2,285</u>	<u>1,010</u>	<u>119</u>	<u>189</u>

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

4. Loans and advances to customers

- (a) Gross advances to customers by industry sector classified according to the usage of loans and analysed by percentage covered by collateral

	As at 31 Dec 2008		As at 31 Dec 2007	
	Outstanding balance	% of gross advances covered by collateral	Outstanding balance	% of gross advances covered by collateral
Industrial, commercial and financial				
- Property investment	81,270	100.0	75,326	100.0
- Financial concerns	30,303	-	67,562	-
- Stockbrokers	4,400	-	22,000	-
- Wholesale and retail trade	-	-	3,519	100.0
- Manufacturing	26,641	-	66,691	-
- Transport and transport equipment	89,454	58.2	122,365	48.8
- Recreational activities	-	-	50,030	-
	232,068	57.4	407,493	34.0
Individuals				
- Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	25,820	99.9	22,655	100.0
- Loans for the purchase of other residential properties	535,716	99.8	583,720	100.0
- Credit card advances	330,921	-	296,806	-
- Others	361,678	37.9	342,301	35.4
	1,254,135	55.6	1,245,482	58.4
Loans for use in Hong Kong	1,486,203	55.9	1,652,975	52.4
Loans for use outside Hong Kong	359,118	35.9	403,604	30.0
	1,845,321	52.0	2,056,579	48.0

MEVAS Bank Limited**Supplementary Financial Information**

(Expressed in thousands of Hong Kong dollars)

4. Loans and advances to customers (Continued)

- (a) Gross advances to customers by industry sector classified according to the usage of loans and analysed by percentage covered by collateral (Continued)

For each industry sector reported above with loan balance constituting 10% or more of the total balance of advances to customers, the attributable amount of overdue loans and collectively assessed loan impairment allowances are as follows:

	As at 31 Dec 2008		
	Outstanding balance	Gross advances overdue for more than 3 months	Collectively assessed impairment allowances
Loans for use in Hong Kong			
Individuals			
- Loans for the purchase of other residential properties	535,716	-	21
- Credit card advances	330,921	1,253	4,532
	As at 31 Dec 2007		
	Outstanding balance	Gross advances overdue for more than 3 months	Collectively assessed impairment allowances
Loans for use in Hong Kong			
Individuals			
- Loans for the purchase of other residential properties	583,720	2,660	219
- Credit card advances	296,806	2,175	6,157

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

4. Loans and advances to customers (Continued)

- (a) Gross advances to customers by industry sector classified according to the usage of loans and analysed by percentage covered by collateral (Continued)

The amount of new allowances charged to income statement and advances written off during the year were disclosed in the tables below.

	2008		
	Allowances written back	Loans written off as uncollectible	Recoveries of advances written off in previous years
Loans for use in Hong Kong			
Industrial, commercial and financial			
- Property investment	(24)	-	-
Individuals			
- Loans for the purchase of other residential properties	(198)	-	-
	(222)	-	-
		2007	
	Allowances written back	Loans written off as uncollectible	Recoveries of advances written off in previous years
Loans for use in Hong Kong			
Industrial, commercial and financial			
- Property investment	(586)	-	-
Individuals			
- Loans for the purchase of other residential properties	(5,011)	-	-
	(5,597)	-	-

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

4. Loans and advances to customers (Continued)

(b) Non-bank Mainland exposures

As at 31 Dec 2008			
Type of counterparties	On-balance sheet exposure	Off-balance sheet exposure	Total
Mainland entities	217,274	-	217,274
Companies and individuals outside Mainland where the credits are granted for use in the Mainland	<u>104,186</u>	<u>-</u>	<u>104,186</u>
As at 31 Dec 2007			
Type of counterparties	On-balance sheet exposure	Off-balance sheet exposure	Total
Mainland entities	305,003	-	305,003
Companies and individuals outside Mainland where the credits are granted for use in the Mainland	<u>113,127</u>	<u>-</u>	<u>113,127</u>

Note: The balances of exposures reported above include gross advances and other balances of claims on the customers.

(c) Analysis of gross advances to customers and overdue loans by geographical area

	As at 31 Dec 2008	As at 31 Dec 2007
Gross advances to customers		
- Hong Kong	1,504,420	1,687,383
- China	75,000	76,135
- Others	<u>265,901</u>	<u>293,061</u>
	<u>1,845,321</u>	<u>2,056,579</u>
Gross advances overdue for over 3 months		
- Hong Kong	<u>1,782</u>	<u>5,071</u>

Advances to customers by geographical area are classified according to the location of the counterparties after taking into account the transfer of risk. In general, risk transfer applies when an advance is guaranteed by a party located in an area which is different from that of the counterparty.

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

5. Capital charge for credit, market and operational risks

The capital adequacy ratio of the Bank as at 31 December 2008 disclosed in Note 1 above is computed on Basel II basis with reference to the methods set out in the Banking (Capital) Rules.

The decrease in regulatory capital in the year of 2008 is mainly due to interim dividend paid in the year.

The capital charge for each class of exposures are summarised as follows.

(a) Capital charge for credit risk

	2008	2007
Sovereign exposures	-	-
Public Sector Entity exposures	574	540
Multilateral Development Bank exposures	-	-
Bank exposures	72,296	83,914
Securities firm exposures	-	-
Corporate exposures	42,112	60,336
Collective investment schemes exposures	-	-
Cash items	-	1
Regulatory retail exposures	34,973	33,072
Residential mortgage loans	24,522	24,677
Other exposures which are not past due exposures	7,273	3,300
Past due exposures	216	513
Total capital charge for on-balance sheet exposures	<u>181,966</u>	<u>206,353</u>
Direct credit substitutes	21	21
Other commitments	2,337	1,791
Exchange rate contracts	-	-
Interest rate contracts	208	10
Total capital charge for off-balance sheet exposures	<u>2,566</u>	<u>1,822</u>
Total capital charge for credit risk	<u>184,532</u>	<u>208,175</u>

This disclosure is made by multiplying the Bank's risk-weighted amount derived from the relevant calculation approach by 8%, not the Bank's actual "regulatory capital".

(b) Operational risk capital charge

The Bank uses the Basic Indicator Approach for calculating operational risk.

	2008	2007
Capital charge for operational risk	<u>17,910</u>	<u>15,743</u>

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

6. Corporate governance

Corporate governance is concerned with how companies are managed and controlled, and in particular the role and operation of the Board of Directors in sustaining sound business integrity and practices, and effective accountability.

(a) *Statement of Compliance*

The Bank has fully complied with the requirements set out in the Supervisory Policy Manual entitled "Corporate Governance of Locally Incorporated Authorized Institutions" issued by the HKMA.

(b) *The Board*

As at 31 December 2008, the Board comprised an executive Chairman, five executive directors including the Chief Executive, and three non-executive directors. The Board meets at least quarterly. Its principal roles include the formulation and approval of corporate and business strategy, review of operations and financial performance, approval of key policies and annual business plan, and ensuring the maintenance of sound risk management and regulatory compliance.

Executive directors are appointed to the Board based on their experience, specialist skill and knowledge of different businesses of the Bank. Non-executive directors bring to the Board their knowledge and experience of other markets and industries, guide executive management's strategy development and policy implementation, and provide valuable external perspectives in the Board's deliberations.

(c) *Board and Specialised Committees*

(i) Audit Committee

The Banking Group Audit Committee, established by the Board of Dah Sing Banking Group Limited ("DSBG" or the "Group"), has the authority to review all matters related to the financial statements and disclosures, audit work performed by internal and external auditors, internal control systems, and the effectiveness of risk management and compliance for the whole Group including the Bank. The Committee reports to the Board of DSBG and of the Bank its observations and comments on any issue that needs to be brought to the attention of the Board, and makes recommendation to the Board regarding financial statements and results announcements.

Three independent non-executive directors of DSBG comprise the Group Audit Committee, which meets at least twice a year with the Group's and the Bank's senior management, the head of internal audit and the external auditors. The Chairman of the Committee is an independent non-executive director with a very high level of financial and audit experience.

The head of internal audit of the Group reports functionally to the Audit Committee. External auditors have direct access to the Committee for expressing their views and comments on any matter or concern relating to the Group or the Bank.

(ii) Executive Committee

The Executive Committee is chaired by the Group Chief Executive. Members include the Chief Executive of the Bank and the Alternate Chief Executives of the Bank, the Group's Finance Director, and Head of Group Risk. It is responsible for developing and setting the strategy and objectives of the Bank. It provides direction and guidance to business divisions, reviews business performance, ensures effective internal control systems, allocates resources, prioritises business initiatives and investment, and is delegated with the authority of the Board to exercise the authority and power of the Board on matters relating to the normal course of business of the Bank.

The Committee can call upon other directors or members of senior management for advice or participation in its discussion as it deems appropriate.

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

6. Corporate governance (Continued)

(c) *Board and Specialised Committees (Continued)*

(iii) Asset and Liability Management Committee

The Banking Group Asset and Liability Management Committee (“ALCO”) is accountable to the Banking Group Executive Committee, and oversees the overall management of the balance sheet, liquidity, funding, interest rate risk and market risk of the Group and of the Bank. It is responsible for formulating business plans affecting lending business, loan mix, treasury investments, deposit taking and capital management. It also plays a key role in the overall risk governance and management of the Group and the Bank.

ALCO meets every week and its regular tasks include the review of key business emphasis and development, loan and deposit changes, funding requirement, liquidity, surplus funds investments, capital market dealing, and review of market changes and competition. ALCO also conducts a regular monthly review of overall balance sheet and business performance, including trend analysis and actual positions against limits and targets.

ALCO is chaired by the Group Chief Executive. Members of the Committee include all executive directors of the Bank, heads of most business divisions, risk management and financial control.

(iv) Credit Committee

The Group’s Joint Retail Credit Committee consists of the relevant executive directors, Head of Group Risk, senior business, credit and risk officers of the Group which include the Chief Executive of the Bank, and is chaired by the Chief Executive of the Group. The Committee has the responsibility for formulating and revising credit policies and procedures for the Bank, approving credits which exceed individual credit officer’s credit authority, and reviewing credit performance and loan provisioning. Credit policies and procedures define the credit extension criteria and guidelines, credit approval, review and monitoring process and the systems of loan classification and provisioning.

The Bank’s commercial banking activities (mainly in the form of syndicated lending) are conducted, controlled and monitored in accordance with the commercial banking credit policy and procedure of Dah Sing Bank, Limited (“DSB”). The Bank has outsourced the credit administration, credit review and control of its commercial lending portfolio to DSB and its commercial banking credit committee.

(v) Compliance Committee

The Banking Group Compliance Committee is responsible for overseeing and guiding the development, maintenance and enhancement of compliance system, policies and practices to ensure compliance with all statutory requirements and regulatory guidelines. The Committee serves to uphold a high level of awareness and accountability for compliance requirements. The Banking Group has adopted an ongoing compliance control and monitoring process within business and support functions to enhance compliance control.

Members of the Compliance Committee include the Group Chief Executive, the Head of Legal and Compliance, a number of executive directors and senior operation and risk control executives of the Group. Minutes of the Committee meetings and regular reports are submitted to the Banking Group Audit Committee.

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

6. Corporate governance (Continued)

(c) *Board and Specialised Committees (Continued)*

(vi) IT Steering Committee

The Group IT Steering Committee is responsible for providing IT strategic direction, ensuring sound and robust IT infrastructure and processes to support the Group's businesses. It is also responsible for ensuring that IT risk control, information security and operations continuity are managed effectively, and for overseeing the Group's IT resources allocation, project justification and prioritisation.

The Committee is chaired by the Group Chief Executive and includes most division heads of the Group, including the Chief Executive of the Bank, as its members.

(vii) Human Resources Committee

The Group Human Resources Committee is responsible for setting the overall human resources direction of the Group and guiding the development of people strategy, policy and practices. It is responsible for overseeing corporate culture development, planning and implementation, remuneration programs and changes, staff development plans, employee relations projects and human resources systems.

The Committee is chaired by the Group Chief Executive. Members comprise the Chairman of the Group and a number of division heads.

7. Risk management

The Bank recognises the changing nature of risk and manages it through a well developed management structure.

Risk management is focused on the five major areas of risk – credit risk, market risk, interest rate risk, liquidity risk and operational risk. Credit risk occurs mainly in the Bank's credit portfolios comprising primarily retail secured and unsecured lending.

Market risk arises mainly in Treasury and is associated principally with the Bank's on-balance sheet positions in the trading book, and off-balance sheet positions taken to hedge elements of the trading book.

Interest rate risk means the risk to the Bank's financial condition resulting from adverse movements in interest rates.

Liquidity risk arises across the Bank's balance sheet.

Operational risk is the risk of loss (direct or indirect) resulting from inadequate or failed internal processes, people and systems or from external events.

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

7. Risk management (Continued)

Apart from the description of financial risk management disclosed in Note 3 to the financial statements, the other risk management aspects are disclosed below:

(a) *The risk management structure of the Bank*

The Board of Directors has the broad overall responsibility for the management of all types of risk. The responsibilities of the Board in relation to risk control are:

- the approval of the overall strategy and policies to ensure that credit and other risks are properly managed at both the transaction and portfolio levels;
- the management of risk, both financial and non-financial, conducted through operational and administrative control systems including the operation of the Audit Committee; review of key results (against forecasts), operational statistics and policy compliance; and
- financial performance by analysis against approved budgets and analysis of variations in key non-financial measures.

The Executive Committee has been delegated the authority to oversee and guide the management of different risks which are more particularly managed and dealt with by Group Risk and different functional committees.

(b) *Group risk function*

The independent Group Risk function is responsible for ensuring that policies and mandates are established for the Group as a whole. Group Risk monitors and reports Group risk positions to the Board via the Executive Committee, sets standards for financial risks and data integrity and ensures that the financial risks are fully considered in the product planning and pricing process. Group Risk reviews and approves all credit and risk exposure policies for the Bank including the approval of exposures to new markets, economic sectors, organisations, credit products and financial instruments which expose the Bank to credit and related risks. In determining credit and risk policies, Group Risk takes into account the guidelines established by the HKMA, business direction and risk adjusted performance of each business. The Group Risk director is a member of the Group's Joint Retail Credit Committee and an executive director of the Bank.

The Bank's risk management expertise continues to advance the overall quality of the Bank's lending portfolios, and enables the Bank to meet the changing regulatory requirements and enter into credit exposures with the confidence that it understands the associated risks and rewards.

The Bank is continuing to evolve its risk management capabilities under the aegis of the Head of Group Risk, increasing the focus of its risk strategy on risk and reward and returns on capital. The Bank uses a range of risk measurement and analytical tools in its management of the various risks which it faces in its day-to-day businesses and these are continually being enhanced and upgraded to reflect the ever-changing business needs and the requirements of the regulators.

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

7. Risk management (Continued)

(c) Credit risk

(i) Credit risk exposures

Standard & Poor's Ratings Services ("Standard & Poor's"), Moody's Investors Services ("Moody's") and Fitch Ratings are the external credit assessment institutions ("ECAIs") that the Bank uses for the assessment of its credit risk exposures to banks, sovereigns, public sector entities, and collective investment schemes as well as securitisation exposures and exposures to corporates that do not qualify as regulatory retail exposures.

The process the Bank uses to map ECAI issuer ratings to exposures booked in its banking book follows the process prescribed in Part 4 of the Banking (Capital) Rules.

2008 Class of exposures	Exposures after recognised credit risk mitigation		Risk-weighted amounts				Total exposure covered by recognised collateral	Total exposure covered by recognised guarantees or recognised credit derivative contracts
	Total Exposures (Note 1)	Rated (Note 2)	Unrated (Note 3)	Rated (Note 2)	Unrated (Note 3)	Total risk- weighted amounts		
A. On-balance sheet								
1. Sovereign	2,817	2,817	-	-	-	-	-	-
2. Public Sector Entity	-	35,860	-	7,172	-	-	-	-
3. Multilateral Development Bank	-	-	-	-	-	-	-	-
4. Bank	4,393,468	4,393,468	-	903,702	-	903,702	-	-
5. Securities firm	-	-	-	-	-	-	-	-
6. Corporate	526,402	-	526,402	-	526,402	526,402	-	-
7. Collective investment scheme	-	-	-	-	-	-	-	-
8. Cash items	19,701	-	21,013	-	-	-	-	-
9. Regulatory retail	584,190	-	582,878	-	437,159	437,159	1,312	-
10. Residential mortgage loans	739,393	-	703,533	-	306,524	306,524	-	35,860
11. Other exposures which are not past due exposures	90,911	-	90,911	-	90,911	90,911	-	-
12. Past due exposures	1,803	-	1,803	-	2,705	2,705	-	-
B. Off-balance sheet								
1. Off-balance sheet exposures other than OTC derivative transactions or credit derivative contracts	35,936	8,000	27,936	1,600	27,878	29,478	-	-
2. OTC derivative transactions	3,377	1,561	1,816	780	1,816	2,596	-	-
3. Credit derivative contracts	-	-	-	-	-	-	-	-
Exposures deducted from capital base	2,147							

MEVAS Bank Limited

Supplementary Financial Information (Expressed in thousands of Hong Kong dollars)

7. Risk management (Continued)

(c) Credit risk (Continued)

(i) Credit risk exposures (Continued)

2007 Class of exposures	Exposures after recognised credit risk mitigation		Risk-weighted amounts				Total exposure covered by recognised collateral	Total exposure covered by recognised guarantees or recognised credit derivative contracts
	Total Exposures (Note 1)	Rated (Note 2)	Unrated (Note 3)	Rated (Note 2)	Unrated (Note 3)	Total risk- weighted amounts		
A. On-balance sheet								
1. Sovereign	18,438	-	-	-	-	-	-	-
2. Public Sector Entity	-	33,750	-	6,750	-	6,750	-	-
3. Multilateral Development Bank	-	-	-	-	-	-	-	-
4. Bank	4,874,542	4,874,542	-	1,048,922	-	1,048,922	-	-
5. Securities firm	-	-	-	-	-	-	-	-
6. Corporate	754,200	-	754,200	-	754,200	754,200	-	-
7. Collective investment scheme	-	-	-	-	-	-	-	-
8. Cash items	17,388	-	19,243	-	17	17	-	-
9. Regulatory retail	553,047	-	551,192	-	413,394	413,394	1,855	-
10. Residential mortgage loans	752,038	-	718,288	-	308,461	308,461	-	33,750
11. Other exposures which are not past due exposures	41,250	-	41,250	-	41,250	41,250	-	-
12. Past due exposures	5,206	-	5,206	-	6,418	6,418	2,783	-
B. Off-balance sheet								
1. Off-balance sheet exposures other than OTC derivative transactions or credit derivative contracts	29,758	8,000	21,758	1,600	21,052	22,652	-	-
2. OTC derivative transactions	345	240	105	120	-	120	-	-
3. Credit derivative contracts	-	-	-	-	-	-	-	-
Exposures deducted from capital base	504							

Note

- (1) principal amount or credit equivalent amount, as applicable, net of individually assessed impairment allowances
- (2) including exposures with ECAI issue-specific rating and exposures which have an inferred rating (i.e. exposures which do not have an issue-specific rating but whose risk-weights are determined under the Capital Rules by reference to an ECAI issuer rating assigned to the obligor of the exposure or to an ECAI issue rating of any other exposures of the obligor).
- (3) exposures which do not have ECAI issue-specific rating, nor inferred rating.

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

7. Risk management (Continued)

(c) Credit risk (Continued)

(ii) Counterparty credit risk exposures

The Bank exercises strict control limits in tenor and outstanding amounts on net open positions arising from over-the-counter ("OTC") derivative transactions booked in its banking book. The credit risk exposures associated with these contracts are predominantly their fair values (i.e. the positive marked-to-market values favourable to the Bank). These credit risk exposures together with potential exposures from market movements are managed as part of the overall lending limits allowed to counterparties. Collateral or other security is generally not obtained for such credit risk exposures.

Settlement risk arises in situations where a payment in cash or a delivery of securities or equities is made in expectation of a corresponding receipt in cash, securities or equities. To mitigate settlement risk, daily settlement limits are established for each counterparty on the aggregate of all settlements on any day. The Bank will also enter into netting arrangements and make settlement on the basis of delivery against payment as appropriate.

The following table summarises the Bank's main credit exposures arising from OTC derivative transactions.

	2008	2007
OTC derivative:		
Gross total positive fair value	2,719	64
Credit equivalent amounts	<u>3,377</u>	<u>345</u>
Risk weighted amounts	<u>2,596</u>	<u>120</u>

An analysis of the credit equivalent amounts or net credit exposures, and the risk-weighted amount is summarised as follows.

	2008	2007
OTC derivative:		
Notional amounts:		
- Banks	45,660	100,400
- Others	<u>91,320</u>	<u>7,161</u>
	<u>136,980</u>	<u>107,561</u>
Credit equivalent amounts:		
- Banks	1,561	240
- Others	<u>1,816</u>	<u>105</u>
	<u>3,377</u>	<u>345</u>
Risk-weighted amounts:		
- Banks	780	120
- Others	<u>1,816</u>	<u>-</u>
	<u>2,596</u>	<u>120</u>

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

7. Risk management (Continued)

(c) Credit risk (Continued)

(iii) Credit risk mitigation

The credit risk mitigation techniques used by the Bank are generally those recognised by the Banking (Capital) Rules for reduced capital weighting. Common types of collateral obtained are cash deposits and real estate properties. For certain types of advances to customers, the Bank also places reliance on guarantees issued by governments, public sector entities and corporates with acceptable credit rating.

The value of all real estate properties taken as collateral is appraised prior to the inception of the loans. For property collateral supporting problem accounts, their open market values are appraised at least every six months. For property collateral that has been repossessed, the Bank's policy is to arrange for realisation as soon as practicable.

(d) Market risk

The Bank is exposed to various types of market risk. Details of the risk management policies and procedures adopted are set out in Note 3.3 to the financial statements.

(e) Equity exposures in banking book

The Bank distinguishes its equity holdings between those taken for strategic reasons and those taken for capital appreciation purposes at inception of the acquisition. Equity holdings identified for capital appreciation purpose is evaluated based on rigorous investment analysis and is subject to internal guidelines on stock selection, marketability, valuation, position limit, management action trigger, and various other control guidelines specified in the Treasury Policy Manual. Equity holdings are valued on the basis of bid market prices.

	2008	2007
Realised gains from sales and redemption	546	3,651
Unrealised revaluation gains		
- Amount included in reserves but not through income statement	528	44
- Amount deducted from supplementary capital	237	20
	<u>237</u>	<u>20</u>

(f) Interest rate risk exposures in banking book

2008	Currency		Total
	HK\$	US\$	
Interest rate risk shock +200 basis points			
- Increase in earnings	<u>10,000</u>	<u>1,000</u>	<u>11,000</u>
2007			
Interest rate risk shock +200 basis points			
- Increase in earnings	<u>7,000</u>	<u>-</u>	<u>7,000</u>

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

7. Risk management (Continued)

(g) Operational risk

The Bank manages its operational risk through a management structure comprising members of senior management and operational risk officers from each business and support function, and operating through a set of operational risk policies, risk tool-kits, operational risk incident reporting and tracking system, and control self assessment and key risk indicator tools. Together with a well established internal control systems, operational risk in most situations can be adequately identified, assessed, monitored and mitigated. To allow the operational risk framework to be clearly communicated to all levels within the Bank, awareness and training programs are conducted from time to time.

To minimise the impact on the Bank's business in the event of system failure or disasters, back-up sites and operational recovery policies and plans have been established and tested for all critical business and operations functions.

Operational risk framework is also supported by periodic independent reviews of internal control systems by external and internal auditors. Reporting and assessment of the performance of operational risk management are monitored by the Group Risk and reported to the Group's Risk Management Committee.

(h) Reputation risk

Reputation risk is the risk arising from the potential that negative publicity regarding the Bank's business practices, operational errors or operating performance, whether true or not, could cause customer concerns or negative view, decline in the customer base or market share, or lead to costly litigation or revenue reductions.

The Bank manages reputation risk through upholding a high standard of corporate governance and management oversight, maintenance of effective policies and procedures with emphasis on internal control, risk management and compliance; proper staff training and supervision; proper handling of customer complaints or dissatisfaction; and adherence to sound business practices. Standards are set and policies and procedures are established by the Bank in all areas, which operate to reduce vulnerability to reputation risk.

(i) Strategic risk

Strategic risk generally refers to the corporate risk that may bring significant immediate or future negative impact on the financial and market positions of the Bank because of poor strategic decisions, unacceptable financial performance, improper implementation of strategies and lack of effective response to the market changes.

The Board of Directors, assisted by senior management, is directly responsible for the management of strategic risk. Directors formulate the strategic goals and key direction of the Bank, ensure business strategies are developed to achieve these goals, oversee the strategic development and implementation to secure compatibility with the Bank's strategic goals, review business performance, deploy proper resources to achieve the Bank's objectives, and authorise management to take appropriate actions to mitigate risks.

MEVAS Bank Limited

Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

7. Risk management (Continued)

(j) Implementation of the Basel II Capital Accord

The revised capital adequacy framework known as Basel II has come into force for all locally incorporated authorized institutions in Hong Kong from January 2007. To implement Basel II, the HKMA published the final Banking (Capital) Rules and Banking (Disclosure) Rules at the end of 2006.

Basel II is structured around three "Pillars". Pillar 1 sets out the minimum capital requirements for a bank's operational risk, in addition to revising the "Basel I" treatment of credit risk and market risk. Pillar 2 requires that banks should have in place sound internal processes to assess the adequacy of their capital, based on a thorough assessment of their risks including those risks not covered under Pillar 1, and that supervisors should carry out supervisory review of this process. Pillar 3 complements Pillar 1 and Pillar 2 through enhanced market transparency and market discipline by requiring banks to make public disclosure of information on their risk profiles, capital adequacy and risk management.

Starting January 2007, the Bank adopts the standardised approach for credit risk, and the basic indicator approach for operational risk. These are the default approaches as specified in the Banking (Capital) Rules. Accordingly, the Bank has overhauled its systems and controls in order to meet the standards required for these approaches.

(k) The role of Internal Audit

The Banking Group's Internal Audit Division is an independent, objective assurance and consulting unit which is designed to focus on enhancing and sustaining sound internal control in all business and operational units of the Banking Group including the Bank. The Division reports functionally to the Banking Group Audit Committee, which is chaired by an Independent Non-Executive Director. The Division conducts a wide variety of internal control activities such as compliance audits and operations and systems reviews to ensure the integrity, efficiency and effectiveness of the systems of control of the Bank.

Independent Auditor's Report
To the shareholders of MEVAS Bank Limited
(incorporated in Hong Kong with limited liability)

We have audited the financial statements of MEVAS Bank Limited (the "Bank") set out on pages 4 to 66 which comprise the balance sheet as at 31 December 2008, and the income statement, the statement of changes in equity and the cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility for the financial statements

The directors of the Bank are responsible for the preparation and the true and fair presentation of these financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants, and the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with section 141 of the Hong Kong Companies Ordinance and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

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

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

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

Opinion

In our opinion, the financial statements give a true and fair view of the state of affairs of the Bank as at 31 December 2008 and of its profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

PricewaterhouseCoopers

Certified Public Accountants

Hong Kong, 20 April 2009