HSBC AMANAH MALAYSIA BERHAD
(Company No. 807705-X)
(Incorporated in Malaysia)

FINANCIAL STATEMENTS – 31 DECEMBER 2016

Domiciled in Malaysia.
Registered Office:
10th Floor, North Tower
2, Leboh Ampang,
50100 Kuala Lumpur

HSBC AMANAH MALAYSIA BERHAD
(Company No 807705-X)
(Incorporated in Malaysia)

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BOARD OF DIRECTORS

Dr. Mohamed Ashraf bin Mohamed Iqbal
Chairman *(appointed on 3 January 2017)*
Independent Non-Executive Director

Louisa Cheang Wai Wan
Non-Independent Executive Director (*re-appointed and re-designated on 1 January 2017)*

Mukhtar Malik Hussain
Non-Independent Executive Director

Azlan bin Abdullah
Independent Non-Executive Director

Adil Ahmad
Independent Non-Executive Director

Lee Choo Hock
Independent Non-Executive Director *(appointed on 30 May 2016)*

Albert Quah Chei Jin
Independent Non-Executive Director *(appointed on 5 September 2016)*

Seow Yoo Lin
Independent Non-Executive Director (*resigned on 14 March 2016)*

Mohamed Ross bin Mohd Din
Independent Non-Executive Director *(retired on 13 April 2016)*

CORPORATE GOVERNANCE DISCLOSURES

The Bank is committed to high standards of corporate governance. As a licensed financial institution, the Bank is subject to and complies with Bank Negara Malaysia policy document on 'Corporate Governance'.

The statement of corporate governance practices set out on pages 2 to 15 and information incorporated by reference constitutes the Corporate Governance Disclosures of HSBC Amanah Malaysia Berhad (the Bank).

Directors

The Directors serving as at the date of this report are set out below.

Dr. Mohamed Ashraf bin Mohamed Iqbal, 52
Independent Non-Executive Director
Appointed to the Board: 6 August 2008

Chairman of Board

Dr. Ashraf has been appointed as the Chairman of the Board on 3 January 2017. He is also a member of Nominations Committee, Risk Committee and Connected Party Transactions Committee of the Bank.

Dr. Ashraf graduated from California State University, United States of America with a Bachelor of Science in Mechanical Engineering and thereafter obtained a Masters in Business Administration from the same institution. In addition he holds a post graduate diploma in Islamic Studies from the International Islamic University, Malaysia. He subsequently obtained his Doctorate of Philosophy in Islamic Finance from International Centre for Education in Islamic Finance in 2016.

His earlier career included a period of over 5 years with Shell Malaysia involved in a variety of human resource and business re-engineering projects. He then moved on to Proton Berhad where he assumed the positions of Managing Director of Proton Cars (UK) Ltd, Executive Director of Proton Cars (Europe) Ltd and Director of Proton Cars (Australia) Ltd. He then assumed the position of Director of Hay Group, Asia from 1999 to 2002 and Managing Director of Federal Auto Holdings Berhad from 2002 to 2005. He was formerly a Partner of CEO Solutions Sdn Bhd and an Advisor to Maestro Planning Solutions Sdn Bhd.

Dr. Ashraf is currently a Director of MindSpring Sdn Bhd, a consulting firm that he started in 2005.

Louisa Cheang Wai Wan, 54
Non-Independent Executive Director
Appointed to the Board and as chairman: 1 January 2012
Re-appointed and re-designated as Non-Independent Executive Director: 1 January 2017

Ms Cheang served as the Chairman of the Bank from 1 January 2012 to 31 December 2016.

Ms Cheang graduated from the University of Hong Kong majoring in Political Science and Management Studies. Ms Cheang is currently the Group General Manager, Group Head of Retail Banking and Wealth Management (RBWM), HSBC, London. She has been Regional Director of Personal Financial Services Asia-Pacific since June 2009 overseeing HSBC's personal financial services business in Hong Kong and 18 other countries and territories in the region. Prior to this, Ms Cheang was Head of Personal Financial Services Hong Kong and Head of Marketing in Asia-Pacific. Before joining HSBC, Ms Cheang was the marketing head at Citibank, Smartone Mobile Communications and American Express.

Ms Cheang's other current roles include International Advisor of China Union Pay and Honorary Certified Financial Management Planner of the Hong Kong Institute of Bankers.

Mukhtar Malik Hussain, 57
Non-Independent Executive Director
Appointed to the Board: 15 December 2009

Mr Mukhtar graduated from University of Wales with a Bachelor of Science in Economics. He first joined the HSBC Group in 1982 as a Graduate Trainee in Midland Bank International. He was then appointed as Assistant Director in Samuel Montagu in 1991. After more than 10 years of working in the HSBC Group's London offices, Mr Mukhtar held numerous posts in Dubai including Chief Executive Officer of HSBC Financial Services (Middle East) Limited from 1995 to 2003. He established the initiative to create the first foreign investment bank in Saudi Arabia for HSBC.

In 2003, Mr Mukhtar assumed the position of Chief Executive Officer, Corporate and Investment Banking. He headed back to London as the Co-Head of Global Banking in 2005. He was the Global Head of Principal Investments in London from 2006 to 2008. Between 2008 to 2009, he was the Deputy Chairman, HSBC Bank Middle East Limited and Global Chief Executive Officer of HSBC Amanah. He was also the Chief Executive Officer, Global Banking and Markets for Middle East and North Africa.

Mr Mukhtar is currently also the Director and Chief Executive Officer of HSBC Bank Malaysia Berhad, a HSBC Group General Manager and member of the Executive Committee of HSBC Asia Pacific.

Azlan bin Abdullah, 59
Independent Non-Executive Director
Appointed to the Board: 6 August 2008

En Azlan is a member of the Audit Committee , Nominations Committee and Connected Party Transactions Committee of the Bank. En Azlan graduated from Trinity University, United States of America with a Bachelor of Science in Business Administration and Morehead State University, United States of America with a Masters in Business Administration. En Azlan began his career in Citibank N.A in the World Corporate Group, a division within the Corporate Banking Group in 1983. After 5 years, he then moved on to United Asian Bank which later merged with Bank of Commerce. In 1994, he joined Citibank Berhad as Vice President and Head of the Public Sector, a division in the Corporate Banking Group focusing on lending to government-owned entities (GLCs).

En Azlan is currently the Group Managing Director/Chief Executive Officer of Melewar Industrial Group Berhad and the Chief Executive Officer of Mycron Steel Berhad and Mycron Steel CRC Sdn Bhd. He also serves as director of Langkawi Yatch Club Berhad and in several other private limited companies. In addition, he is a council member and the Deputy President of Malaysian Iron and Steel Industry Federation and an alumni member of International Association of Traffic and Safety Sciences based in Japan.

Adil Ahmad, 60
Independent Non-Executive Director
Appointed to the Board: 5 May 2014

Chairman of Nominations and Remuneration Committee

En Adil is the Chairman of Nominations and Remuneration Committee, a member of the Audit Committee, Risk Committee and Connected Party Transactions Committee of the Bank. He holds a Masters in Business Administration (Finance & Accounting) and BA in Economics from Cornell University, Ithaca, New York. He has 30 years of international banking experience and began his career in the 1980s at ANZ Grindlays Bank Pakistan. He was the Director and Head of Global Islamic Finance of ANZ Investment Bank in London from 1993 to 1997 and thereafter Executive, Group Strategy of ANZ Banking Group Ltd in Melbourne from 1997 to 2000. He assumed the position as the Chief Executive Officer of ANZ Banking Group Ltd Vietnam from 2000 to 2005. In 2006 he left the ANZ Banking Group to become CEO of Kuwait International Bank, from where he retired in 2009.

Since retiring to Malaysia, En Adil has advised international clients on strategic and financial matters for projects in Vietnam, Malaysia and Pakistan, and has provided Islamic and conventional banking training programs for banks and other financial institutions.

Lee Choo Hock, 64
Independent Non-Executive Director
Appointed to the Board: 30 May 2016

Chairman of Risk Committee

Mr Lee is the Chairman of Risk Committee and a member of the Audit Committee and Nominations Committee of the Bank. He is a member of the Institute of Chartered Accountants in England and Wales as well as the Malaysian Institute of Accountants. He began his career with Miller, Brener & Co., London, a professional accounting firm in 1975 and joined Maybank in 1982. Having worked with Maybank for 27 years, Mr Lee has built a successful career as a professional accountant. He served various management positions during his tenure with Malayan Banking Berhad until he retired in 2008 and last position was as the Executive Vice President, Head of Accounting Services and Treasury Back Office Operations. He has also served as a Director of a number of subsidiaries of Malayan Banking Berhad.

In addition to his current role, Mr Lee also sits on the Board of HSBC Bank Malaysia Berhad, Kossan Rubber Industries Berhad and Yayasan Kossan.

CORPORATE GOVERNANCE DISCLOSURES (Cont'd)

Albert Quah Chei Jin, 64
Independent Non-Executive Director
Appointed to the Board: 5 September 2016

Chairman of Audit Committee

Mr Albert Quah is the Chairman of Audit Committee and a member of the Risk Committee and Nominations Committee of the Bank. Mr Albert Quah holds a Masters Degree in Accounting and Finance from the London School of Economics and Political Science. He is a member of the Institute of Chartered Accountants in England and Wales as well as the Malaysian Institute of Accountants. He was with Touche Ross & Co, Chartered Accountants in London before returning to Malaysia.

He has more than 30 years banking experience. Mr Albert Quah began his banking career with Southern Bank Berhad in 1982 where he served in various management positions including as a Card Centre Manager as well as a Corporate Banker. He joined Standard Chartered Bank Malaysia Berhad as Senior Corporate Banker in 1989 and was the CFO of Standard Chartered Bank Malaysia Berhad from 1993 to 2001. He later served as Group CFO in the AmBank Group from 2004 to 2006. He retired as CFO of United Overseas Bank Malaysia Berhad in 2013.

In addition to his current role, Mr Albert Quah also sits on the Board of Indah Water Konsortium Sdn Bhd and also the Non-Executive Trustee of Methodist Education Foundation.

BOARD RESPONSIBILITY AND OVERSIGHT

Board of Directors

The objectives of the management structures within the Bank, headed by the Board of Directors and led by the Chairman, are to deliver sustainable value to shareholders. The Board sets the strategy and risk appetite for the Bank and approves capital and operating plans presented by management for the achievement of the strategic objectives it has set.

The Board meets regularly and Directors receive information between meetings about the activities of committees and developments in the Bank's business. All Directors have full and timely access to all relevant information and may take independent professional advice if necessary.

At the date of this report, the Board consists of seven (7) members comprising two (2) Non-Independent Executive Directors and five (5) Independent Directors. The names of the Directors serving at the date of this report and brief biographical particulars for each of them are set out on pages 2 to 5.

On 3 January 2017, Dr Mohamed Ashraf bin Mohamed Iqbal has been appointed as Independent Board Chairman of the Bank in replacement of Louisa Cheang Wai Wan who has been re-appointed and re-designated as Non Independent Executive Director of the Bank on 1 January 2017.

Lee Choo Hock was appointed as Independent Non-Executive Director and as the Chairman of Risk Committee, a member of the Audit Committee and Nominations Committee on 30 May 2016.

Albert Quah Chei Jin was appointed as an Independent Non-Executive Director and as the Chairman of Audit Committee, a member of the Risk Committee and Nominations Committee on 5 September 2016.

Seow Yoo Lin resigned as an Independent Non-Executive Director on 14 March 2016 and Mohamed Ross bin Mohd Din retired as an Independent Non-Executive Director on 13 April 2016.

All Directors, including those appointed by the Board to fill a casual vacancy, are subject to annual re-election at the Bank's Annual General Meeting.

Non-executive Directors are not HSBC employees and do not participate in the daily business management of the Bank. They bring an external perspective, constructively challenge and help develop proposals on strategy, scrutinise the performance of management in meeting agreed goals and objectives, and monitor the risk profile and reporting of performance of the Bank. The Board has determined that each non-executive Director is independent in character and judgement, and there are no relationships or circumstances likely to affect the judgement of the independent non-executive Directors. The Board has also determined the minimum time commitment expected of non-executive directors to be about 30 days per annum and with appointment in not more than 5 public listed companies. Time devoted to the Bank could be considerably more, particularly if serving on Board committees.

CORPORATE GOVERNANCE DISCLOSURES (Cont'd)

BOARD RESPONSIBILITY AND OVERSIGHT (Cont'd)

Board of Directors (Cont'd)

Board Meetings

Six (6) Board meetings were held in 2016. The table below show each Director's attendance at meetings of all Board and Committees' meetings during 2016. All Directors have complied with the Bank Negara Malaysia requirements that Directors must attend at least 75% of Board meetings held in the financial year.

2016	**Board**	**Audit Committee**	**Risk Committee**	**Nominations Committee**
Total number of meetings held	6	4	5	6
Independent Non-executive Directors/Chairman:				
Dr.Mohamed Ashraf bin Mohamed Iqbal[1]	6/6	4/4	5/5	6/6
Non-Independent Executive Director:				
Louisa Cheang Wai Wan[2]	6/6	-	-	-
Mukhtar Hussain	6/6	-	-	-
Independent Non-executive Directors:				
Adil Ahmad	6/6	4/4	5/5	6/6
Albert Quah Chei Jin[3]	2/2	1/1	2/2	2/2
Azlan bin Abdullah	6/6	4/4	5/5	6/6
Lee Choo Hock[4]	4/4	3/3	4/4	4/4
Mohamed Ross bin Mohd Din[5]	1/1	1/1	1/1	1/1
Seow Yoo Lin[6]	1/1	1/1	1/1	1/1

[1] *appointed as Chairman on 3 January 2017*
[2] *re-appointed and re-designated as Non-Independent Executive-Director on 1 January 2017*
[3] *appointed on 5 September 2016*
[4] *appointed on 30 May 2016*
[5] *retired on 13 April 2016*
[6] *resigned on 14 March 2016*

Directors' Emoluments

Details of the emoluments of the Directors of the Bank for 2016, disclosed in accordance with the Companies Act, 1965, are shown in Note 32(b) to the financial statements.

CORPORATE GOVERNANCE DISCLOSURES (Cont'd)

BOARD RESPONSIBILITY AND OVERSIGHT (Cont'd)

Board of Directors (Cont'd)

Training and Development

Formal, tailored induction programmes are arranged for newly appointed Directors. The induction programmes consists of a series of meetings with senior executives to enable new Directors to familiarise themselves with the business. Directors also received comprehensive guidance from the Company Secretary on Directors' duties and responsibilities.

Training and development is provided for Directors. Executive Directors develop and refresh their skills and knowledge through day-to-day interactions and briefings with senior management of the Bank's businesses and functions. Non-Executive Directors have access to internal training and development resources and personalized training is provided, where necessary. The Nominations Committee, with support from the Company Secretary, regularly reviews the training and development of each Director.

The table below shows a summary of training and development undertaken by each Director during 2016.

	Training Areas				
	Regulatory updates	**Corporate Governance**	**Financial industry developments**	**Financial Crime Risk**	**Briefings on Board committees related topics**
Non-Independent Executive Directors:					
Louisa Cheang Wai Wan[1]	√	√	√	√	√
Mukhtar Hussain	√	√	√	√	√
Independent Non-executive Directors:					
Dr. Mohamed Ashraf bin Mohamed Iqbal	√	√	√	√	√
Adil Ahmad	√	√	√	√	√
Albert Quah Chei Jin	√	√	√	√	√
Azlan bin Abdullah	√	√	√	√	√
Lee Choo Hock	√	√	√	√	√

[1] *re-appointed and re-designated as Non-Independent Executive Director on 1 January 2017*

BOARD RESPONSIBILITY AND OVERSIGHT (Cont'd)

Board Committees

The Board has established a number of committees, the membership of which comprise independent non-executive Directors who have the skills, knowledge and experience relevant to the responsibilities of the committee. The Board and each Board committee have terms of reference to document their responsibilities and governance procedures. The details of the Board Charter comprising the Board committees' Terms of Reference are available at http://www.hsbcamanah.com.my/1/2/amanah/hsbc-amanah-and-you/corporate-information/board-of-directors.

The key roles of the Board committees are described in the paragraph below. The Chairman of each Board committee reports to each subsequent Board meeting when presenting the meeting minutes of the relevant committee.

As at the date of this report, the following are the principal Board committees:

1. Audit Committee

The Audit Committee is accountable to the Board and has non-executive responsibility for oversight of and advice to the Board on financial reporting related matters and internal controls over financial reporting, covering all material controls The Audit Committee reviews the financial statements of the Bank before submission to the Board. It also monitors and reviews the effectiveness of the internal audit function and the Bank's financial and accounting policies and practices. The Audit Committee advises the Board on the appointment of the external auditors and is responsible for oversight of the external auditors.

The Audit Committee meets regularly with the Bank's senior financial and internal audit management and the external auditor to consider, *inter alia*, the Bank's financial reporting, the nature and scope of audit reviews and the effectiveness of the systems of internal control relating to financial reporting.

The current members of the Audit Committee, all being independent non-executive Directors, are:
- Albert Quah Chei Jin (Chairman)
- Adil Ahmad
- Azlan bin Abdullah
- Lee Choo Hock

During 2016, the Audit Committee held 4 meetings. Attendance is set out in the table on page 7.

2. Risk Committee

The Risk Committee is accountable to the Board and has non-executive responsibility for oversight of and advice to the Board on high level risk related matters and risk governance.

The Risk Committee meets regularly with the Bank's senior financial, risk, internal audit and compliance management to consider, *inter alia*, risk reports and the effectiveness of compliance.

The Board and the Risk Committee oversee the maintenance and development of a strong risk management framework by continually monitoring the risk environment, top and emerging risks facing the Bank and mitigation actions planned and taken. The Risk Committee recommends the approval of the Bank's risk appetite statement to the Board and monitors performance against the key performance/risk indicators included within the statement. The Risk Committee monitors the risk profiles for all of the risk categories within the Bank's business.

The current members of the Risk Committee, all being independent non-executive Directors, are:
- Lee Choo Hock (Chairman)
- Adil Ahmad
- Albert Quah Chei Jin
- Dr. Mohamed Ashraf bin Mohamed Iqbal

During 2016, the Risk Committee held 5 meetings. Attendance is set out in the table on page 7.

BOARD RESPONSIBILITY AND OVERSIGHT (Cont'd)

Board Committees (Cont'd)

3. Nominations Committee

The Nominations Committee has the responsibility for leading the process for Board appointments and for identifying and nominating, for the approval of the Board, candidates for appointment to the Board and for the Chief Executive Officer.

The Nominations Committee considers plans for orderly succession to the Board and the appropriate balance of skills, knowledge and experience on the Board. The Nominations Committee assists the Board in the evaluation of the Board's own effectiveness and that of its committees annually. The findings of the performance evaluation and the implementation of actions arising from the performance evaluation are reported to the Board during 2016.

The members of the Nominations Committee, all being independent non-executive Directors, are:

- Dr. Mohamed Ashraf bin Mohamed Iqbal (Chairman until 31 December 2016)
- Adil Ahmad
- Albert Quah Chei Jin
- Azlan bin Abdullah
- Lee Choo Hock

During 2016, the Nominations Committee held 6 meetings. Attendance is set out in the table on page 7.

On 7 February 2017, the Board approved the setting up of a combined Nominations and Remuneration Committee and delegated the non-executive responsibility for identifying and nominating candidates for appointment by the Board and for supporting the Board in overseeing the operation of the Bank's remuneration system and reviewing the remuneration of Directors on the Board.

The members of the Nominations and Remuneration Committee, all being independent non-executive Directors, are:

- Adil Ahmad (Chairman)
- Albert Quah Chei Jin
- Azlan bin Abdullah
- Dr. Mohamed Ashraf bin Mohamed Iqbal
- Lee Choo Hock

4. Shariah Committee

The Shariah Committee was established with delegated authorities of the Board on the shariah operations and management of day-to-day running of the Bank in accordance with Shariah compliance and principles based on the Board's policies and directions.

The current members of the Shariah Committee are:

- Dr. Ziyaad Mahomed (appointed on 2 January 2017) – Chairman effective 7 February 2017
- Assoc. Prof. Dr. Younes Soualhi
- Assoc. Prof. Dr. Muhammad Yusuf Saleem Ghulam Nabi
- Khairul Anuar Ahmad
- Prof. Dr. Abdul Rahim Abdul Rahman
- Prof. Dr. Obiyathulla Ismath Bacha

BOARD RESPONSIBILITY AND OVERSIGHT (Cont'd)

Board Committees (Cont'd)

Delegations By the Board

Connected Party Transactions Committee

The Connected Party Transactions Committee is delegated with the authority of the Board to approve transactions with a connected party of the Bank.

The current members of the Connected Party Transactions Committee, are:
- Adil Ahmad
- Azlan bin Abdullah
- Chief Risk Officer
- Dr. Mohamed Ashraf bin Mohmaed Iqbal
- Head of Wholesale Credit and Market Risk

Executive Committee

The Executive Committee consists of key senior management members meets regularly and operates as a general management committee under the direct authority of the Board, exercising all of the powers, authorities and discretions of the Board in so far as they concern the management and day-to-day running of the Bank, in accordance with such policies and directions as the Board may from time to time determine. The Bank's Chief Executive Officer, Arsalaan Ahmed, chairs the Executive Committee.

Regular Risk Management Meetings of the Executive Committee, chaired by the Chief Risk Officer, Malaysia, are held to establish, maintain and periodically review the policy and guidelines for the management of risk within the Bank.

To strengthen the governance framework in anticipation of structural and regulatory changes that affect the Bank, the following sub-committees of the Executive Committee were established:

(i) Asset and Liability Management Committee

The Asset and Liability Management Committee is responsible for the efficient management of the Bank's balance sheet and the prudent management of risks.

(ii) Risk Management Meeting

The Risk Management Meeting is responsible for the oversight of the risk framework.

(iii) IT Steering Committee

The IT Steering Committee is responsible for the oversight of the implementation and development of IT strategy. The committee is accountable for reviewing, challenging and approving the financial planning and IT performance.

(iv) People Committee

The People Committee is established as a principle human resource forum to drive People Plan i.e. build capability, talent, succession and leaders. The Committee oversees the development and delivery of key people initiative or programs, and resolve any critical people risks or issues.

BOARD RESPONSIBILITY AND OVERSIGHT (Cont'd)

Board Committees (Cont'd)

Conflicts of Interest and Indemnification of Directors

The Bank's Articles of Association gives the Board authority to approve Directors' conflicts and potential conflicts of interest. The Board has adopted a policy and procedures for the approval of Directors' conflicts or potential conflicts of interest. The Board's powers to authorise conflicts are operating effectively and the procedures are being followed.

A review of situational conflicts which have been authorised, including the terms of authorisation, is undertaken by the Board annually.

The Articles of Association provide that Directors are entitled to be indemnified out of the assets of the Bank against claims from third parties in respect of certain liabilities arising in connection with the performance of their functions. Such indemnity provisions have been in place but have not been utilised by the Directors. All Directors have the benefit of directors' and officers' liability insurance.

MANAGEMENT REPORTS

The Board meetings are structured around a pre-set agenda and reports for discussion, notation and approvals are circulated in advance of the meeting dates. To enable Directors to keep abreast with the performance of the Bank, key reports submitted to the Board during the financial year include:

- Minutes of the Board Committees
- Annual Operating Plan
- Business Progress Report
- Capital Contingency Funding Plan
- Credit Advances Reports
- Credit Transactions and Exposures to Connected Parties
- Financial Crime Compliance: Anti-Money Laundering and Counter Terrorist Financing Reports
- Financial Performance Report
- Internal Capital Adequacy Assessment Process
- Market Risk Limits
- Operational Risk Report
- People Plan
- Regulatory Compliance Report
- Risk Appetite Statement
- Risk Management Reports
- Scenario Stress Testing Results

INTERNAL CONTROL FRAMEWORK

The Directors are responsible for reviewing the effectiveness of risk management and internal control systems and for determining the nature and extent of the principal risks the Bank is willing to take in achieving its strategic objectives. To meet this requirement, procedures have been designed for safeguarding assets against unauthorised use or disposal; for maintaining proper accounting records; and for ensuring the reliability and usefulness of financial information used within the business or for publication.

These procedures can only provide reasonable but not absolute assurance against material mis-statement, errors, losses or fraud. Key risk management and internal control procedures include the following:

- **HSBC Group standards**

  HSBC Global Standards Manual (GSM) brings together the common standards and principles used in the conduct of all businesses, whatever its location or nature. The GSM overlays all other manuals throughout HSBC Group and is a fundamental component of the HSBC Group's risk management structure. It establishes the high level standards and policies by which, and within which, all members of the HSBC Group conduct their businesses. The GSM is mandatory and applies to, and must be observed by, all businesses within the HSBC Group, regardless of the nature or location of their activities.

- **Delegation of authority within limits set by the Board**

  Authority to manage the day to day running of the Bank is delegated within limits set by the Board to the Chief Executive who has responsibility for overseeing the establishment and maintenance of systems of control appropriate to the business and who has the authority to delegate such duties and responsibilities as he sees fit. Appointments to certain senior positions within the Bank require the approval of the Board of Directors.

- **Risk identification and monitoring**

  Systems and procedures are in place to identify, control and report on the major risks facing the Bank as set out below:
  - wholesale credit risk;
  - retail credit risk;
  - financial crime compliance risk
  - capital management risk;
  - liquidity risk management risks;
  - market risk;
  - financial management risk;
  - strategic risk;
  - sustainability risk; and
  - operational risk (including accounting, tax, legal, regulatory compliance, financial crime, compliance, fiduciary, political, physical, internal, external, contingency, information security systems, operations, project and people risks.)

  Exposure to these risks is monitored by Board Risk Committee, Asset, Liability and Capital Management Committee, Executive Committee and Risk Management Meeting (RMM) of the Executive Committee which is chaired by Chief Risk Officer. The RMM also monitors the Bank's operational risk profile and the effective implementation of the Bank's operational risk management framework.

INTERNAL CONTROL FRAMEWORK (Cont'd)

- **Changes in market conditions/practices**

  Processes are in place to identify new risks arising from changes in market conditions/practices or customer behaviours, which could expose the Bank to heightened risk of loss or reputational damage. The Bank employs a top and emerging risks framework, which enables it to identify current and forward-looking risks and to take action which either prevents them materialising or limits their impact.

  During 2016, attention was focused on:
  – financial crime compliance risk;
  – affiliate risk;
  – macroeconomic and geopolitical risk;
  – macro prudential/ regulatory risk
  – people risk;
  – security risk (Information and physical security)

- **Strategic plans**

  Periodic strategic plans are prepared for Businesses and Functions within the framework of the HSBC Group's strategy. The Bank also prepares and adopts an Annual Operating Plan, which is informed by detailed analysis of risk appetite, describing the types and quantum of risk that we are prepared to take in executing our strategy and sets out the key business initiatives and the likely financial effects of those initiatives.

- **Financial reporting**

  The Bank's financial reporting process for preparing the financial statements is in accordance with the Malaysian Financial Reporting Standards, International Financial Reporting Standards, the requirements of the Companies Act, 1965 in Malaysia and guidelines issued by Bank Negara Malaysia, and, supported by a chart of accounts with detailed instructions and guidance on reporting requirements, issued by Global Finance to the Bank in advance of each reporting period end. The submission of financial information from the Bank is subject to certification by the responsible financial officer, and analytical review procedures at the Bank.

- **Responsibility for risk management**

  Management of global businesses and global functions are primarily accountable for measuring, monitoring, mitigating and managing their risks and controls. Processes are in place to ensure weaknesses are escalated to senior management and addressed, supported by our three lines of defence model.

- **IT operations**

  Centralised functional control is exercised over all IT development and operations. Common systems are employed for similar business processes wherever practicable.

- **Function management**

  Group-set policies, procedures and standards to control the principal risks detailed under 'Risk identification and monitoring' will be followed, unless those contravene the local regulations. In cases where the two do not contravene, the stricter one will be adopted. Limits of authorities to enter into credit and market risk exposures are delegated to line management of the Bank. The concurrence of the appropriate Global Risks is required, for credit proposals with specified higher risk characteristics. Credit and market risks are measured and reported at Bank level and aggregated for risk concentration analysis on a Groupwide basis.

INTERNAL CONTROL FRAMEWORK (Cont'd)

- **Internal audit**

  The establishment and maintenance of appropriate systems of risk management and internal control is primarily the responsibility of business management. The Global Internal Audit function, provides independent and objective assurance in respect of the adequacy of the design and operating effectiveness of the framework of risk management, control and governance processes, focusing on the areas of greatest risk to HSBC using a risk-based approach.

  Executive management is responsible for ensuring that recommendations made by the Global Internal Audit function are implemented within an appropriate and agreed timetable. Confirmation to this effect must be provided to Global Internal Audit.

  During the year, the Risk Committee and the Audit Committee have kept under review the effectiveness of this system of internal control and have reported regularly to the Board. In carrying out their reviews, the Audit Committee and Risk Committee receive regular business and operational risk assessments; regular reports from the heads of key risk functions, which cover all internal controls, both financial and non-financial; internal audit reports; external audit reports; prudential reviews; and regulatory reports.

  The Risk Committee monitors the status of principal risks and considers whether the mitigating actions put in place are appropriate. In addition, when unexpected losses have arisen or when incidents have occurred which indicate gaps in the control framework or in adherence to HSBC policies, the Risk Committee and the Audit Committee review special reports, prepared at the instigation of management, which analyse the cause of the issue, the lessons learned and the actions proposed by management to address the issue.

REMUNERATION POLICY

The remuneration policy for the HSBC Group is aiming to reward success, not failure, and to be properly aligned with the risk management framework and risk outcomes. In order to ensure alignment between remuneration and business strategy, individual remuneration is determined through assessment of performance, delivered against both annual and long-term objectives summarised in performance scorecards, as well as adherence to HSBC Values of being 'open, connected and dependable' and acting with 'courageous integrity'. Altogether, performance is judged not only on what is achieved over the short and long term, but also on how it is achieved, as the latter contributes to the sustainability of the organisation. The financial and non-financial measures incorporated in the annual and long-term scorecards are carefully considered to ensure alignment with the long-term strategy of the HSBC Group.

The Bank has fully adopted the remuneration policy of HSBC Holdings plc. Please refer to the HSBC remuneration practices and governance at http://www.hsbc.com/about-hsbc/corporate-governance for more details of the governance structure and the remuneration strategy of the HSBC Group.

In recognition to the local regulations, the materiality of definition needs to be taken into consideration in ensuring a robust corporate governance framework has been duly applied for the Bank. Further reviews will be conducted to ensure continued adherence to the underlying principles of the local regulations.

RATING BY EXTERNAL RATING AGENCIES

Details of the Bank's ratings are as follows:

Rating Agency	Date	Rating Classification	Ratings Received
RAM Ratings Services Berhad	Jun 2016	• Long term	AAA
		• Short term	P1
		• Multi-Currency Sukuk Programme	AAA
		• Outlook	Stable

DIRECTORS' REPORT

The Directors hereby submit their report and the audited financial statements of HSBC Amanah Malaysia Berhad (the Bank) for the financial year ended 31 December 2016.

Principal Activities

The principal activities of the Bank are Islamic banking business and related financial services.

There have been no significant changes in these activities during the financial year.

Results

	RM'000
Profit for the financial year attributable to the owner of the Bank	
Profit before tax	**101,624**
Tax expense	**(20,231)**
Profit after tax	**81,393**

Dividends

The Directors do not recommend any dividend payment in respect of the current financial year.

Reserves and Provisions

There were no material transfers to or from reserves or provisions during the financial year other than those disclosed in the financial statements.

Other statutory information

Before the financial statements of the Bank were finalised, the Directors took reasonable steps to ascertain that:

i) all known bad debts have been written off and adequate provision made for doubtful debts, and
ii) any current assets which were unlikely to be realised in the ordinary course of business have been written down to an amount which they might be expected so to realise.

At the date of this report, the Directors are not aware of any circumstances:

i) that would render the amount written off for bad debts, or the amount of provision for doubtful debts, in the financial statements of the Bank inadequate to any substantial extent,
ii) that would render the value attributed to the assets in the financial statements of the Bank misleading, or
iii) which have arisen which render adherence to the existing methods of valuation of assets or liabilities of the Bank misleading or inappropriate, or
iv) not otherwise dealt with in this report or the financial statements, that would render any amount stated in the financial statements of the Bank misleading.

At the date of this report, there does not exist:

i) any charge on the assets of the Bank that has arisen since the end of the financial year and which secures the liabilities of any other person, or
ii) any contingent liability in respect of the Bank that has arisen since the end of the financial year other than in the ordinary course of business.

Other statutory information (Cont'd)

No contingent liability or other liability of the Bank has become enforceable, or is likely to become enforceable within the period of twelve months after the end of the financial year which, in the opinion of the directors, will or may affect the ability of the Bank to meet its obligations as and when they fall due.

In the opinion of the Directors, the financial performance of the Bank for the financial year ended 31 December 2016 has not been substantially affected by any item, transaction, or event of a material and unusual nature, nor has any such item, transaction or event occurred in the interval between the end of that financial year and the date of this report.

Significant and Subsequent Events

There were no significant events and events subsequent to the date of the statement of financial position that require disclosure or adjustment to the audited financial statements.

2016 Business Strategy

The global economy remained soft in 2016. Issues faced by major regions varied with Europe coping with migration and UK-Brexit related issues, Middle East and North Africa region suffering from geopolitical risks and China facing an economic slowdown. This is heightened by the uncertainty related to potential policy changes, post completion of the US presidential election. Amidst the lackluster backdrop, the Malaysian economy registered a moderate growth of 4.2% in 2016 (2015: 5.0%). Malaysia's growth was supported by private sector demand, and additional support from net exports.

The Bank continued to demonstrate resilience and remained strong in both its liquidity and capital position in 2016 despite having to operate in an increasingly regulated banking landscape with expectation to always observe the highest global standards in all business transactions and processes. Its resilience is recognised by RAM Ratings Services Berhad, which has reaffirmed the Bank's long term and short term ratings of AAA and P1 ratings respectively. The Bank also continued to maintain its market leadership position in the sukuk issuance, evident by the numerous awards that the Bank won in 2016.

On the retail business, Retail Banking and Wealth Management (RBWM) focused on growing emerging affluent population, enhancing wealth management business, acquiring new-to-bank card customers and strengthening the financial crime compliance control. Premier proposition continued to be supported through various customer acquisition campaigns, new offering of wealth products and customer engagement framework, with additional investment spent to support development plan for relationship managers. Amidst increased competition, new cards issued grew year-on-year, driven by targeted acquisition campaigns and nationwide spent campaigns, including new Premier Travel Card. Card balance transfer process has been streamlined to support foreign currency businesses, via newly launched New Worldwide and In-house Transfer program.

2016 was a year where Malaysia experienced capital outflows (similar to other emerging markets) in response to global economic developments including US normalising its interest rate. During the year, especially towards 4Q2016, Ringgit weakened and bond yield increased, resulting in Bank Negara Malaysia introducing new controls on foreign exchange transactions to increase liquidity and depth of the onshore foreign exchange market. Global Banking & Markets (GBM) has worked closely with our corporate customers (both importers and exporters) to manage their exposure accordingly. EvolveFX, a dealing platform for foreign exchange sales and trading, was rolled out for better efficiency in capturing automated forex flows. GBM also took advantage of its debt capital market capabilities to secure key deals, enhance cross border connectivity, capture key growth opportunities in ASEAN and drive Renminbi (RMB) usage among our customers.

Commercial Banking (CMB) aims to position the Bank as the centre of excellence for Islamic cross-border deals including Global Trade and Receivables Finance (GTRF) trade re-financing opportunities in the Middle East and North Africa (MENA) region and collaborate with the International Subsidiary Banking (ISB) closely on realising the initiative. Growth was achieved in the top tier corporate customers segment, consisting of large local conglomerates, inbound ISBs and upper business banking clientele.

Performance Review 2016

2016 was a challenging year where the management's focus was on the control agenda. The Bank recorded a profit before tax of RM101.6 million for the financial year ended 31 December 2016, a decrease of 33.7% or RM51.5 million compared to previous year.

The bottom line was mainly impacted by higher impairment loses on financing (up RM54.4 million), lower income derived from investment of depositors' funds and others (down RM 32.2 million) but partially offset by higher income derived from investment of shareholder's funds (up RM13.6 million) and lower income attributable to depositors (down RM24.4 million).

Income derived from investment of depositors' funds and others decreased by RM32.2 million, mainly due to lower financing income (down RM37.8 million), but partially offset by higher trading income (up RM8.3 million). The lower net financing income was a result of a leaner customer financing portfolio size and continuous margin compression although at a decrease rate amid intense market competition. The downward revision of overnight policy rate (OPR) in July 2016 from 3.25% to 3.00% also impacted the net financing income.

Income derived from investment of shareholder's funds increased by RM13.6 million, mainly due to higher net gains on disposal of financial assets available-for-sale (up RM6.6 million) and higher net gains on fair-valued through profit or loss (up RM6.0 million) on financial instruments.

Impairment losses on financing increased by RM54.4 million arising mainly from higher collective impairment provision (up RM59.3 million) partially offset by lower individual impairment provision (down RM6.2 million).

The Bank continued to place high importance on the need to manage its operating expenses to ensure the resources are invested in a sustainable manner. In 2016, the Bank maintained its overall costs base. Savings recorded across personnel expenses, and establishment related expenses. Investments in compliance related costs increased in 2016, reflecting our commitment to invest in people and systems to detect, deter and protect the Bank against financial crime.

Total balance sheet size at 31 December 2016 stood at RM16.3 billion, RM3.0 billion lower compared against 31 December 2015 (RM19.3 billion). The Bank's capital and liquidity ratios continues to remain strong and well above regulatory requirements.

Outlook for 2017

Malaysia's real Gross Domestic Product (GDP) grew by 4.2% in 2016. Domestic demand and foreign direct investment in various infrastructure projects will be the key drivers of growth. Private consumption should moderate in 2017 after the implementation of the Goods and Services Tax (GST) in April 2015. The still low unemployment rate at a circa of 3.5% will support household spending.

Malaysia's oil sector and economy is expected to be boosted by the recent agreed Organisation of Petroleum Exporting Countries (OPEC) output cuts which would stabilise the demand-supply of the oil market. However, the country will remain vulnerable to external development such as slowdown in China, which is Malaysia's largest trading partner.

Inflation rate is projected to rise moderately in 2017 to 2.3%. To ensure healthy business activities, Bank Negara Malaysia (BNM) had on 13 July 2016, taken the pre-emptive step to reduce the OPR from 3.25% to 3.00%. This was kept unchanged during the January 2017 monetary policy meeting. Supported by strong capital buffers, the financial institutions will have the capacity to shoulder any adverse market development.

Ringgit continues to be driven by shifts in investor sentiments and the rebalancing activity of portfolio investors. Foreign exchange volatility will continue to be a major issue for emerging markets given the change in USD interest rate cycle, concern over further slowdown in China and uncertainties in the outlook for commodities market. The offshore value of Ringgit dropped to its lowest level in over a decade during November 2016, following Donald Trump's victory in the US presidential elections. BNM implemented new controls for foreign exchange transactions in December 2016 to promote onshore foreign exchange for Ringgit by offshore investors.

In the bond market, there was lower trading as investors traded cautiously amidst continued uncertainties over the timing of US interest rate normalisation, resulting in lower liquidity ratios across all bond segments. As foreign holdings of bonds remain high, trading activities are expected to continue in 2017 with domestic bond yields staying attractive after recent spike in yields.

Overall, while domestic conditions remain resilient, uncertainties in the external environment may pose downside risks to Malaysia's growth prospects. External events will continue to weigh heavily on investor sentiments and volatility in the domestic financial markets. These include increased uncertainty over policy adjustments and growth in the major economies, volatile commodity prices and uncertainties over the timing and developments in the United Kingdom (UK) post the European Union (EU) referendum. Domestic financial stability is nonetheless expected to be maintained.

As for the banking sector, challenges facing the industry include moderate loans growth, competition for deposits, weak capital market activities, potential rising credit costs, escalation of costs of doing business and compliance costs. Margin compression will continue given heightened competition within the banking industry.

Despite the challenges above, the increasing commitment towards the ASEAN Economic Community (AEC) amongst its members may fuel greater intra-ASEAN trade and investments flows. Usage of RMB for trade settlement may see a wider acceptance by both Malaysia and China corporates. Foreign direct investment from China is expected to increase in 2017 which may cushion the negative impact of lower international trade volume on the Malaysia economy. Inbound China investments are predominantly in infrastructure projects which lead to foreign exchange business opportunities. Hence, the Bank will continue to capitalise on infrastructure related opportunities, especially arising from Belt and Road Initiative where the focus is to capture opportunities along the entire supply chain as Chinese investment into Malaysia infrastructure is expected to be a key driver of growth.

For 2017, the Bank focus will be on expanding customer base and financing growth opportunities to increase market share.There are also opportunities for RBWM wealth management from diversification of client portfolio and rollovers of maturing structured investments in 2017.

Corporate social responsibility is also a key focus area which the Bank continues to put high emphasis on. During the year, the Bank continued to invest in the long term future of the community in which we operate by focusing on education, environmental and community development initiatives because we believe they provide the fundamental building blocks to driving economic development, helping to create thriving communities. The Bank endeavours to continue to contribute towards changing people's lives and the environment they live in for the better, and encourages active participation from our colleagues in all corporate sustainability initiatives. Being sustainable means building our business for the long term by living up to these responsibilities, and bringing us to HSBC's vision in becoming the world's leading international bank.

Awards won during the financial year

1. **Best Local Currency Sukuk** - Cagamas 500 million ringgit Murabahah Sukuk, HSBC acted as one of the Shariah advisers, The Asset Triple A Islamic Finance Awards 2016

2. **Best Project Finance Deal -** Jimah East Power 8.98 billion ringgit Murabahah Sukuk, HSBC acted as one of the Joint Lead Arranger, Shariah adviser and Joint Bookrunner and Lead Manager, The Asset Triple A Islamic Finance Awards 2016

3. **Best Loan Syndication -** SapuraKencana TMC US$2.1 billion equivalent syndicated Murabahah term financing facility, HSBC has acted as one of the mandated Lead Arrangers, The Asset Triple A Islamic Finance Awards 2016

4. **Best Sovereign Sukuk -** Government of Malaysia US$1.5 billion 10-year and 30-year Wakalah and Murabahah Sukuk, HSBC acted as one of the Joint Bookrunners and Joint Shariah advisers, The Asset Triple A Islamic Finance Awards 2016

5. **Best Sukuk -** Government of Malaysia US$1.5 billion 10-year and 30-year Wakalah and Murabahah Sukuk**,** HSBC acted as one of the Joint Bookrunners and Joint Shariah advisers, The Asset Triple A Islamic Finance Awards 2016

6. **Best Quasi-Sovereign Sukuk -** Petronas - US$1.25 billion Wakalah Sukuk, HSBC acted as one of the passive Joint Bookrunners, The Asset Triple A Islamic Finance Awards 2016

7. **Best Deal - China**, Country Garden Real Estate 115 million ringgit Sukuk, HSBC acted as one of the Joint Lead Managers, The Asset Triple A Islamic Finance Awards 2016

8. **Best Deal - Malaysia**, Government of Malaysia US$1.5 billion 10-year and 30-year Wakalah and Murabahah Sukuk, HSBC acted as one of the Joint Bookrunners and Joint Shariah advisers, The Asset Triple A Islamic Finance Awards 2016

9. **Innovation in Islamic Finance -** Government of Malaysia US$1.5 billion 10-year and 30-year Wakalah and Murabahah Sukuk, HSBC acted as one of the Joint Bookrunners and Joint Shariah advisers, Euromoney Awards for Innovation in Islamic Finance 2016

10. **Best Foreign Currency Bond Deal of the Year 2016 in Southeast Asia –** TNB Global Ventures Capital's US$750 million Sukuk Wakalah, HSBC acted as Joint Lead Managers and Joint Bookrunners, 10th Alpha Southeast Asia Deal & Sccolution Awards 2016

11. **Best Sovereign Bond Deal of the Year 2016 in Southeast Asia –** Republic of Malaysia's US$1.5 billion Global Islamic Sukuk, HSBC acted as Joint Lead Managers and Joint Bookrunners, 10th Alpha Southeast Asia Deal & Solution Awards 2016

Directors and their Interests in Shares

The names of the Directors of the Bank in office since the date of the last report and at the date of this report are:

- Dr. Mohamed Ashraf bin Mohamed Iqbal
- Louisa Cheang Wai Wan
- Mukhtar Malik Hussain
- Adil Ahmad
- Azlan bin Abdullah
- Lee Choo Hock *(appointed on 30 May 2016)*
- Albert Quah Chei Jin *(appointed on 5 September 2016)*
- Mohamed Ross bin Mohd Din *(retired on 13 April 2016)*
- Seow Yoo Lin *(resigned on 14 March 2016)*

In accordance with Articles 73 of the Articles of Association, all Directors shall retire from the Board at the forthcoming Annual General Meeting and, being eligible, offers themselves for re-election.

The interests and deemed interests in the shares and options over shares of the Bank of those who were Directors at financial year end (including the interests of the spouses or children of the Directors who themselves are not Directors of the Bank) as recorded in the Register of Directors' Shareholdings are as follows:

	Number of Shares			
	Balance at 1.1.2016	Bought	Sold	Balance at 31.12.2016
HSBC Holdings plc				
Ordinary Shares				
Mukhtar Malik Hussain	1,219,379	90,287	(69,090)	1,240,576
Louisa Cheang Wai Wan	87,847	-	(40,156)	47,691
Adil Ahmad	-	3,200	-	3,200

	Number of Shares			
	Balance at 1.1.2016	Shares issued during the year [1]	Shares vested during the year	Balance at 31.12.2016
HSBC Holdings plc				
HSBC Share Plan				
Mukhtar Malik Hussain	341,647	156,626	(99,736)	398,537

[1] *Includes scrip dividends*

None of the other Directors holding office at 31 December 2016 had any interest in the ordinary shares and options of the Bank and of its related corporations during the financial year.

Directors' Benefits

Since the end of the previous financial year, no Director of the Bank has received or become entitled to receive any benefit (other than a benefit included in the aggregate amount of emoluments received or due and receivable by Directors as shown in the financial statements or the fixed salary of a full-time employee of the Bank or of a related company) by reason of a contract made by the Bank or a related corporation with the Director or with a firm of which the Director is a member, or with a company in which the Director has a substantial financial interest.

There were no arrangements during the financial year which any Directors might acquire benefits by means of the acquisition of shares in, or debentures of, the Bank or any other body corporate, except for:

(i) Directors who were granted the option to subscribe for shares in the ultimate holding company, HSBC Holdings plc, under Executive/Savings-Related Share Option Schemes at prices and terms as determined by the schemes, and

(ii) Directors who were conditionally awarded shares of the ultimate holding company, HSBC Holdings plc, under its Restricted Share Plan/HSBC Share Plan.

Immediate and Ultimate Holding Company

The Directors regard HSBC Bank Malaysia Berhad, a company incorporated in Malaysia, and HSBC Holdings plc, a company incorporated in England, as the immediate and ultimate holding companies of the Bank respectively.

Zakat Obligation

The Bank is not obliged to pay zakat for the financial year ended 31 December 2016.

Auditors

The financial statements for the financial year ended 31 December 2016 have been audited by PricewaterhouseCoopers (PwC). A resolution to re-appoint PwC as auditors of the Bank will be proposed at the forthcoming Annual General Meeting.

Signed on behalf of the Directors in accordance with a resolution of the Directors:

……………………..……………………..…..…

MUKHTAR MALIK HUSSAIN
Director

……………………..……………………..…..…

ALBERT QUAH CHEI JIN
Director

Kuala Lumpur, Malaysia
07 February 2017

DIRECTORS' STATEMENT

In the opinion of the directors:

We, Mukhtar Malik Hussain and Albert Quah Chei Jin, being two of the Directors of HSBC Amanah Malaysia Berhad, do hereby state on behalf of the Directors that, in our opinion, the financial statements set out on pages 33 to 124 are drawn up in accordance with Malaysian Financial Reporting Standards, International Financial Reporting Standards and the requirements of the Companies Act, 1965 in Malaysia so as to give a true and fair view of the financial position of the Bank as at 31 December 2016 and of the financial performance and cash flows of the Bank for the financial year then ended.

Signed at Kuala Lumpur, Malaysia this 07 February 2017.

Signed on behalf of the Board of Directors in accordance with a resolution of the Directors:

…………….…………………………………
MUKHTAR MALIK HUSSAIN
Director

…………………….…………………..…..….
ALBERT QUAH CHEI JIN
Director

HSBC AMANAH MALAYSIA BERHAD
(Company No 807705-X)
(Incorporated in Malaysia)

STATUTORY DECLARATION

I, Neoh Elly, being the officer primarily responsible for the financial management of HSBC Amanah Malaysia Berhad, do solemnly and sincerely declare that, to the best of my knowledge and belief, the financial statements set out on pages 33 to 124 are correct, and I make this solemn declaration conscientiously believing the same to be true, and by virtue of the provisions of the Statutory Declarations Act 1960.

Subscribed and solemnly declared by the above named.

in Kuala Lumpur, Malaysia on 07 February 2017.

....
NEOH ELLY

BEFORE ME:

…………………………………………….
Signature of Commissioner for Oaths

SHARIAH COMMITTEE'S REPORT

In the name of Allah, the most Beneficent, the most Merciful.

Praise to Allah, the Lord of the Worlds and peace and blessings be upon our Prophet Muhammad, his family and companions.

Assalamu 'Alaikum Warahmatullahi Wabarakatuh

In carrying out the roles and responsibilities as Shariah Committee of HSBC Amanah Malaysia Berhad as prescribed in the Shariah Governance Framework for Islamic Financial Institutions issued by Bank Negara Malaysia, the Bank's Shariah Governance Policy as well as the Bank's Committee's Terms of Reference, we hereby submit the following report for the financial year ended 31 December 2016:

1. We have conducted nine (9) meetings for the whole year of 2016 and reviewed the principles and the contracts relating to the transactions and applications introduced by the Bank during the financial year ended 31 December 2016 to ensure conformity with Shariah requirements.

2. We have performed oversight role through the Shariah review and Shariah audit functions in ensuring the Bank has complied with the Shariah principles and rulings issued by us and the Shariah Advisory Council of Bank Negara Malaysia.

3. The management of the Bank is responsible for ensuring that the financial institution conducts its business in accordance with Shariah principles. It is our responsibility to form an independent opinion, based on our review of the operations of the Bank, and to report to you.

4. We have assessed the work carried out by Shariah Department and its effectiveness to implement the Shariah Governance Framework which included pre and post examination, on a test basis, each type of transaction across business lines, the relevant documentations and procedures adopted and/or entered into by the Bank.

5. In performing our duties, we planned and performed our review and had obtained all the information and explanations which we considered indispensable and necessary in order to provide us with satisfactory evidence to arrive at sound Shariah decisions and to give reasonable assurance that the Bank has complied with Shariah requirements and has not violated the Shariah rules and principles based on the evidences which have been disclosed and tabulated before us.

On that note, we, being the members of the Shariah Committee of HSBC Amanah Malaysia Berhad, do hereby confirm that, with the exception of identified breaches that are being remedied, in our opinion:

(a) the contracts, transactions, dealings entered into by the Bank during the financial year ended 31 December 2016 have been reviewed by us and are in compliance with Shariah rules and principles;

(b) the allocation of profit and charging of losses relating to the Bank's assets and liabilities conform to the basis that had been approved by us in accordance with Shariah principles;

(c) all earnings that have been realised from sources or by means prohibited by the Shariah principles have been considered for disposal to charitable causes; and

(d) the Bank is not required to pay zakat for the financial year ended 31 December 2016 because its shareholder has no obligation to pay zakat.

SHARIAH COMMITTEE'S REPORT (Cont'd)

We, the members of the Shariah Committee of HSBC Amanah Malaysia Berhad, do hereby confirm that with the exception of identified breaches that are being remedied, the operations of the Bank for the financial year ended 31 December 2016 have been conducted in conformity with the Shariah principles.

We pray to Allah the Almighty to grant us success and the path of straight forwardness.

Wassalamu 'Alaikum Warahmatullahi Wabarakatuh

Chairman of the Shariah Committee ……………………………………………
Assoc. Prof Dr Younes Soualhi (Chairman until 7 Feb 2017)

Member of the Shariah Committee ……………………………………………
Assoc. Prof. Dr. Muhammad Yusuf Saleem Ghulam Nabi

Member of the Shariah Committee ……………………………………………
Khairul Anuar Ahmad

Member of the Shariah Committee ……………………………………………
Prof. Dr. Abdul Rahim Abdul Rahman

Member of the Shariah Committee ……………………………………………
Prof. Dr. Obiyathulla Ismath Bacha

Kuala Lumpur, Malaysia 07 February 2017

INDEPENDENT AUDITORS' REPORT
TO THE MEMBER OF HSBC AMANAH MALAYSIA BERHAD
(Incorporated in Malaysia)
(Company No. 807705-X)

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS

Our opinion

In our opinion, the financial statements of HSBC Amanah Malaysia Berhad ("the Bank") give a true and fair view of the financial position of the Bank as at 31 December 2016 and of its financial performance and its cash flows for the year then ended in accordance with Malaysian Financial Reporting Standards, International Financial Reporting Standards and the requirements of the Companies Act, 1965 in Malaysia.

What we have audited

We have audited the financial statements of the Bank, which comprise the statement of financial position as at 31 December 2016, the statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, as set out on pages 33 to 124.

Basis for opinion

We conducted our audit in accordance with approved standards on auditing in Malaysia and International Standards on Auditing. Our responsibilities under those standards are further described in the "Auditors' responsibilities for the audit of the financial statements" section of our report.

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

Independence and other ethical responsibilities

We are independent of the Bank in accordance with the By-Laws (on Professional Ethics, Conduct and Practice) of the Malaysian Institute of Accountants ("By-Laws") and the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants ("IESBA Code"), and we have fulfilled our other ethical responsibilities in accordance with the By-Laws and the IESBA Code.

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS (Cont'd)

Information other than the financial statements and auditors' report thereon

The directors of the Bank are responsible for the other information. The other information comprises the list of the Board of Directors, Corporate Governance Disclosures, Internal Control Framework, Rating by External Rating Agencies, Directors' Report and Shariah Committee's Report, but does not include the financial statements of the Bank and our auditors' report thereon.

Our opinion on the financial statements of the Bank does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements of the Bank, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements of the Bank or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the directors for the financial statements

The directors of the Bank are responsible for the preparation of the financial statements of the Bank that give a true and fair view in accordance with Malaysian Financial Reporting Standards, International Financial Reporting Standards and the requirements of the Companies Act, 1965 in Malaysia. The directors are also responsible for such internal control as the directors determine is necessary to enable the preparation of financial statements of the Bank that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements of the Bank, the directors are responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

INDEPENDENT AUDITORS' REPORT
TO THE MEMBER OF HSBC AMANAH MALAYSIA BERHAD
(Incorporated in Malaysia)
(Company No 807705-X)

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS (Cont'd)

Auditors' responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements of the Bank as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with approved standards on auditing in Malaysia and International Standards on Auditing will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with approved standards on auditing in Malaysia and International Standards on Auditing, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

(a) Identify and assess the risks of material misstatement of the financial statements of the Bank, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

(b) Obtain an understanding of internal control relevant to the audit 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 Bank's internal control.

(c) Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.

(d) Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements of the Bank or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Bank to cease to continue as a going concern.

(e) Evaluate the overall presentation, structure and content of the financial statements of the Bank, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

INDEPENDENT AUDITORS' REPORT
TO THE MEMBER OF HSBC AMANAH MALAYSIA BERHAD
(Incorporated in Malaysia)
(Company No 807705-X)

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS (Cont'd)

Auditors' responsibilities for the audit of the financial statements (continued)

We communicate with the directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

In accordance with the requirements of the Companies Act, 1965 in Malaysia, we also report that, in our opinion, the accounting and other records and the registers required by the Act to be kept by the Bank have been properly kept in accordance with the provisions of the Act.

OTHER MATTERS

This report is made solely to the members of the Bank, as a body, in accordance with Section 174 of the Companies Act, 1965 in Malaysia and for no other purpose. We do not assume responsibility to any other person for the content of this report.

PRICEWATERHOUSECOOPERS
(No. AF: 1146)
Chartered Accountants

SOO HOO KHOON YEAN
2682/10/17(J)
Chartered Accountant

Date: 13 February 2017

Kuala Lumpur

HSBC AMANAH MALAYSIA BERHAD
(Company No. 807705-X)
(Incorporated in Malaysia)

STATEMENT OF FINANCIAL POSITION AT 31 DECEMBER 2016

	Note	**31 Dec 2016 RM'000**	31 Dec 2015 RM'000
Assets			
Cash and short-term funds	*6*	**2,359,591**	4,750,390
Financial assets held-for-trading	*7*	**488**	10,492
Financial investments available-for-sale	*8*	**1,368,574**	1,701,243
Financing and advances	*9*	**11,743,263**	11,968,217
Derivative financial assets	*11*	**395,748**	307,299
Other assets	*12*	**80,041**	241,611
Statutory deposits with Bank Negara Malaysia	*13*	**325,462**	329,662
Equipment	*14*	**7,237**	10,288
Deferred tax assets	*16*	**10,395**	5,548
Tax recoverable	*17*	**10,285**	5,162
Total assets		**16,301,084**	19,329,912
Liabilities			
Deposits from customers	*18*	**8,726,543**	9,386,123
Deposits and placements from banks and other financial institutions	*19*	**1,951,602**	4,160,089
Bills and acceptances payable		**23,632**	14,904
Derivative financial liabilities	*11*	**490,755**	473,231
Other liabilities	*20*	**1,185,135**	1,475,375
Multi-Currency Sukuk Programme	*21*	**1,756,001**	1,749,823
Subordinated Commodity Murabahah Financing	*22*	**646,265**	618,461
Total liabilities		**14,779,933**	17,878,006
Equity			
Share capital	*23*	**50,000**	50,000
Reserves	*24*	**1,471,151**	1,401,906
Total equity attributable to owner of the Bank		**1,521,151**	1,451,906
Total liabilities and equity		**16,301,084**	19,329,912
Restricted investment accounts [1]		**2,230,065**	2,632,404
Total Islamic Banking asset [1]		**18,531,149**	21,962,316
Commitments and Contingencies	*35*	**22,149,853**	21,889,668

[1] The disclosure is in accordance with the requirements of Bank Negara Malaysia's Guideline on Financial Reporting for Islamic Banking Institutions dated 5 February 2016.

The accompanying notes form an integral part of the financial statements.

HSBC AMANAH MALAYSIA BERHAD
(Company No. 807705-X)
(Incorporated in Malaysia)

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2016

	Note	**31 Dec 2016 RM'000**	31 Dec 2015 RM'000 (Restated)
Income derived from investment of depositors' funds and others	*25*	**686,267**	718,486
Income derived from investment of shareholder's funds	*26*	**136,729**	123,144
Impairment losses on financing	*27*	**(136,865)**	(82,487)
Total distributable income		**686,131**	759,143
Income attributable to depositors	*28*	**(351,148)**	(375,509)
Total net income		**334,983**	383,634
Operating expenses	*29*	**(233,359)**	(230,473)
Profit before tax		**101,624**	153,161
Tax expense	*30*	**(20,231)**	(31,099)
Profit for the financial year		**81,393**	122,062
Other comprehensive income/(expense)			
Items that will subsequently be reclassified to profit or loss when specific conditions are met:			
Available-for-sale reserve:			
Change in fair value		**(8,268)**	15,276
Amount transferred to profit or loss		**(6,854)**	(232)
Income tax effect		**3,629**	(3,610)
Other comprehensive income for the financial year, net of tax		**(11,493)**	11,434
Total comprehensive income for the financial year		**69,900**	133,496
Profit attributable to the owner of the Bank		**81,393**	122,062
Total comprehensive income attributable to the owner of the Bank		**69,900**	133,496
Basic earnings per RM0.50 ordinary share		**81.4 sen**	122.1 sen

The accompanying notes form an integral part of the financial statements.

HSBC AMANAH MALAYSIA BERHAD
(Company No. 807705-X)
(Incorporated in Malaysia)

STATEMENT OF CHANGES IN EQUITY FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2016

	Non-distributable						*Distributable*	
	Share capital	*Share premium*	*Statutory reserve*	*Available-for-sale reserve*	*Capital contribution reserve*	*Regulatory reserve* [1]	*Retained profits*	*Total*
	RM'000	**RM'000**	**RM'000**	**RM'000**	**RM'000**	**RM'000**	**RM'000**	**RM'000**
2016								
Balance at 1 January	**50,000**	**610,000**	**50,000**	**4,946**	**1,058**	**34,000**	**701,902**	**1,451,906**
Total comprehensive income for the financial year								
Profit for the financial year	**-**	**-**	**-**	**-**	**-**	**-**	**81,393**	**81,393**
Other comprehensive income, net of tax								
Available-for-sale reserve:								
Net change in fair value	**-**	**-**	**-**	**(6,284)**	**-**	**-**	**-**	**(6,284)**
Net amount transferred to profit or loss	**-**	**-**	**-**	**(5,209)**	**-**	**-**	**-**	**(5,209)**
Total other comprehensive income	**-**	**-**	**-**	***(11,493)***	**-**	**-**	**-**	***(11,493)***
Total comprehensive income for the financial year	**-**	**-**	**-**	**(11,493)**	**-**	**-**	**81,393**	**69,900**
Transactions with the owner, recorded directly in equity								
Share based payment transactions	**-**	**-**	**-**	**-**	**(655)**	**-**	**-**	**(655)**
Balance at 31 December	**50,000**	**610,000**	**50,000**	**(6,547)**	**403**	**34,000**	**783,295**	**1,521,151**

[1] The Bank maintains a regulatory reserve to meet local regulatory requirements; the effect of this requirement is to restrict the amount of reserves that can be distributed to shareholders.

The accompanying notes form an integral part of the financial statements.

HSBC AMANAH MALAYSIA BERHAD
(Company No. 807705-X)
(Incorporated in Malaysia)

STATEMENT OF CHANGES IN EQUITY FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2016 (Cont'd)

	Non-distributable						*Distributable*	
	Share capital	*Share premium*	*Statutory reserve*	*Available-for-sale reserve*	*Capital contribution reserve*	*Regulatory reserve* [1]	*Retained profits*	*Total*
	RM'000	**RM'000**	**RM'000**	**RM'000**	**RM'000**	**RM'000**	**RM'000**	**RM'000**
2015								
Balance at 1 January	50,000	610,000	50,000	(6,488)	1,374	13,000	600,823	1,318,709
Total comprehensive income for the financial year								
Profit for the financial year	-	-	-	-	-	-	122,062	122,062
Other comprehensive income, net of tax								
Available-for-sale reserve:								
Net change in fair value	-	-	-	11,610	-	-	-	11,610
Net amount transferred to profit or loss	-	-	-	(176)	-	-	-	(176)
Total other comprehensive income	-	-	-	*11,434*	-	-	-	*11,434*
Total comprehensive income for the financial year	-	-	-	11,434	-	-	122,062	133,496
Transactions with the owner, recorded directly in equity								
Share based payment transactions	-	-	-	-	(316)	-	17	(299)
Transfer relating to regulatory reserves	-	-	-	-	-	21,000	(21,000)	-
Balance at 31 December	50,000	610,000	50,000	4,946	1,058	34,000	701,902	1,451,906

[1] The Bank maintains a regulatory reserve to meet local regulatory requirements; the effect of this requirement is to restrict the amount of reserves that can be distributed to shareholders.

The accompanying notes form an integral part of the financial statements.

HSBC AMANAH MALAYSIA BERHAD
(Company No. 807705-X)
(Incorporated in Malaysia)

STATEMENT OF CASH FLOWS FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2016

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Cash Flows from Operating Activities		
Profit before income tax expense	**101,624**	153,161
Adjustments for:		
Unrealised gains on revaluation of financial assets held-for-trading	**(496)**	(2,519)
Unrealised losses from dealing in foreign currency	**5,853**	12,060
Unrealised losses on revaluation of derivatives	**623**	15,827
Allowance for impairment losses on financing	**168,730**	114,716
Share based payment transactions	**(589)**	365
Depreciation of equipment	**5,029**	7,106
Amortisation of intangible assets	**-**	2
Unrealised losses on revaluation of subordinated commodity murabahah financing	**27,804**	96,526
Unrealised losses/(gains) on financial instruments fair value through profit or loss	**6,178**	(2,031)
Operating profit before changes in operating assets and liabilities	**314,756**	395,213
Decrease/(Increase) in operating assets		
Financial assets held-for-trading	**10,500**	12,082
Financing and advances	**56,224**	(1,402,395)
Derivative financial assets	**(94,925)**	(211,344)
Other assets	**155,181**	(24,023)
Statutory deposits with Bank Negara Malaysia	**4,200**	149,400
Total Decrease/(Increase) in operating assets	**131,180**	(1,476,280)
(Decrease)/Increase in operating liabilities		
Deposits from customers	**(659,580)**	(1,590,058)
Deposits and placements from banks and other financial institutions	**(2,208,487)**	1,658,336
Bills and acceptances payable	**8,728**	(10,805)
Derivative financial liabilities	**17,524**	345,614
Other liabilities	**(204,201)**	1,381,959
Total (Decrease)/Increase in operating liabilities	**(3,046,016)**	1,785,046
Net cash (used in)/generated from operating activities	**(2,600,080)**	703,979
Income tax paid	**(26,659)**	(28,802)
Net cash (used in)/generated from operating activities	**(2,626,739)**	675,177

The accompanying notes form an integral part of the financial statements.

HSBC AMANAH MALAYSIA BERHAD
(Company No. 807705-X)
(Incorporated in Malaysia)

STATEMENT OF CASH FLOWS FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2016 (Cont'd)

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Cash Flows from Investing Activities		
Purchase of financial assets available-for-sale	**(651,495)**	(1,588,287)
Proceeds from disposal of financial assets available-for-sale	**975,431**	4,059,155
Purchase of equipment	**(1,978)**	(1,224)
Net cash generated from investing activities	**321,958**	2,469,644
Cash Flows from Financing Activities		
Proceeds from multi-currency sukuk programme	**-**	750,000
Proceeds from subordinated commodity murabahah financing	**-**	250,299
Profit paid on multi-currency sukuk programme	**(69,378)**	(54,823)
Profit paid on subordinated commodity murabahah financing	**(16,640)**	(10,841)
Net cash (used in)/generated from financing activities	**(86,018)**	934,635
Net (decrease)/increase in Cash and Cash Equivalents	**(2,390,799)**	4,079,456
Cash and Cash Equivalents at beginning of the financial year	**4,750,390**	670,934
Cash and Cash Equivalents at end of the financial year	**2,359,591**	4,750,390
Analysis of Cash and Cash Equivalents		
Cash and short-term funds	**2,359,591**	4,750,390

The accompanying notes form an integral part of the financial statements.

HSBC AMANAH MALAYSIA BERHAD
(Company No. 807705-X)
(Incorporated in Malaysia)

NOTES TO THE FINANCIAL STATEMENTS

1 General Information

HSBC Amanah Malaysia Berhad (the Bank) is a licensed Islamic Bank under the Islamic Financial Services Act, 2013. The principal activities of the Bank are Islamic banking and related financial services.

There were no significant changes in these activities during the financial year.

The Bank is a public limited liability company, incorporated and domiciled in Malaysia. The registered office of the Bank is located at 2, Leboh Ampang, 50100 Kuala Lumpur.

The immediate parent bank and ultimate holding company during the financial year are HSBC Bank Malaysia Berhad (HBMY) and HSBC Holdings Plc, respectively.

The financial statements were approved and authorised for issue by the Board of Directors on 7 February 2017.

2 Basis of Preparation

(a) Statement of compliance

The financial statements of the Bank have been prepared in accordance with the requirements of Malaysian Financial Reporting Standards (MFRS), International Financial Reporting Standards, the requirements of the Companies Act, 1965 in Malaysia and BNM requirements on Shariah related disclosures.

(i) Standards and amendments to published standards that are effective

The new accounting standards and amendments to published accounts that are effective and applicable to the Bank for the financial year beginning on 1 January 2016 are as follows:

- Amendments to MFRS 127 'Separate Financial Statements'. The amendments introduced equity accounting for separate financial statements.

- MFRS 101 'Presentation of Financial Statements' - Disclosure Initiative (Amendments to MFRS 101). The amendments are part of a major initiative to improve disclosure requirements in MFRS financial statements. These amendments include narrow - focus improvements in five areas as follows:
    - Materiality
    - Disaggregation and subtotals
    - Notes structure
    - Disclosure of accounting policies
    - Presentation of items in Other Comprehensive Income (OCI) arising from equity accounted investments.

- Amendments to MFRS 11 'Joint arrangements'. The amendments introduced accounting for acquisition of interest in joint operations.

- Amendments to MFRS 10, 12 & 128 'Investment entities'. The amendments introduced application of consolidation exception.

- Annual improvement to MFRSs 2012 - 2014 Cycle
    - Amendment to MFRS 5, 'Non-current assets Held for Sale and Discontinued Operations'
    - Amendment to MFRS 7, 'Financial Instruments: Disclosure - Servicing contracts'
    - Amendment to MFRS 7, 'Financial Instruments: Disclosure - Applicability of the amendments to MFRS 7 to condensed interim financial statements'
    - Amendment to MFRS 119, 'Employee Benefits'
    - Amendments to MFRS 134, 'Interim Financial Reporting'

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

2 Basis of Preparation (Cont'd)

(a) Statement of compliance (Cont'd)

(i) Standards and amendments to published standards that are effective (Cont'd)

The adoption of the new accounting standards, amendments and improvements to published standards are not expected to have impact on the financial statements of the Bank on the current period or any prior period and is not likely to affect the future periods.

(ii) Standards, amendments to published standards and interpretations to existing standards have been issued but not yet effective

The Bank will apply these standards, amendments to published standards from:

a. Financial year beginning on/after 1 January 2017:

- Amendments to MFRS 107 'Statement of Cash Flows - Disclosure Initiative'

  Disclosure Initiative introduces additional on changes in liabilities arising from financing activities.

- Amendments to MFRS 112 'Recognition on Deferred Tax Assets For Unrealised Losses'

  Amendments to MFRS 112 clarify the requirements for recognising deferred tax assets on unrealised losses arising from deductible temporary difference on asset carried at fair value.

  In addition, in evaluating whether an entity will have sufficient taxable profits in future periods against which deductible temporary differences can be utilised, the amendments require an entity to compare the deductible temporary differences with future taxable profits that excludes tax deductions resulting from the reversal of those temporary differences.

  The amendments shall be applied retrospectively.

b. Financial year beginning on/ after 1 January 2018:

- Amendments to MFRS 140 'Classification on 'Change in Use' – Assets transferred to, or from, Investment Properties' clarify that to transfer to, or from investment properties there must be a change in use. A change in use would involve an assessment of whether a property meet, or has ceased to meet, the definition of investment property. The change must be supported by evidence that the change in use has occurred and a change in management's intention in isolation is not sufficient to support a transfer of property.

  The amendments also clarify the same principle applies to assets under construction.

- IC Interpretation 22 'Foreign Currency Transactions and Advance Consideration' applies when an entity recognises a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration. MFRS 121 requires an entity to use the exchange rate at the 'date of the transaction' to record foreign currency transactions.

  IC Interpretation 22 provides guidance how to determine 'the date of transaction' when a single payment/receipt is made, as well as for situations where multiple payments/receipts are made.

  The date of transaction is the date when the payment or receipt of advance consideration gives rise to the non-monetary asset or non-monetary liability when the entity is no longer exposed to foreign exchange risk.

  If there are multiple payments or receipts in advance, the entity should determine the date of the transaction for each payment or receipt.

  An entity has the option to apply IC Interpretation 22 retrospectively or prospectively.

2 Basis of Preparation (Cont'd)

(a) Statement of compliance (Cont'd)

(ii) Standards, amendments to published standards and interpretations to existing standards have been issued but not yet effective (Cont'd)

b. Financial year beginning on/ after 1 January 2018 (Cont'd):

- MFRS 9 'Financial Instruments' will replace MFRS 139 'Financial Instruments: Recognition and Measurement'.

  MFRS 9 retains but simplifies the mixed measurement model in MFRS 139 and establishes three primary measurement categories for financial assets: amortised cost, fair value through profit or loss and fair value through OCI. The basis of classification depends on the entity's business model and the cash flow characteristics of the financial asset. Investments in equity instruments are always measured at fair value through profit or loss with an irrevocable option at inception to present changes in fair value in OCI (provided the instrument is not held for trading). A debt instrument is measured at amortised cost only if the entity is holding it to collect contractual cash flows and the cash flows represent principal and profit.

  For liabilities, the standard retains most of the MFRS 139 requirements. These include amortised cost accounting for most financial liabilities, with bifurcation of embedded derivatives. The main change is that, in cases where the fair value option is taken for financial liabilities, the part of a fair value change due to an entity's own credit risk is recorded in other comprehensive income rather than the profit or loss, unless this creates an accounting mismatch.

  MFRS 9 introduces an expected credit loss model on impairment for all financial assets that replaces the incurred loss impairment model used in MFRS 139. The expected credit loss model is forward-looking and eliminates the need for a trigger event to have occurred before credit losses are recognised.

- MFRS 15 'Revenue from contracts with customers' replaces MFRS 118 'Revenue' and MFRS 111 'Construction contracts' and related interpretations. The core principle in MFRS 15 is that an entity recognises revenue to depict the transfer of promised goods or services to the customer in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

  Revenue is recognised when a customer obtains control of goods or services, i.e. when the customer has the ability to direct the use of and obtain the benefits from the goods or services.

  A new five-step process is applied before revenue can be recognised:

  - Identify contracts with customers
  - Identify the separate performance obligations
  - Determine the transaction price of the contract;
  - Allocate the transaction price to each of the separate performance obligations; and
  - Recognise the revenue as each performance obligation is satisfied.

  Key provisions of the new standard are as follows:

  - Any bundled goods or services that are distinct must be separately recognised, and any discounts or rebates on the contract price must generally be allocated to the separate elements.
  - If the consideration varies (such as for incentives, rebates, performance fees, royalties, success of an outcome etc.), minimum amounts of revenue must be recognised if they are not at significant risk of reversal.
  - The point at which revenue is able to be recognised may shift: some revenue which is currently recognised at a point in time at the end of a contract may have to be recognised over the contract term and vice versa.
  - There are new specific rules on licenses, warranties, non-refundable upfront fees, and consignment arrangements, to name a few.
  - As with any new standard, there are also increased disclosures.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

2 Basis of Preparation (Cont'd)

(a) Statement of compliance (Cont'd)

(ii) Standards, amendments to published standards and interpretations to existing standards have been issued but not yet effective (Cont'd)

c. Financial year beginning on/after 1 January 2019:

- MFRS 16 'Leases'

  MFRS 16 'Leases' supersedes MFRS 117 'Leases' and the related interpretations.

  Under MFRS 16, a lease is a contract (or part of a contract) that conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

  MFRS 16 eliminates the classification of leases by the lessee as either finance leases (on balance sheet) or operating leases (off balance sheet). MFRS 16 requires a lessee to recognise a "right-of-use" of the underlying asset and a lease liability reflecting future lease payments for most leases.

  The right-of-use asset is depreciated in accordance with the principle in MFRS 116 'Property, Plant and Equipment' and the lease liability is accreted over time with profit expense recognised in the income statement.

  For lessors, MFRS 16 retains most of the requirements in MFRS 117. Lessors continue to classify all leases as either operating leases or finance leases and account for them differently.

The initial application of the above accounting standards, amendments and interpretation are not expected to have any material financial impacts to the current and prior year's financial statement of the Bank upon its first adoption, except for MFRS 9.

MFRS 9 replaces the guidance in MFRS 139 'Financial Instruments, Recognition and Measurement' on the classification and measurement of financial assets and financial liabilities, and on hedge accounting. The Bank is currently assessing the financial impact that may arise from the adoption of MFRS 9.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

2 Basis of Preparation (Cont'd)

(b) Basis of measurement

The financial statements of the Bank have been prepared on the historical cost basis, except for the following assets and liabilities as explained in their respective accounting policy notes:

- Trading assets and liabilities
- Financial investments
- Derivatives and hedge accounting

(c) Functional and presentation currency

These financial statements are presented in Ringgit Malaysia (RM), which is the Bank's functional currency. All financial information presented in RM has been rounded to the nearest thousand, unless otherwise stated.

(d) Use of estimates and judgments

The results of the Bank are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of the financial statements. The significant accounting policies are described in Note 3 on the financial statements. The preparation of the financial statements in conformity with MFRSs requires management to make estimates and assumptions about future conditions. The use of available information and the application of judgment are inherent in the formation of estimates; actual results in the future may differ from estimates upon which financial information is prepared.

Management believes that the Bank's critical accounting policies where judgment is necessarily applied are those which relate to impairment of financing and advances and the valuation of financial instruments (see Note 5). There are no other significant areas of estimation uncertainty and critical judgments in applying accounting policies that have significant effect on the amounts recognised in the financial statements other than those disclosed above.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

3 Significant Accounting Policies

The accounting policies set out below have been applied consistently to the periods presented in these financial statements and have been applied consistently by the Bank.

(a) Foreign Currencies

Transactions in foreign currencies are translated to the functional currency at exchange rates at the dates of the transactions.

Monetary assets and liabilities denominated in foreign currencies at the reporting period are retranslated to the functional currency at the exchange rate at that date.

Non-monetary assets and liabilities denominated in foreign currencies are not retranslated at the end of the reporting date except for those that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined.

Foreign currency differences arising on retranslation are recognised in profit or loss, except for differences arising on the retranslation of available-for-sale equity instruments or a financial instrument designated as a hedge of currency risk, which are recognised in other comprehensive income.

(b) Financing Income and Expenses

Financing income and expenses for all financial instruments of the Bank, except those classified as held-for-trading, are recognised within 'finance income' and 'income attributable to deposits' in the profit or loss on an accrual basis using the effective profit rate method in accordance with the principles of Shariah.

The effective profit rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability, or where appropriate, a shorter period, to the net carrying amount of the financial asset or liability. When calculating the effective profit rate, the Bank estimates cash flows considering all contractual terms of the financial instrument but not future credit losses.

The calculation includes all amounts paid or received by the Bank that are an integral part of the effective profit rate, including transaction costs and all other premiums or discounts.

Profit on impaired financial assets of the Bank is recognised using the rate of profit used to discount the future cash flows for the purpose of measuring the impairment loss.

i) <u>Murabahah</u>
Income is recognised on effective profit rate basis over the period of the contract based on the principal amounts outstanding.

ii) <u>Ijarah Thumma Al-Bai</u>
Income is recognised on effective profit rate over the term of the contract.

iii) <u>Musharakah (Co-ownership)</u>
Income is accounted for on the basis of the reducing balance on a time-apportioned (the Bank's co-ownership portion) basis that reflects the effective yield on the asset.

iv) <u>Bai Al-Inah (Sale and Buy Back)</u>
Income is recognised on effective profit rate basis over the period of the contract based on the principal amounts outstanding.

v) <u>Bai Bithaman Ajil</u>
Income is recognised on effective profit rate basis over the period of the contract based on the principal amounts outstanding.

vi) <u>Bai Al-Dayn</u>
Income is recognised on effective profit rate basis over the period of the contract based on the principal amounts outstanding.

3 Significant Accounting Policies (Cont'd)

(b) Financing Income and Expenses (Cont'd)

vii) Ujrah (rendering services for credit card-i holders)
Income is recognised based on the identified services, benefits and privileges in exchange of a fee.

viii) Ujrah (rendering services for facilities other than credit card-i holders)
Income is recognised based on mutually agreed fee to provide the facility to customers.

Profit on impaired financial assets of the Bank is recognised using the rate of profit used to discount the future cash flows for the purpose of measuring the impairment loss.

Financing income and expense of the Bank presented in the statement of profit and loss and other comprehensive income include:
- profit on financial assets and liabilities measured at amortised costs calculated on an effective profit rate basis;
- profit on available-for-sale investment securities calculated on an effective profit rate basis;
- the effective portion of fair value changes in qualifying hedging derivatives designated in cash flow hedges of variability in profit cash flows, in the same period that the hedged cash flows affect financing income/expense; and
- the effective portion of fair value changes in qualifying hedging derivatives designated in fair value hedges of interest rate risk.

(c) Fees and Commission, Net Trading Income and Other Operating Income

Fee income is earned from a diverse range of services the Bank provides to their customers. Fee income is accounted for as follows:

- income earned on the execution of a significant act is recognised as revenue when the significant act has been completed;
- income earned from the provision of services is recognised as revenue as the services are provided; and
- income which forms an integral part of the effective profit rate of a financial instrument is recognised as an adjustment to the effective profit rate and recorded in 'financing income' (see Note 3(b)).

Other fees and commission expense relates mainly to transaction and service fees, which are expensed as the services are rendered.

Dividend income is recognised when the right to receive payment is established. This is the ex-dividend date for listed equity securities, and usually the date when shareholders approve the dividend for unlisted equity securities.

Net trading income comprises all gains and losses from changes in the fair value of financial assets and financial liabilities held-for-trading, together with the related profit income and attributable profit on financial liabilities.

Net income/(expense) from financial instruments designated at fair value includes:
- all gains and losses from changes in the fair value of financial assets and financial liabilities designated at fair value through profit or loss, including liabilities under investment contracts;
- all gains and losses from changes in the fair value of derivatives that are managed in conjunction with financial assets and liabilities designated at fair value through profit or loss; and
- profit income, profit expense and dividend income in respect of:
  - financial assets and financial liabilities designated at fair value through profit or loss; and
  - derivatives managed in conjunction with the above,

Except for profit arising from debt securities issued by the group and derivatives managed in conjunction with those debt securities, which is recognised in 'financing expense' (Note 3(b)).

(d) Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the profit or loss except to the extent that it relates to items recognised directly in other comprehensive income or equity, in which case it is recognized in the same statement in which the related item appears.

Current tax is the tax expected to be payable or receivable on the taxable income or loss for the financial year, calculated using tax rates enacted or substantively enacted at the end of the reporting period, and any adjustment to tax payable in respect of previous financial years. The Bank provides for potential current tax liabilities that may arise on the basis of the amounts expected to be paid to the tax authorities. Current tax assets and liabilities are offset when the Bank intends to settle on a net basis and the legal right to offset exists.

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

Deferred tax is calculated using the tax rates expected to apply in the periods in which the assets will be realised or the liabilities settled, based on tax rates and laws enacted, or substantively enacted, by the balance sheet date. Deferred tax assets and liabilities are offset when they arise in the same tax reporting group and relate to income taxes levied by the same taxation authority, and when the Bank have a legal right to offset.

Deferred tax relating to fair value re-measurements of available-for-sale investments which are charged or credited directly to other comprehensive income, is also charged or credited to other comprehensive income and is subsequently recognised in the profit or loss when the deferred fair value gain or loss is recognised in the profit or loss.

(e) Financial instruments

(i) Initial recognition and measurement

A financial asset or a financial liability is recognised in the statement of financial position when, and only when the Bank becomes a party to the contractual provisions of the instrument.

A financial instrument is recognised initially, at its fair value plus, in the case of a financial instrument not at fair value through profit or loss, transactions costs that are directly attributable to the acquisition or issue of the financial instrument.

An embedded derivative is recognised separately from the host contract and accounted for as a derivative if, and only if, it is not closely related to the economic characteristics and risks of the host contract and the host contract is not categorised as fair value through profit or loss. The host contract, in the event an embedded derivative is recognised separately, is accounted for in accordance with policy applicable to the nature of the host contract.

(ii) Financial instrument categories and subsequent measurement

The Bank categorises financial assets as follows:
- financing and advances (See Note 3(j))
- financial investments held to maturity (See Note 3(i)(i))
- financial investments available-for-sale (See Note 3(i)(ii)); or
- trading assets (see Note 3(h)):

The Bank classifies its financial liabilities, other than financial guarantees, as measured at amortised cost or trading liabilities. (See accounting policies in Notes 3(h), 3(p), 3(r)).

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

3 Significant Accounting Policies (Cont'd)

(e) Financial instruments (Cont'd)

(iii) Derecognition of financial assets and liabilities

Financial assets are derecognised when the rights to receive cash flows from the assets have expired; or where the Bank has transferred its contractual rights to receive the cash flows of the financial assets, and have transferred substantially all the risks and rewards of ownership; or where both control and substantially all the risks and rewards are not retained.

Financial liabilities are derecognised when they are extinguished, i.e. when the obligation is discharged, cancelled, or expires.

(iv) Offsetting financial assets/liabilities and income/expenses

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position when there is currently a legally enforceable right to offset the recognised amounts and the Bank intends to settle on a net basis, or realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under the MFRSs, or for gains and losses arising from a group of similar transactions such as in the Bank's trading activity.

(v) Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective profit method of any difference between the initial amounts recognised and the maturity amount, minus any reduction for impairment.

(vi) Fair value measurement

All financial instruments are recognised initially at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of a financial instrument on initial recognition is the transaction price (that is, the fair value of the consideration given or received). In certain circumstances, however, the fair value will be based on other observable current market transactions in the same instrument, without modification or repackaging, or on a valuation technique whose variables include only data from observable markets, such as profit rate yield curves, option volatilities and currency rates. When such evidence exists, the Bank recognise a trading gain or loss on inception of the financial instrument, being the difference between the transaction price and the fair value. When unobservable market data have a significant impact on the valuation of financial instruments, the entire initial difference in fair value from the transaction price as indicated by the valuation model is not recognised immediately in the income statement. Instead, it is recognised over the life of the transaction on an appropriate basis, when the inputs become observable, the transaction matures or is closed out, or when the Bank enter into an offsetting transaction.

Subsequent to initial recognition, the fair values of financial instruments measured at fair value are measured in accordance with the Bank's valuation methodologies, which are described in Note 5(b)(ii).

(f) Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents include highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value. Such investments comprise cash at hand and bank balances, short term deposits and placements with banks maturing within one month.

(g) Contracts under Islamic Sell and Buyback Agreements

When securities are sold subject to a commitment to repurchase them at a predetermined price (repos), they remain on the balance sheet and a liability is recorded for the consideration received.

Securities purchased under commitments to re-sell (reverse repos) are not recognised on the balance sheet and an asset is recorded in respect of the initial consideration paid.

Non-trading repos and reverse repos are measured at amortised cost. The difference between the sale and repurchase price or between the purchase and resale price is treated as profit income and recognised in net profit income over the life of the agreement.

(h) Trading assets and trading liabilities

Treasury bills, financing and advances to and from customers, placings with and by banks, debt securities, equity securities, debt securities in issue, certain deposits and short positions in securities which have been acquired or incurred principally for the purpose of selling or repurchasing in the near term, or are part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent pattern of short-term profit-taking are classified as held-for-trading. Financial assets or financial liabilities are recognised on trade date, when the Bank enters into contractual arrangements with counterparties to purchase or sell the financial instruments, and are normally derecognised when either sold (assets) or extinguished (liabilities). Measurement is initially at fair value, with transaction costs taken to the profit or loss. Subsequently, the fair values are remeasured and gains and losses from changes therein are recognised in the profit or loss within 'Other operating income'.

In order to conform with the BNM presentation of the balance sheet to present financial instruments by types rather than by measurement, trading liabilities are not disclosed as a separate item on the face of the balance sheet. They are included into the respective types of financial liabilities instrument categories.

Islamic structured placement is classified as trading liabilities as they are initiated by the trading desk for trading and not for funding purposes and the market risk of the embedded derivative is actively managed as part of the trading portfolio.

(i) Financial investments

Treasury bills, debt securities and equity securities intended to be held on a continuing basis, other than those designated at fair value, are classified as available-for-sale or held-to-maturity. They are recognised on trade date when the Bank enters into contractual arrangements to purchase those instruments, and are normally derecognised when either the securities are sold or redeemed.

(i) Held-to-maturity

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank positively intends and is able to hold until maturity. These investments are initially recorded at fair value plus any directly attributable transaction costs, and are subsequently measured at amortised cost using the effective profit rate method, less any impairment losses.

(ii) Available-for-sale

Available-for-sale financial assets are initially measured at fair value plus direct and incremental transaction costs. Available-for-sale financial assets are recognised on the trade date when the bank enters into contractual arrangements to purchase those instruments, and are normally derecognised when either the securities are sold or redeemed. They are subsequently remeasured at fair value, and changes therein are recognised in other comprehensive income in 'Available-for-sale reserves – changes in fair value' until they are either sold or become impaired. When available-for-sale financial assets are sold, cumulative gains or losses previously recognised in other comprehensive income are recognised in the profit or loss as 'Disposal of financial investments available-for-sale'.

(i) Financial investments (Cont'd)

Profit earned is recognised on available-for-sale debt securities using the effective profit rate method, calculated over the asset's expected life. Premiums and/or discounts arising on the purchase of dated investment securities are included in the calculation of their effective profit rates. Dividends are recognised in the profit or loss when the right to receive payment is established.

Available-for-sale financial assets are assessed at each balance sheet date for objective evidence of impairment. Impairment losses are recognised if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the financial asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset and can be reliably estimated.

If the available-for-sale financial asset is impaired, the difference between the financial asset's acquisition cost (net of any principal repayments and amortisation) and the current fair value, less any previous impairment loss recognised in the profit or loss, is removed from other comprehensive income and recognised in the profit or loss.

Impairment losses for available-for-sale debt securities are recognised within 'Financing impairment charges and other credit risk provisions' in the profit or loss and impairment losses for available-for-sale equity securities are recognised within 'Gains/losses from financial investments' in the profit or loss.

- *Available-for-sale debt securities*
  In assessing objective evidence of impairment at the reporting date, the Bank considers all available evidence, including observable data or information about events specifically relating to the securities which may result in a shortfall in the recovery of future cash flows. These events may include a significant financial difficulty of the issuer, a breach of contract such as a default, bankruptcy or other financial reorganisation, or the disappearance of an active market for the debt security because of financial difficulties relating to the issuer.

  These types of specific event and other factors such as information about the issuers' liquidity, business and financial risk exposures, levels of and trends in default for similar financial assets, national and local economic trends and conditions, and the fair value of collateral and guarantees may be considered individually, or in combination, to determine if there is objective evidence of impairment of a debt security.

- *Available-for-sale equity securities*
  Objective evidence of impairment for available-for sale equity securities may include specific information about the issuer as detailed above, but may also include information about significant changes in technology, markets, economics or the law that provides evidence that the cost of the equity securities may not be recovered.

  A significant or prolonged decline in the fair value of the equity below its cost is objective evidence of impairment. In assessing whether it is significant, the decline in fair value is evaluated against the original cost of the asset at initial recognition. In assessing whether it is prolonged, the decline is evaluated against the continuous period in which the fair value of the asset has been below its original cost at initial recognition.

Once an impairment loss has been recognised on an available-for-sale financial asset, the subsequent accounting treatment for changes in the fair value of that asset differs depending on the nature of the available-for-sale financial asset concerned:

- *Available-for-sale debt security*
  A subsequent decline in the fair value of the instrument is recognised in the profit or loss when there is objective evidence of impairment as a result of further decreases in the estimated future cash flows of the financial asset. Where there is no further objective evidence of impairment, the decline in the fair value of the financial asset is recognised directly in other comprehensive income. If the fair value of a debt security increases in a subsequent period, and the increase can be objectively related to an event occurring after the impairment loss was recognised in the profit or loss, the impairment loss is reversed through the profit or loss to the extent of the increase in fair value.

3 Significant Accounting Policies (Cont'd)

(i) Financial investments (Cont'd)

- *Available-for-sale equity security*
  All subsequent increases in the fair value of the instrument are treated as a revaluation and are recognised directly in other comprehensive income. Subsequent decreases in the fair value of the available-for-sale equity security are recognised in the profit or loss, to the extent that further cumulative impairment losses have been incurred in relation to the acquisition cost less cumulative impairment to date of the equity security. Impairment losses recognised on the equity security are not reversed through the profit or loss.

(j) Financing and Advances

Financing and advances consist of Murabahah, Diminishing Musharakah, Bai Al-Inah, Bai Bithaman Ajil, Ijarah, Ijarah Thumma Al-Bai, Bai Al-Dayn and Ujrah contracts. They include financing and advances to customers and placements with banks that originated from the Bank, which are not classified as either held for trading or designated at fair value. They are recognised when cash is advanced to customers and derecognised when either the customer repays its obligations, or the advances are sold or written off, or substantially all the risks and rewards of ownership are transferred. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective profit rate method, less any reduction from impairment or uncollectibility.

Assets funded under Ijarah financing are owned by the Bank throughout the tenure of the Ijarah financing. Ownership of the assets will be transferred to the customers at the end of the Ijarah financing subject to the customer's execution of the purchase option.

For financing under the Syndicated Investment Account for Financing/Investment Agency Account (SIAF/IAA) or Restricted Profit Sharing Investment Account (RPSIA) arrangements, the Bank applies the derecognition principles as stated in accounting policy Note 3(e)(iii) on derecognition of financial assets.

(k) Impairment of financing and advances

Losses for impaired financing and advances are recognised when there is objective evidence that impairment of a financing or portfolio of financing has occurred or when principal or profit or both are past due for more than ninety (90) days, whichever is sooner. Impairment allowances are calculated on individual financing and on groups of financing assessed collectively. Impairment losses are recorded as charges to the profit or loss. The carrying amount of impaired financing on the balance sheet is reduced through the use of impairment allowance accounts. Losses which may arise from future events are not recognised.

The Bank's allowance for impaired financing are in conformity with MFRS 139.

(i) Individually assessed financing and advances

The factors considered in determining whether a financing is individually significant for the purposes of assessing impairment include the size of the financing, the number of financing in the portfolio and the importance of the individual financial relationship, and how this is managed.

Financing that are determined to be individually significant will be individually assessed for impairment, except when volumes of defaults and losses are sufficient to justify treatment under a collective methodology.

Financing considered as individually significant are typically to corporate and commercial customers, are for larger amounts and are managed on an individual basis. Retail financing portfolios are generally assessed for impairment on a collective basis as the portfolios generally consist of large pools of homogeneous financing.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

3 Significant Accounting Policies (Cont'd)

(k) Impairment of financing and advances (Cont'd)

(i) Individually assessed financing and advances (Cont'd)

For all financing that are considered individually significant, the Bank assesses on a case-by-case basis at each balance sheet date to identify whether evidence of impairment exists based on the following criteria:
- known cash flow difficulties experienced by the borrower;
- contractual payments of either principal or profit being past due for more than 90 days;
- the probability that the borrower will enter bankruptcy or other financial realisation;
- a concession granted to the borrower for economic or legal reasons relating to the customer's financial difficulty that results in forgiveness or postponement of principal, profit or fees, where the concession is not insignificant; and
- there has been deterioration in the financial condition or outlook of the customer such that its ability to repay is considered doubtful.

For those financing where objective evidence of impairment exists, impairment losses are determined considering the following factors:
- the Bank's aggregate exposure to the customer;
- the viability of the customer's business model and their capacity to trade successfully out of financial difficulties and generate sufficient cash flow to service debt obligations;
- the amount and timing of expected receipts and recoveries;
- the likely dividend available on liquidation or bankruptcy;
- the extent of other creditors' commitments ranking ahead of, or pari passu with, the Bank and the likelihood of other creditors continuing to support the company;
- the complexity of determining the aggregate amount and ranking of all creditor claims and the extent to which legal and insurance uncertainties are evident;
- the realisable value of security (or other credit mitigants) and likelihood of successful repossession;
- the likely deduction of any costs involved in recovery of amounts outstanding;
- the ability of the borrower to obtain, and make payments in, the currency of the financing if not denominated in local currency; and
- when available, the secondary market price of the debt.

The realisable value of security is determined based on the most recently updated market value at the time when the impairment assessment is performed. The value is not adjusted for expected future changes in market prices, though adjustments are made to reflect local conditions such as forced sale discounts.

Impairment losses are calculated by discounting the expected future cash flows of a financing, which include expected future receipts of contractual profit, at the financing's original effective profit rate or an approximation thereof, and comparing the resultant present value with the financing's current carrying amount. The impairment allowances on individually significant accounts are reviewed at least quarterly and more regularly when circumstances require. This normally encompasses re-assessment of the enforceability of any collateral held and the timing and amount of actual and anticipated receipts. Individually assessed impairment allowances are only released when there is reasonable and objective evidence of a reduction in the established loss estimate.

(ii) Collectively assessed financing and advances

Impairment is assessed collectively to cover losses which have been incurred but have not yet been identified on financing subject to individual assessment and for homogeneous groups of financing and advances that are not considered individually significant, generally retail lending portfolios.

Individually assessed financing for which no evidence of impairment has been specifically identified on an individual basis are grouped together according to their credit risk characteristics for a collective impairment assessment. These credit risk characteristics may include country of origination, type of business involved, type of products offered, security obtained or other relevant factors. This assessment captures impairment losses that the Bank has incurred as a result of events occurring before the balance sheet date, which the Bank is not able to identify on an individual financing basis, and that can be reliably estimated when information becomes available which identifies losses on individual financing within the group, those financing are removed from the group and assessed individually.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

3 Significant Accounting Policies (Cont'd)

(k) Impairment of financing and advances (Cont'd)

(ii) Collectively assessed financing and advances (Cont'd)

The collective impairment allowance is determined after taking into account:

- historical loss experience in portfolios of similar credit risk characteristics (for example, by industry sector, financing grade or product);
- the estimated period between impairment occurring and the loss being identified and evidenced by the establishment of an appropriate allowance against the individual financing; and
- management's experienced judgment as to whether current economic and credit conditions are such that the actual level of inherent losses at the balance sheet date is likely to be greater or less than that suggested by historical experience.

The period between a loss occurring and its identification is estimated by local management for each identified portfolio based on economic and market conditions, customer behaviour, portfolio management information, credit management techniques and collection and recovery experiences in the market. The estimated period between a loss occurring and its identification may vary over time as these factors change.

Homogeneous groups of financing and advances

Statistical methods are used to determine impairment losses for homogeneous groups of financing and advances not considered individually significant. Losses in these groups of financing are recorded individually when individual financing are removed from the group and written off. Two methods that are used to calculate collective allowances are:

- When appropriate empirical information is available, the Bank utilises roll rate methodology which employs statistical analyses of historical data and experience of delinquency and default to reliably estimate the amount of financing that will eventually be written off as a result of the events occurring before the balance sheet date. Individual financing are grouped using ranges past due days and statistical analysis are made of the likelihood that financing in each range will progress through the various stages of delinquency and become irrecoverable. Additionaly, individual financing are segmented based on their credit characteristics as described above. Current economic conditions are also evaluated when calculating the appropriate level of allowance required to cover inherent loss. The estimated loss is the difference between the present value of expected future cash flows, discounted at the original effective profit rate of the portfolio, and the carrying amount of the portfolio.

- When the portfolio size is small or when information is insufficient or not reliable enough to adopt a roll rate methodology, the Bank adopts a basic formulaic approach based on historical loss rate experience, or a discounted cash flow model. When a basic formulaic approach is undertaken, the period between losses occurring and its identification is explicitly estimated by local management, and is typically between six and twelve months.

The inherent loss within each portfolio is assessed on the basis of statistical models using historical data observations, which are updated periodically to reflect recent portfolio and economic trends. When the most recent trends arising from changes in economic, regulatory or behavioural conditions are not fully reflected in the statistical models, they are taken into account by adjusting the impairment allowances derived from the statistical models to reflect these changes as at the balance sheet date.

These additional portfolio risk factors may include recent financing portfolio growth and product mix, unemployment rates, bankruptcy trends, geographic concentrations, financing product features (such as the ability of customers to repay adjustable-rate financing where reset profit rates give rise to increases in profit charges), economic conditions such as national and local trends in housing markets and profit rates, portfolio seasoning, account management policies and practices, current levels of write-offs, adjustments to the period of time between loss identification and write-off, changes in laws and regulations and other factors which can affect customer payment patterns on outstanding financing, such as natural disasters. These risk factors, where relevant, are taken into account when calculating the appropriate level of impairment allowances by adjusting the impairment allowances derived solely from historical loss experience.

Roll rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure they remain appropriate.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

3 Significant Accounting Policies (Cont'd)

(k) Impairment of financing and advances (Cont'd)

(iii) Write-off of financing and advances

Financing (and the related impairment allowance accounts) are normally written off, either partially or in full, when there is no realistic prospect of recovery. Where financing are secured, this is generally after receipt of any proceeds from the realisation of security. In circumstances where the net realisable value of any collateral has been determined and there is no reasonable expectation of further recovery, write-off may be earlier.

(iv) Reversals of impairment

If the amount of an impairment loss decreases in a subsequent period, and the decrease can be related objectively to an event occurring after the impairment was recognised, the excess is written back by reducing the financing impairment allowance account accordingly. The write-back is recognised in profit or loss.

(v) Renegotiated financing

Financing subject to collective impairment assessment whose terms have been renegotiated are no longer considered past due, but are treated as up to date financing, once a minimum number of 12 monthly payments have been received. Financing subject to collective impairment assessment whose terms have been renegotiated are segregated from other parts of the financing portfolio for the purposes of collective impairment assessment, to reflect their risk profile.

Financing subject to individual impairment assessment, whose terms have been renegotiated remain as impaired until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future contractual payments, and there are no other indicators of impairment. The renegotiated financing will only be reclassified as unimpaired when restructured payment is received and observed for a minimum period of 12 months.

A financing that is renegotiated is derecognised if the existing agreement is cancelled and a new agreement made on substantially different terms, or if the terms of an existing agreement are modified, such that the renegotiated financing is substantially a different financial instrument. Any new financing that arise following derecognition events will continue to be disclosed as renegotiated financing and are assessed for impairment as above.

(l) Equipment

Equipment, fixtures and fittings and motor vehicles are stated at cost less accumulated depreciation and any accumulated impairment losses. Depreciation is calculated on a straight-line basis to write off the assets over their useful lives as follows:

Office equipment, fixtures and fittings	5 to 10 years
Computer equipment	3 to 7 years
Motor vehicles	5 years

Additions to equipment costing RM1,000 and under are fully depreciated in the year of purchase. For those assets costing more than RM1,000, depreciation is provided at the above rates.

The gains or losses on disposal of an item of equipment is determined by comparing the proceeds from disposal with the carrying amount of the equipment and is recognised net within "other operating income" in the profit or loss.

Equipment is subject to an impairment review if there are events or changes in circumstances which indicate that the carrying amount may not be recoverable.

3 Significant Accounting Policies (Cont'd)

(m) Operating leases

Leases, where the Bank does not assume substantially all the risks and rewards of ownership, are classified as operating leases and the leased assets are not recognised in the statement of financial position of the Bank. Rentals payable under operating leases are accounted for on a straight line basis over the periods of the leases and are included in 'establishment related expenses'.

(n) Intangible Assets

Intangible assets of the Bank represent computer software that have a finite useful life, and are stated at cost less accumulated amortisation and any accumulated impairment losses. Computer software includes both purchased and internally generated software. The cost of internally generated software comprises all directly attributable costs necessary to create, produce and prepare the software to be capable of operating in the manner intended by management. Costs incurred in the ongoing maintenance of software are expensed immediately as incurred.

Amortisation of intangible assets is calculated to write off the cost of the intangible assets on a straight line basis over the estimated useful lives of 3 to 5 years. Intangible assets are subject to impairment review if there are events or changes in circumstances which indicate that the carrying amount may not be recoverable.

(o) Bills and Acceptances Payable

Bills and acceptances payable represent the Bank's own bills and acceptances rediscounted and outstanding in the market.

(p) Debt securities issued, subordinated Commodity Murabahah financing, multi-currency sukuk programme and deposits by customers and banks

Financial liabilities are recognised when the Bank enters into the contractual provisions of the arrangements with counterparties, which is generally on trade date, and initially measured at fair value, which is normally the consideration received, net of directly attributable transaction costs incurred. Subsequent measurement of financial liabilities, other than those measured at fair value through profit or loss and financial guarantees, is at amortised cost, using the effective profit method to amortise the difference between proceeds received, net of directly attributable transaction costs incurred, and the redemption amount over the expected life of the instrument.

Subordinated Commodity Murabahah financing and the multi-currency sukuk programme of the Bank are measured at amortised cost using the effective profit method, except for the portions which are fair value hedged, which are adjusted for the fair value gains or losses attributable to the hedged risks. Profits payable on subordinated commodity murabahah financing and multi-currency sukuk programme of the Bank are recognised on an accrual basis.

(q) Provisions

Provisions recognised when it is probable that an outflow of economic benefits will be required to settle a present legal or constructive obligation which has arisen as a result of past events and for which a reliable estimate can be made.

Contingent liabilities, which include certain guarantees and letters of credit pledged as collateral security and contingent liabilities related to legal proceedings or regulatory matters, are possible obligations that arise from past events whose existence will be confirmed only by the occurrence, or non-occurrence, of one or more uncertain future events not wholly within the control of the Bank; or are present obligations that have arisen from past events but are not recognised because it is not probable that settlement will require the outflow of economic benefits, or because the amount of the obligations cannot be reliably measured. Contingent liabilities are not recognised in the financial statements but are disclosed (if there are any) unless the probability of settlement is remote.

(r) Financial guarantee contracts

Liabilities under financial guarantee contracts which are not classified as insurance contracts are recorded initially at their fair value, which is generally the fee received or present value of the fee receivable. Subsequently, financial guarantee liabilities are measured at the higher of the initial fair value, less cumulative amortisation, and the best estimate of the expenditure required to settle the obligations.

Fee income recognised on financial guarantee contracts are amortised to profit or loss using a straight-line method over the contractual period or, when there is no specified contractual period, recognised in the profit or loss upon discharge of the guarantee.

(s) Derivative financial instruments and hedge accounting

Derivatives are financial instruments that derive their value from the price of underlying items such as equities, profit rates or other indices. Derivatives are initially recognised, and are subsequently remeasured, at fair value. Fair values of exchange traded derivatives are obtained from quoted market prices. Fair values of over-the-counter derivatives are obtained using valuation techniques, including discounted cash flow models and option pricing models. Derivative assets and liabilities arising from different transactions are only offset for accounting purposes if the offsetting criteria are met.

Derivatives may be embedded in other financial instruments, for example, a convertible sukuk with an embedded conversion option. Embedded derivatives are treated as separate derivatives (bifurcated) when their economic characteristics and risks are not clearly and closely related to those of the host non-derivative contract; the terms of the embedded derivative would meet the definition of a stand-alone derivative if they were contained in a separate contract; and the combined contract is not held for trading or designated at fair value. These embedded derivatives are measured at fair value with changes therein recognised in the profit or loss.

Derivatives are classified as assets when their fair value is positive, or as liabilities when their fair value is negative. Derivative assets and liabilities arising from different transactions are only offset if the transactions are with the same counterparty, a legal right of offset exists, and the parties intend to settle the cash flows on a net basis.

The method of recognising fair value gains and losses depends on whether derivatives are held for trading or are designated as hedging instruments, and if the latter, the nature of the risks being hedged. All gains and losses from changes in the fair value of derivatives held for trading are recognised in the statements of profit or loss and other comprehensive income. When derivatives are designated as hedges, the Bank classify them as either: (i) hedges of the change in fair value of recognised assets or liabilities or firm commitments (fair value hedges) or (ii) hedges of the variability in highly probable future cash flows attributable to a recognised asset or liability, or a forecast transaction (cash flow hedges). Hedge accounting is applied to derivatives designated as hedging instruments in a fair value, cash flow or net investment hedge provided certain criteria are met.

<u>Hedge accounting</u>

At the inception of a hedging relationship, the Bank documents the relationship between the hedging instruments and the hedged items, its risk management objective and its strategy for undertaking the hedge. The Bank requires documented assessment, both at hedge inception and on an ongoing basis, of whether or not the hedging instruments are highly effective in offsetting the changes attributable to the hedged risks in the fair values or cash flows of the hedged items. Profit on designated qualifying hedges is included in 'Finance income'.

i) Fair value hedge

Changes in the fair value of derivatives that are designated and qualify as fair value hedging instruments are recorded in the profit or loss, along with changes in the fair value of the hedged assets or liabilities attributable to the hedged risk. If a hedge relationship no longer meets the criteria for hedge accounting, the hedge accounting is discontinued: the cumulative adjustment to the carrying amount of the hedged item is amortised to statements of profit or loss and other comprehensive income on a recalculated effective profit rate over the residual period to maturity, unless the hedged item has been derecognised, in which case, it is recognised in the profit or loss immediately.

(s) Derivative financial instruments and hedge accounting (Cont'd)

Hedge accounting (Cont'd)

ii) Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income. Any gain or loss in fair value relating to an ineffective portion is recognised immediately in the profit or loss within 'Other operating income'.

The accumulated gains and losses recognised in other comprehensive income are reclassified to the profit or loss in the same periods in which the hedged item affects the profit or loss. In hedges of forecast transactions that result in recognition of a non-financial asset or a non-financial liability, previous gains and losses recognised in other comprehensive income are removed from equity and included in the initial measurement of the asset or liability.

When a hedge relationship is discontinued, any cumulative gain or loss recognised in other comprehensive income at that time remains in equity until the forecast transaction is eventually recognised in the profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss previously recognised in other comprehensive income is immediately reclassified to the profit or loss.

(t) Financial instruments designated at fair value

Financial instruments, other than those held for trading, are classified in this category if they meet the criteria set out below and are so designated irrevocably by management on initial recognition. The Bank may designate financial instruments at fair value when the designation:

- eliminates or significantly reduces measurement or recognition inconsistencies that would otherwise arise from measuring financial instruments, or recognising the gains and losses different bases from related positions. Under this criterion, the main class of financial instruments designated by the Bank are:

  Long-term debt issues. The profit payable on certain fixed-rate long-term debt securities issued has been matched with the profit on 'receive fixed/pay variable' profit swaps as part of a documented profit rate risk management strategy. An accounting mismatch would arise if the debt securities issued were accounted for at amortised cost, because the related derivatives are measured at fair value with changes in the fair value recognised in the profit or loss. By designating the long-term debt at fair value, the movement in the fair value of the long-term debt will also be recognised in the profit or loss;

- applies to a groups of financial instruments are managed and their performance evaluated, on a fair value basis, in accordance with a documented risk management or investment strategy, and where information about that groups of financial instruments is reported to management on that basis. The Bank has documented risk management and investment strategies designed to manage and monitor market risk of those assets on net basis, after considering non-linked liabilities. Fair value measurement is also consistent with the regulatory reporting requirements under the appropriate regulations for these insurance operations; and

- relates to financial instruments containing one or more non-closely related embedded derivatives.

Designated financial assets are recognised at fair value when the Bank enters into contracts with counterparties, which is generally on trade date, and are normally derecognised when sold. Subsequent changes in fair values are recognised in the profit or loss in 'Net gain/(loss) from financial instruments fair value through profit and loss'.

3 Significant Accounting Policies (Cont'd)

(u) Employee benefits

(i) Short term employee benefits

Short term employee benefit obligations in respect of salaries, annual bonuses, paid annual leave and sick leave are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognised for the amount expected to be paid under short term cash bonus or profit-sharing plans if the Bank have a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(ii) Defined contribution plan

As required by law, companies in Malaysia make contributions to the Employees Provident Fund (EPF). Such contributions are recognised as an expense in the statements of profit or loss and other comprehensive income as incurred.

(v) Share based payments

The Bank's ultimate holding company, HSBC Holdings Plc operates a number of equity-settled share based payment arrangements with the Bank's employees as compensation for services provided by the employees. Equity-settled share based payment arrangements entitle employees to receive equity instruments of the ultimate holding company.

The cost of share-based payment arrangements with employees is measured by reference to the fair value of equity instruments on the date they are granted, and recognised as an expense on a straight-line basis over the vesting period, with a corresponding credit to the equity. The credit to equity is treated as capital contribution as the ultimate holding company is compensating the Bank's employees with no expense to the Bank. The vesting period is the period during which all the specified vesting conditions of a share-based payment arrangement are to be satisfied. The fair value of equity instruments that are made available immediately, with no vesting period attached to the award, are expensed immediately.

Fair value is determined by using market prices or appropriate valuation models, taking into account the terms and conditions upon which the equity instruments were granted. Vesting conditions include service conditions and performance conditions; any other features of a share-based payment arrangement are non-vesting conditions. Market performance conditions and non-vesting conditions are taken into account when estimating the fair value of equity instruments at the date of grant, so that an award is treated as vesting irrespective of whether the market performance condition or non-vesting condition is satisfied, provided all other vesting conditions are satisfied.

Vesting conditions, other than market performance conditions, are not taken into account in the initial estimate of the fair value at the grant date. They are taken into account by adjusting the number of equity instruments included in the measurement of the transaction, so that the amount recognised for services received as consideration for the equity instruments granted shall be based on the number of equity instruments that eventually vest. On a cumulative basis, no expense is recognised for equity instruments that do not vest because of a failure to satisfy non-market performance or service conditions.

Where an award has been modified, as a minimum, the expense of the original award continues to be recognised as if it had not been modified. Where the effect of a modification is to increase the fair value of an award or increase the number of equity instruments, the incremental fair value of the award or incremental fair value of the extra equity instruments is recognised in addition to the expense of the original grant, measured at the date of modification, over the modified vesting period.

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

Where the ultimate holding company recharges the Bank for the equity instruments granted, the recharge is recognised over the vesting period.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

3 Significant Accounting Policies (Cont'd)

(w) Earnings per share

The Bank presents basic earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to the ordinary shareholder of the Bank by the weighted average number of shares outstanding during the year.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

4 Financial risk management

a) Introduction and overview

All of the Bank's activities involve analysis, evaluation, acceptance and management of some degree of risk or combination of risks. The Bank has exposure to the following risks from financial instruments:

- credit risk
- liquidity risk
- market risks (includes foreign exchange, profit rate and basis risk)
- operational risks

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, policies and processes for measuring and managing risk, and the Bank's management of capital.

Risk management framework

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 limits continually by means of reliable and up-to-date administrative and information systems. The Bank regularly reviews its risk management policies and systems to reflect changes in markets, products and best practice risk management processes. Training, individual responsibility and accountability, together with a disciplined, conservative and constructive culture of control, lie at the heart of the Bank's management of risk.

The Executive Committee and Board Risk Committee (constituted by Non-Executive Directors), appointed by the Board of Directors, formulate risk management policy, monitor risk and regularly review the effectiveness of the Bank's risk management policies.

The Board Risk Committee is entrusted with the responsibility to oversee Senior Management's activities in managing credit, market, liquidity, operational, legal and other risks and to ensure that the risk management process is in place and functioning. A separate internal Risk Management Meeting made up of EXCO members (in line with the HSBC Group's Enterprise Risk Management Framework) are responsible to oversee and ensure that risk issues across all businesses are appropriately managed, and that adequate controls exist. Additionally, the Bank also has an internal Operational Risk and Governance Working Group to oversee and manage operational risk and ensure that adequate controls are maintained over operational processes.

b) Credit risk management

Credit risk is the risk that financial loss arises from the failure of a customer or counterparty to meet its payment obligations under a contract. It arises principally from cash and deposit placements, direct lending, trade finance, and holdings of investment debt securities. The Bank has dedicated standards, policies and procedures to control and monitor all such risks.

A Credit and Risk Management structure under the Chief Risk Officer who reports to the Chief Executive Officer, is in place to ensure a more coordinated management of credit risk and a more independent evaluation of credit proposals. The Chief Risk Officer, who also has strong oversight of market, operational and environmental risk, has a functional reporting line to the HBMY Country Chief Risk Officer.

The Bank have established a credit process involving credit policies, procedures and financing guidelines which are regularly updated and credit approval authorities delegated from the Board of Directors to the Chief Risk Officer who in turn will delegate the credit approval authorities to the credit risk executives. Excesses or deterioration in credit risk grade are monitored on a regular and ongoing basis and at the periodic, normally annual, review of the facility. The objective is to build and maintain risk assets of acceptable quality where risk and return are commensurate. Reports are produced for the Risk Management Meeting, Executive Committee, Board Risk Committee and the Board, covering:

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

4 Financial risk management (Cont'd)

b) Credit risk management (Cont'd)

- well defined credit risk appetite on business with growth, maintain and shrink sectors.
- risk concentrations and exposures by industry (main sectors exposures) and portfolio/business.
- single counterparty exposure limit.
- portfolio management exposures by Customer Risk Rating (asset quality by CRR);
- large impaired accounts and impairment allowances;
- early risk identification 'Worry & Watch' List trend and Top 10 Distressed names; and
- rescheduled and restructured financing.

The Bank has systems in place to control and monitor the exposure at the customer and counterparty level. A regional Credit Review and Risk Identification (CRRI) team undertakes regular thematic reviews based on a representative sample of accounts to assess the level and trend of portfolio credit risk, integrity of risk rating, quality of credit risk assessment and the approval process as well as quality of credit risk management and control activities. Where risk ratings are considered to be inappropriate, CRRI will discuss with the management and their subsequent recommendations for revised grades must then be assigned to the facilities concerned.

In addition, the regional CRRI team undertakes periodic sampling to assess the quality of credit assessment, integrity of customer risk ratings, quality of management controls, adherence to policy and procedures and use of appropriate approval authority. Furthermore, credit risk surveillance is also undertaken by a local Risk Identification team to identity potential high risk accounts for remedial or mitigating actions to be taken at an early stage.

The Bank's exposure to credit risk is shown in Note 4(b)(viii).

(i) Impairment assessment

Individually impaired financing and securities are financing and advances and investment debt securities for which the Bank determines that there is objective evidence of impairment and it does not expect to collect all principal and profit due according to the contractual terms of the financing/investment security. These financing are graded CRR 9-10 in the Bank's internal credit risk grading system. Please refer to Note 4(b)(viii) for further information on the Bank's internal credit risk rating system.

When impairment losses occur, the Bank reduces the carrying amount of financing and advances through the use of an allowance account. When impairment of available-for-sale financial assets occurs, the carrying amount of the asset is reduced directly. For further details, see Note 3(i) (ii) and Note 3(k). Impairment allowances may be assessed and created either for individually significant accounts or, on a collective basis, for groups of individually significant accounts for which no evidence of impairment has been individually identified or for high-volume groups of homogeneous financing that are not considered individually significant. It is the Bank's policy that allowances for impaired financing are created promptly and consistently. Management regularly evaluates the adequacy of the established allowances for impaired financing by conducting a detailed review of the financing portfolio, comparing performance and delinquency statistics with historical trends and assessing the impact of current economic conditions.

(ii) Past due but not impaired financing and investment debt securities

Past due but not impaired financing and investment debt securities are those for which contractual profit or principal payments are past due, but the Bank believes that impairment is not appropriate on the basis of the level of security/collateral available and/or the stage of collection of amounts owed to the Bank.

Examples of exposures past due but not impaired include overdue financing fully secured by cash collateral; house financing that are individually assessed for impairment, and that are in arrears less than 90 days, but where the value of collateral is sufficient to pay both the principal financial obligation and potential profit; and short-term trade facilities past due for technical reasons such as delays in documentation, but where there is no concern over the creditworthiness of the counterparty.

(iii) Financing with renegotiated terms

Financing with renegotiated terms are financing that have been restructured due to deterioration in the customer's financial position and where the Bank has made concessions it would not otherwise consider. Once the financing is restructured it remains in this category independent of satisfactory performance after restructuring.

b) Credit risk management (Cont'd)

(iv) Write-off of financing and advances

Financing are normally written off, either partially or in full, when there is no realistic prospect of further recovery. Where financing are secured, this is generally after receipt of any proceeds from the realisation of security. In circumstances where the net realisable value of any collateral has been determined and there is no reasonable expectation of further recovery, write off may be earlier.

In line with HSBC Global policy, financing is made on the basis of the customer's capacity to repay, as opposed to placing primary reliance on credit risk mitigation. Depending on the customer's standing and the type of product, facilities may be provided unsecured. Mitigation of credit risk is nevertheless a key aspect of effective risk management and in the Bank, takes many forms, the most common method of which is to take collateral. The principal collateral types employed by the Bank are as follows:

- under the residential and real estate business; mortgages over residential and financed properties;
- under certain Islamic specialised financing and leasing transactions (such as vehicle financing) where physical assets form the principal source of facility repayment, physical collateral is typically taken;
- in the commercial and industrial sectors, charges over business assets such as premises, stock and debtors;
- facilities provided to small and medium enterprises are commonly granted against guarantees by their owners/directors;
- guarantees from third parties can arise where facilities are extended without the benefit of any alternative form of security, e.g. where the Bank issues a bid or performance bond in favour of a non-customer at the request of another bank;
- under the institutional sector, certain trading facilities are supported by charges over financial instruments such as cash, debt securities and equities; and
- financial collateral in the form of cash and marketable securities is used in much of the over-the-counter (OTC) derivatives activities and in the Bank's securities financing business (securities lending and borrowing or repos and reverse repos).

(v) Collateral held as security

The Bank does not disclose the fair value of collateral held as security or other credit enhancements on financing and advances past due but not impaired, or on individually assessed financing and advances, as it is not practicable to do so.

The financial effect of collateral (quantification of the extent to which collateral and other credit enhancements mitigate credit risk) held for impaired financing for the Bank as at 31 Dec 2016 are 60.27% (2015: 49.66%). The financial effect of collateral held for other remaining on-balance sheet financial assets is not significant.

Collateral especially properties are made available for sale in an orderly fashion, with the proceeds used to reduce or pay the outstanding financing amount. If excess funds arise after the financing has been repaid, they are made available either to pay other secured financiers with lower priority or are returned to the customer. The Bank does not generally occupy repossessed properties for its business use.

(vi) Concentration of credit risk

The Bank monitors concentration of credit risk by sector and geographical location. The analysis of concentration of credit risk from financing and advances to customers is shown in Note 9. The analysis of concentration of credit risk from the Bank's financial assets are shown in Note 4(b)(ix).

(vii) Financial assets held-for-trading

The Bank holds financial assets held-for-trading of RM0.5 million (2015: RM10.5 million). An analysis of the credit quality of the maximum credit exposure, based on the rating agency Standard & Poor's, is as disclosed in Note 7 to the financial statements.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

4 Financial risk management (Cont'd)

b) Credit risk management (Cont'd)

(viii) Exposure to credit risk (Cont'd)

	2016		
	Financing and advances to customers RM'000	**Financing and advances to banks [1] RM'000**	**Other financial assets [2] RM'000**
Carrying amount	**11,743,263**	**2,359,591**	**1,844,851**
Assets at amortised cost			
Individually impaired:			
Gross amount	**303,526**	**-**	**-**
Allowance for impairment	**(62,757)**	**-**	**-**
Carrying amount	**240,769**	**-**	**-**
Past due but not impaired:			
Carrying amount	**834,641**	**-**	**-**
Past due comprises:			
up to 29 days	**607,497**	**-**	**-**
30 - 59 days	**157,441**	**-**	**-**
60 - 89 days	**69,703**	**-**	**-**
	834,641	**-**	**-**
Neither past due nor impaired:			
Strong	**5,677,276**	**2,359,591**	**-**
Medium -good	**2,501,861**	**-**	**-**
Medium-satisfactory	**2,331,861**	**-**	**-**
Substandard	**356,870**	**-**	**-**
Carrying amount	**10,867,868**	**2,359,591**	**-**
of which includes accounts with renegotiated terms	***39,984***	**-**	**-**
Collective allowance for impairment	**(200,015)**	**-**	**-**
Carrying amount-amortised cost	**11,743,263**	**2,359,591**	**-**
Other financial assets			
Neither past due nor impaired:			
Strong	**-**	**-**	**1,583,720**
Medium-good	**-**	**-**	**245,013**
Medium-satisfactory	**-**	**-**	**16,118**
Sub-standard	**-**	**-**	**-**
Carrying amount [3]	**-**	**-**	**1,844,851**
Carrying amount - fair value	**-**	**-**	**1,844,851**

In addition to the above, the Bank had entered into financing commitments and contingencies of RM9,738.2 million. The Bank had also issued financial guarantee contracts for which the maximum amount payable by the Bank, assuming all guarantees are called on, is RM1,760.0 million.

[1] Consists of cash and short term funds and deposits and placements with banks and other financial institutions.

[2] Consists of derivative financial assets, financial assets held-for-trading, financial investments available-for-sale and other financial assets.

[3] No available-for-sale accounts were renegotiated during the financial year.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

4 Financial risk management (Cont'd)

b) Credit risk management (Cont'd)

(viii) Exposure to credit risk (Cont'd)

	2015		
	Financing and advances to customers RM'000	Financing and advances to banks [1] RM'000	Other financial assets [2] RM'000
Carrying amount	11,968,217	4,750,390	2,260,645
Assets at amortised cost			
Individually impaired:			
Gross amount	235,279	-	-
Allowance for impairment	(68,647)	-	-
Carrying amount	166,632	-	-
Past due but not impaired:			
Carrying amount	776,757	-	-
Past due comprises:			
up to 29 days	533,081	-	-
30 - 59 days	179,099	-	-
60 - 89 days	64,577	-	-
	776,757	-	-
Neither past due nor impaired:			
Strong	6,202,137	4,750,390	-
Medium -good	2,056,149	-	-
Medium-satisfactory	2,820,917	-	-
Substandard	85,889	-	-
Carrying amount	11,165,092	4,750,390	-
of which includes accounts with renegotiated terms	*30,579*	-	-
Collective allowance for impairment	(140,264)	-	-
Carrying amount-amortised cost	11,968,217	4,750,390	-
Other financial assets			
Neither past due nor impaired:			
Strong	-	-	2,017,417
Medium-good	-	-	231,603
Medium-satisfactory	-	-	11,527
Sub-standard	-	-	98
Carrying amount	-	-	2,260,645
Carrying amount-fair value [3]	-	-	2,260,645

In addition to the above, the Bank had entered into financing commitments and contingencies of RM8,437.9 million. The Bank had also issued financial guarantee contracts for which the maximum amount payable by the Bank, assuming all guarantees are called on, is RM1,884.4 million.

[1] Consists of cash and short term funds and deposits and placements with banks and other financial institutions.

[2] Consists of derivative financial assets, financial assets held-for-trading, financial investments available-for-sale and other financial assets.

[3] No available-for-sale accounts were renegotiated during the financial year.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

4 Financial risk management (Cont'd)

b) Credit risk management (Cont'd)

(viii) Exposure to credit risk (Cont'd)

The five credit quality classifications set out and defined below describe the credit quality of HSBC's financing, debt securities portfolios and derivatives. Since 2008, the medium classification has been subdivided into 'medium-good' and 'medium satisfactory' to provide further granularity. These five classifications each encompass a range of more granular, internal credit rating grades assigned to corporate and retail financing business, as well as the external ratings attributed by external agencies to debt securities. There is no direct correlation between the internal and external ratings at granular level, except to the extent each falls within a single quality classification.

Credit quality of the Bank's debt securities and other bills	External Credit Rating [1]
Strong	A- and above
Good	BBB+ and BBB-
Satisfactory	BB+ to B and unrated
Sub-standard	B- to C
Impaired	D

[1] External ratings have been aligned to the five quality classifications. The ratings of Standard and Poor's are cited, with those of other agencies being treated equivalently.

Credit quality of the Bank's corporate financing/derivative financial assets/ deposits and placements with banks and other financial institutions	Internal Credit Rating
Strong	CRR1 - CRR2
Good	CRR3
Satisfactory	CRR4 - CRR5
Sub-standard	CRR6 - CRR8
Impaired	CRR9 - CRR10

Credit quality of the Bank's retail financing	Internal Credit Rating
Strong	EL1 -EL2
Medium-good	EL3
Medium-satisfactory	EL4 - EL5
Sub-standard	EL6 - EL8
Impaired	EL9 - EL10

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

4 Financial risk management (Cont'd)

b) Credit risk management (Cont'd)

(ix) Concentration by sector and by location [2]

	31 Dec 2016		31 Dec 2015	
	Financing and advances to banks [3] RM'000	**Other financial assets [4] RM'000**	Financing and advances to banks [3] RM'000	Other financial assets [4] RM'000
Carrying amount	**2,359,591**	**1,844,851**	4,750,390	2,260,645
By Sector				
Agricultural, hunting, forestry and fishing	**-**	**81**	-	-
Mining and quarrying	**-**	**126**	-	-
Manufacturing	**-**	**12,621**	-	15,272
Construction	**-**	**1**	-	10,021
Real estate	**-**	**2,692**	-	3,470
Wholesale & retail trade, restaurants & hotels	**-**	**79**	-	23
Transport, storage and communication	**-**	**296**	-	98
Finance, insurance and business services	**2,359,591**	**268,920**	4,750,390	231,174
Central banks and government related	**-**	**1,369,062**	-	1,701,733
Others	**-**	**190,973**	-	298,854
	2,359,591	**1,844,851**	4,750,390	2,260,645
By geographical location				
Within Malaysia	**2,277,933**	**1,600,000**	4,493,310	2,047,745
Outside Malaysia	**81,658**	**244,851**	257,080	212,900
	2,359,591	**1,844,851**	4,750,390	2,260,645

[2] Concentration by sector and location for financing and advances is disclosed under Note 10(iv) and 10(vi) to the financial statements

[3] Consists of cash and short term funds, deposits and placements with banks and other financial institutions, and other financial assets.

[4] Consists of derivative financial assets, financial assets held-for-trading and financial investments available-for-sale

c) Liquidity and funding risk management

Liquidity risk is the risk that the Bank does not have sufficient financial resources to meet their obligations when they fall due, or will have to do it at excessive cost. This risk can arise from mismatches in the timing of cash flows. Funding risk arises when the necessary liquidity to fund illiquid asset positions cannot be obtained at the expected terms and when required.

The Bank maintains a diversified and stable funding base comprising core retail and corporate customer deposits and institutional balances. This is augmented by wholesale funding and portfolios of highly liquid assets. The objective of the Bank's liquidity and funding management is to ensure that all foreseeable funding commitments and deposit withdrawals can be met when due and that wholesale market access is coordinated and cost effective.

Current accounts and savings deposits payable on demand or at short notice form a significant part of HSBC Group's funding, and the Bank places considerable importance on maintaining their stability. For deposits, stability depends upon preserving depositor confidence in the Bank's capital strength and liquidity, and on competitive and transparent pricing. In aggregate, the Bank is a net liquidity providers to the interbank market, placing significantly more funds with other banks than it borrows.

The management of liquidity and funding is primarily carried out in accordance with the BNM's Liquidity Coverage Ratio Framework; and practices and limits set by Asset and Liabilities Management Committee (ALCO) and regional Head Office. These limits vary to take account of the depth and liquidity of the local market in which the Bank operates. The Bank maintains a strong liquidity position and manages the liquidity profile of its assets, liabilities and commitments to ensure that cash flows are appropriately balanced and all obligations are met when due.

The Bank's liquidity and funding management process includes:

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

On 1 January 2016, HSBC Group implemented a new liquidity and funding risk framework (LFRF). It uses the liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) regulatory framework as a foundation, but adds extra metrics, limits and overlays to address the risks that we consider are not adequately reflected by the regulatory framework.

The LFRF is delivered using the following key aspects:

- standalone management of liquidity and funding by operating entity;
- operating entity classification by inherent liquidity risk (ILR) categorisation;
- minimum LCR requirement depending on ILR categorisation;
- minimum NSFR requirement depending on ILR categorisation;
- legal entity depositor concentration limit;
- three-month and 12-month cumulative rolling term contractual maturity limits covering deposits from banks;

c) Liquidity and funding risk management (Cont'd)

- deposits from non-bank financial institutions and securities issued;
- annual individual liquidity adequacy assessment by principal operating entity;
- minimum LCR requirement by currency;
- intraday liquidity; and
- forward-looking funding assessments.

The new internal LFRF and the risk tolerance limits were approved by the Board on the basis of recommendations made by the Group Risk Committee.

Please refer to Note 37 on disclosure on Liquidity Risk.

d) Market risk management

Market risk is the risk that movements in market risk factors, including foreign exchange rates, profit rates, basis risk and equity/commodity prices will reduce the Bank's income or the value of its portfolios.

The objective of the Bank's market risk management is to manage and control market risk exposures in order to optimise return on risk while maintaining a market profile consistent with the HSBC Group's status as one of the world's largest banking and financial services organisations.

There were no significant changes to our policies and practices for the management of market risk in 2016.

The Bank separates exposures to market risk into either trading or non-trading portfolios. Trading portfolios comprise positions arising from market making, proprietary position taking and other marked-to-market positions so designated. Non-trading portfolios primarily arise from the profit rate management of the Bank's retail and commercial banking assets and liabilities, and financial investments available-for-sale.

The management of market risk is principally undertaken using risk limit mandates approved by HSBC's Regional Wholesale and Global Market Risk Management (WMR), an independent unit which develops HSBC Group's market risk management policies and measurement techniques. Market risks which arise on each product are transferred to the Global Markets. The aim is to ensure that all market risks are consolidated within operations which have the necessary skills, tools, management and governance to manage such risks professionally. Limits are set for portfolios, products and risk types, with market liquidity being the principal factor in determining the level of limits set. The Bank has an independent product control function that is responsible for measuring market risk exposures in accordance with the policies defined by WMR. Positions are monitored daily and excesses against the prescribed limits are reported immediately to local senior management and WMR. The nature of the hedging and risk mitigation strategies corresponds to the market instruments available. These strategies range from the use of traditional market instruments, such as profit rate swaps, to more sophisticated hedging strategies to address a combination of risk factors arising at portfolio level.

Market risk in the trading portfolio is monitored and controlled at both portfolio and position levels using a complementary set of techniques such as value at risk and present value of a basis point, together with stress and sensitivity testing and concentration limits. Other controls to contain trading portfolio market risk at an acceptable level include rigorous new product approval procedures and a list of permissible instruments to be traded.

(i) Value at risk (VAR)

VAR is a technique that estimates the potential losses on risk positions as a result of movements in market rates and prices over a specified time horizon and to a given level of confidence. The use of VAR is integrated into market risk management and is calculated for all trading positions regardless of how the group capitalises those exposures. Where there is no approved internal model, the group uses the appropriate local rules to capitalise exposures. The VAR models used by the Bank are predominantly based on historical simulation. These models derive plausible future scenarios from past series of recorded market rates and prices, taking into account inter-relationships between different markets and rates such as profit rates and foreign exchange rates. The models also

d) Market risk management (Cont'd)

(i) Value at risk (VAR) (Cont'd)

incorporate the effect of option features on the underlying exposures. The historical simulation models used by the Bank incorporate the following features:

- historical market rates and prices are calculated with reference to foreign exchange rates and commodity prices, profit rates, equity prices and the associated volatilities;
- potential market movements utilised for VAR are calculated with reference to data from the past two years; and
- VAR measures are calculated to a 99 per cent confidence level and use a one-day holding period.

The nature of the VAR models means that an increase in observed market volatility will lead to an increase in VAR without any changes in the underlying positions. The Bank routinely validates the accuracy of its VAR models by back-testing the actual daily profit and loss results, adjusted to remove non-modelled items such as fees and commissions, against the corresponding VAR numbers. Statistically, the Bank would expect to see losses in excess of VAR only 1 per cent of the time over a one-year period. The actual number of excesses over this period can therefore be used to gauge how well the models are performing.

A summary of the VAR position of the Bank's trading portfolio at the reporting date is as follows:

RM'000	**At 31 Dec 2016**	**Average**	**Maximum**	**Minimum**
Foreign currency risk	**61**	**44**	**248**	**8**
Profit rate risk	**294**	**487**	**673**	**401**
Credit spread risk	**-**	**2**	**8**	**-**
Overall	**311**	**491**	**685**	**35**

RM'000	At 31 Dec 2015	Average	Maximum	Minimum
Foreign currency risk	299	50	321	8
Profit rate risk	387	235	408	36
Credit spread risk	8	-	16	-
Overall	436	242	459	37

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

- the use of historical data as a proxy for estimating future events may not encompass all potential events, particularly those which are extreme in nature;
- the use of a 1-day holding period assumes that all positions can be liquidated or the risk offset during that period. This may not fully reflect the market risk arising at times of severe illiquidity, when a 1-day holding period may be insufficient to liquidate or hedge all positions fully;
- the use of a 99 per cent confidence level, by definition, does not take into account losses that might occur beyond this level of confidence;
- VAR is calculated on the basis of exposures outstanding at the close of business and therefore does not necessarily reflect intra-day exposures; and
- VAR is unlikely to reflect loss potential on exposures that only arise under significant market movements.

The Bank recognise these limitations by augmenting its VAR limits with other position and sensitivity limit structures. Stress tests are produced on a monthly basis based on the HSBC Group's stress-testing parameters, and on a half-yearly basis based on Bank Negara Malaysia's parameters to determine the impact of changes in profit

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

4 Financial risk management (Cont'd)

d) Market risk management (Cont'd)

(i) Value at risk (VAR) (Cont'd)

rates, exchange rates and other main economic indicators on the Bank's profitability, capital adequacy and liquidity. The stress-testing provides the Board Risk Committee with an assessment of the financial impact of identified extreme events on the market risk exposures of the Bank.

Sensitivity measures are used to monitor the market risk positions within each risk type, for example, the present value of a basis point movement in profit rates, for profit rate risk. Sensitivity limits are set for portfolios, products and risk types, with the depth of the market being one of the principal factors in determining the level of limits set.

Derivative financial instruments (principally profit rate swaps) are used for hedging purposes in the management of asset and liability portfolios and structured positions. This enables the Bank to mitigate the market risk which would otherwise arise from structural imbalances in the maturity and other profiles of the assets and liabilities.

(ii) Exposure to profit rate risk - non-trading portfolio

Market risk in non-trading portfolios arises principally from mismatches between the future yields on assets and their funding cost as a result of profit rate changes. This market risk is transferred to Global Markets, taking into account both the contractual and behavioural characteristics of each product to enable the risk to be managed effectively. Behavioural assumptions for products with no contractual maturity are normally based on a two-year historical trend. These assumptions are important as they reflect the underlying profit rate risk of the products and hence are subject to scrutiny from ALCO, the regional Head Office and regional WMR. The net exposure is monitored against the limits granted by regional WMR for the respective portfolios and, depending on the view on future market movement, economically hedged with the use of financial instruments within agreed limits.

Profit rate risk in the banking book or Rate of Return risk in the Banking book (IRR/RORBB) is defined as the exposure of the non-trading products of the Bank to profit rates. Non-trading portfolios are subject to prospective profit rate movements which could reduce future net finance income. Non-trading portfolios include positions that arise from the profit rate management of the Bank's retail and commercial banking assets and liabilities, and financial investments designated as available for sale. IRR/RORBB arises principally from mismatches between future yields on assets and their funding costs, as a result of profit rate changes. Analysis of this risk is complicated by having to make assumptions within certain product areas such as the incidence of financing prepayments, and from behavioural assumptions regarding the economic duration of liabilities which are contractually repayable on demand such as current accounts.

The Bank manages market risk in non-trading portfolios by monitoring the sensitivity of projected net finance income under varying profit rate scenarios (simulation modelling). For simulation modelling, a combination of standard scenarios and non-standard scenarios relevant to the local market are used.

The standard scenarios monitored monthly include a 100 basis points parallel fall or rise in profit rates and a 25 basis points fall or rise in profit rates at the beginning of each quarter for the next 12 months.

The scenarios assume no management action. Hence, they do not incorporate actions that would be taken by the business units to mitigate the impact of the profit rate risk. In reality, the business units would proactively seek to change the profit rate profile to minimise losses and to optimise net revenues. Other simplifying assumptions are made, including that all positions run to maturity.

The profit rate sensitivities set out in the table below are illustrative only and are based on simplified scenarios.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

4 Financial risk management (Cont'd)

d) Market risk management (Cont'd)

(iii) Sensitivity of projected finance income

Change in projected finance income in next 12 months arising from a shift in profit rates of:

	RM'000			
	31-Dec-16		31-Dec-15	
Basis point parallel shift in yield curve	***+100bps***	***-100bps***	*+100bps*	*-100bps*
RM	**(22,711)**	**12,490**	45,092	(45,057)
USD	**(4,767)**	**2,204**	8,961	(6,878)
Others	**(482)**	**(126)**	3,807	(2,934)
	(27,960)	**14,568**	57,860	(54,869)

The increase or decline in economic value for upward and downward rate shocks for measuring profit rate risk/rate of return risk in the banking book are as follows:

Change in projected economic value of equity arising from a shift in profit rates of:

	RM'000			
	31-Dec-16		31-Dec-15	
Basis point parallel shift in yield curve	***+200bps***	***-200bps***	*+200bps*	*-200bps*
RM	**(179,135)**	**201,096**	(38,879)	38,879
USD	**(31,024)**	**23,763**	(21,600)	8,640
Others	**2,844**	**(850)**	8,640	(4,320)
	(207,315)	**224,009**	(51,839)	43,199

(iv) Sensitivity of reported reserves in "other comprehensive income" to profit rate movements

Sensitivity of reported reserves in "other comprehensive income" to profit rate movements are monitored on a monthly basis by assessing the expected reduction in valuation of available-for-sale portfolios and cash flow hedges to parallel movements of plus or minus 100 basis points in all yield curves.

	RM'000			
	31-Dec-16		31-Dec-15	
Basis point parallel shift in yield curve	***+100bps***	***-100bps***	*+100bps*	*-100bps*
RM	**(27,046)**	**27,046**	(30,349)	30,349

(v) Foreign exchange risk

Foreign exchange risk arises as a result of movements in the relative value of currencies. In addition to VAR and stress testing, the Bank controls the foreign exchange risk within the trading portfolio by limiting the open exposure to individual currencies, and on an aggregate basis.

	RM'000			
	31-Dec-16		31-Dec-15	
Appreciation/depreciation	***+1%***	***-1%***	*+1%*	*-1%*
Impact to profit after income tax expense	**(29)**	**29**	104	(104)

Change in foreign exchange rate has no impact to other comprehensive income as at the reporting date (2015: NIL).

4 Financial risk management (Cont'd)

d) Market risk management (Cont'd)

(v) Foreign exchange risk (Cont'd)

The Bank measures the foreign exchange sensitivity based on the foreign exchange net open positions (including foreign exchange structural position) under an adverse movement in all foreign currencies against the functional currency – RM. The result implies that the Bank may be subject to additional translation (losses)/gains if the RM appreciates against other currencies and vice versa.

(vi) Specific issuer risk

Specific issuer (credit spread) risk arises from a change in the value of debt instruments due to a perceived change in the credit quality of the issuer or underlying assets. As well as VAR and stress testing, the Bank manages the exposure to credit spread movements within the trading portfolios through the use of limits referenced to the sensitivity of the present value of a basis point movement in credit spreads.

(vii) Equity risk

Equity risk arises from the holding of open positions, either long or short, in equities or equity based instruments, which create exposure to a change in the market price of the equities or underlying equity instruments. All equity derivative trades in the Bank are traded on a back-to-back basis with HSBC group offices and therefore have no open exposure.

e) Operational risk management

The Group Operational Risk function and the operational risk management framework (ORMF) assist business management in discharging their responsibilities. The ORMF defines minimum standards and processes, and the governance structure for operational risk and internal control across the Bank.

(i) Three lines of defence

The Three Lines of Defence model is used to delineate management accountabilities and responsibilities over risk management and the control environment, thereby creating a robust control environment to manage inherent risks.

The model underpins our approach to strong risk management by defining responsibilities, encouraging collaboration and enabling efficient coordination of risk and control activities.

The three lines consists of:
- The first line of defence owns the risks and is responsible for identifying, recording, reporting and managing them and ensuring that the right controls and assessments are in pace to mitigate these risks.
- The second line of defence sets the policy and guidelines for managing the risks and provides advice, guidance and challenge to the first line of defence on effective risk management.
- The third line of defence is Internal Audit which helps the Board and Executive Committee to protect the assets, reputation and sustainability of the Bank.

Activity to strengthen our operational risk culture and to better embed the use of our ORMF continued in 2016. In particular, we continued to streamline our operational risk management processes, procedures and tool sets to provide more forward-looking risk insights and more effective operation of the ORMF.

Articulating our risk appetite for material operational risks helps business understand the level of risk our organisation is willing to accept. Monitoring operational risk exposure against risk appetite on a regular basis and implementing our risk acceptance process drives risk awareness in a more forward-looking manner. It assists management in determining whether further action is required.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

4 Financial risk management (Cont'd)

e) Operational risk management (Cont'd)

(ii) Other featured operational risks

- *Challenges to achieving the Bank's strategy in a downturn*: businesses and countries have prioritised strategy and annual operating plans to reflect current economic conditions amid increased geo-political risk. Performance against plan is monitored through a number of means including the use of risk consideration and performance reporting at all relevant management committees.

- *Internal and external fraud risks*: the threat of fraud perpetrated by or against our customers, especially in retail and commercial banking, may increase during adverse economic conditions. We have increased monitoring, root cause analysis and review of internal controls to enhance our defences against external attacks and reduce the level of loss in these areas. In addition, HSBC Group Security and Fraud Risk is working closely with the global businesses to continually assess these threats as they evolve and adapt our controls to mitigate them. The Bank is also exposed to potential criminal activities and has invested heavily in improving its customer due diligence and transaction monitoring and screening controls.

- *Third party risks:* the Bank has procedures in place to conduct due diligence and monitor the performance of third party suppliers and service providers in so far as they may affect the Bank's ability service its customers.

- *Regulatory and financial crime compliance:* the Bank to respond to increasing demands or changes in regulatory and financial crime compliance requirements in the markets in which we operate remains a critical focus for the Bank. A Global Standards program is being rolled out to ensure implementation of critical regulatory and financial crime compliance requirements. Various conduct and values initiatives have also been initiated to ensure that exposures to mis-selling or market conduct abuses are minimised.

- *Level of change creating operational complexity*: operational stresses may occur during periods of growth as well as during volatile periods in a market downturn. The Operational Risk function engages with business management in business transformation initiatives to ensure the resilience of the internal control environment. This may involve thematic reviews of new initiatives and analysis of loss or indicator trends, as well as participation and discussion of issues or concerns at relevant governance or management committees.

- *Information security*: the security of our information and technology infrastructure is crucial for maintaining our banking applications and processes while protecting our customers and the HSBC brand. A failure of our defences against such attacks could result in financial loss, loss of customer data and other sensitive information which could undermine both our reputation and our ability to retain the trust of our customers.

- *People Risk*: attracting and retaining staff with appropriate skills and expertise across the markets in which we operate remains a challenge. Significant investment is made in training and management development initiatives to equip our staff for the business changes we face and for the implementation of global standards.

In operationalising the operational risk management framework, the Bank operates a control-based environment in which processes are documented, authorisation is independent and transactions are reconciled and monitored. This is supported by an independent program of periodic reviews undertaken by the Internal Audit function, and by monitoring external operational risk events, which ensures that the Bank stay in line with best practice and takes account of lessons learned from publicised operational failures within the financial services industry.

The Bank adheres to the HSBC Operational Risk Management Framework. This is a set of tools, processes and activities owned by the independent Operational Risk function and used by global business and global functions to support the management of operational risk across the bank. The framework outlines how HSBC manages operational risk by identifying, assessing, monitoring, controlling and mitigating its material risks, rectifying operational risk vulnerabilities and implementing any additional procedures required for compliance with local statutory requirements. The framework covers the following:

- operational risk management responsibility is assigned at Senior Management level within the business operation;
- information systems are used to record the identification and assessment of operational risks and generate appropriate, regular management reporting;

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

4 Financial risk management (Cont'd)

e) Operational risk management (Cont'd)

(ii) Other featured operational risks (Cont'd)

- operational risks are identified by assessments covering operational risks facing each business and risk inherent in processes, activities and products. Risk assessment incorporates a regular review of identified risks to monitor significant changes;
- operational risk loss data is collected and reported to Senior Management. Aggregate operational risk losses are recorded and details of incidents above a materiality threshold are reported to the Risk Management Committee, the Board Risk Committee and Audit Committee, as well as Regional Head of Operational Risk Management Asia Pacific; and
- risk mitigation, including insurance, is considered where this is cost-effective.

The Bank maintains and tests contingency facilities to support operations in the event of disasters. Additional reviews and tests are conducted in the event that the Bank are affected by a business disruption event to incorporate lessons learned in the operational recovery from those circumstances.

f) Capital management

Our approach to capital management is driven by our strategic and organisational requirements, taking into account the regulatory, economic and commercial environment in which we operate.

It is our objective to maintain a strong capital base to support the development of our business and to meet regulatory capital requirements at all times. The policy on capital management is underpinned by a capital management framework, which enables us to manage our capital in a consistent manner.

Our capital management process is articulated in our annual capital plan which is approved by the Board. The plan is drawn up with the objective of maintaining both an appropriate amount of capital and an optimal mix between the different components of capital.

In accordance with Capital Management Framework, capital generated by subsidiaries in excess of planned requirements is returned to the parent companies, normally by way of dividends.

The principal forms of capital are included in the following balances on the balance sheet: share capital, other equity instruments, retained profits, other reserves, and subordinated liabilities.

(i) Externally imposed capital requirements

The Bank's regulatory capital is analysed in two tiers:

- Tier 1 capital is divided into Common Equity Tier 1 (CET1) Capital and Additional Tier 1 Capital. CET1 Capital includes ordinary share capital, share premium, capital redemption reserves, retained earnings, statutory reserves and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes. The Bank does not have any Additional Tier 1 Capital as at 31 December 2016.

- Tier 2 capital, which includes qualifying subordinated liabilities, collective impairment allowances (excluding collective impairment allowances attributable to financing classified as impaired), regulatory reserve, and the element of the fair value reserve relating to revaluation of property.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

4 Financial risk management (Cont'd)

(ii) Basel III

The Bank are required to comply with BNM's Capital Adequacy Framework (Capital Components) Guideline for the purpose of computing regulatory capital adequacy ratios. Under the said Guideline, the Bank are required to maintain the minimum capital adequacy ratios for Common Equity Tier 1 (CET1), Tier 1 and Total Capital Ratios of 4.5%, 6.0% and 8.0% respectively.

With effect from 1 January 2016, banking institutions are also required to maintain capital buffers above the minimum capital adequacy ratios. The capital buffer requirements comprise Capital Conservation Buffer (CCB) of 2.5%, which is to be phased-in from 2016 to 2019, and the Countercyclical Capital Buffer (CCyB) ranging between 0% to 2.5%. CCB is intended to build up capital buffers by individual banking institutions during normal times that can be drawn down during stress periods while CCyB is intended to protect the banking sector as a whole from the build-up of systemic risk during an economic upswing when aggregate credit growth tends to be excessive.

In addition, the Bank are also required to set further buffers to reflect risks not included in the regulatory capital calculation, arising from internal assessment of risks and the results of stress tests.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

5 Use of estimates and judgments

a) Impairment of financing and advances

The results of the Bank are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. The significant accounting policies used in the preparation of the financial statements are described in Note 3 to the financial statements.

The accounting policies that are deemed critical to the Bank's results and financial position, in terms of the materiality of the items to which the policy is applied, and which involve a high degree of judgment including the use of assumptions and estimation, are discussed below. The Bank's accounting policy for losses arising from the impairment of customer financing and advances is described in Note 3(k) to the financial statements. Financing impairment allowances represent management's best estimate of losses incurred in the financing portfolios at the reporting date.

The specific counterparty component of the total allowances for impairment applies to financial assets evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgments about a counterparty's financial situation and the net realisable value of any underlying collateral. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently approved by the Credit Risk function.

b) Fair value of financial instruments carried at fair value

The accounting policies which determine the classification of financial instruments and the use of assumptions and estimation in valuing them are described in Note 3(e)(vi) to the financial statements. The fair value of financial instruments is generally measured on the basis of the individual financial instrument. However, in cases where the Bank manages a group of financial assets and financial liabilities on the basis of its net exposure to either market risks or credit risk, the Bank measures the fair value of the group of financial instruments on a net basis, but presents the underlying financial assets and liabilities separately in the financial statements, unless they satisfy the MFRS offsetting criteria as described in Note 3(e)(iv) to the financial statements.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The following table sets out the financial instruments carried at fair value.

	Level 1	Level 2	Level 3	Total
2016	**RM'000**	**RM'000**	**RM'000**	**RM'000**
Financial Assets Held-for-Trading (Note 7)	**488**	**-**	**-**	**488**
Financial Investments Available-for-Sale (Note 8)	**1,368,574**	**-**	**-**	**1,368,574**
Derivative financial assets (Note 11)	**4**	**395,744**	**-**	**395,748**
	1,369,066	**395,744**	**-**	**1,764,810**
Trading liabilities[1]	**-**	**969,409**	**-**	**969,409**
Derivative financial liabilities (Note 11)	**4**	**490,751**	**-**	**490,755**
	4	**1,460,160**	**-**	**1,460,164**
2015				
Financial Assets Held-for-Trading (Note 7)	10,492	-	-	10,492
Financial Investments Available-for-Sale (Note 8)	1,701,243	-	-	1,701,243
Derivative financial assets (Note 11)	-	307,299	-	307,299
	1,711,735	307,299	-	2,019,034
Trading liabilities[1]	-	1,177,159	91,498	1,268,657
Derivative financial liabilities (Note 11)	101	467,443	5,687	473,231
	101	1,644,602	97,185	1,741,888

[1] *Trading liabilities consist of Islamic structured products classified as trading, net short position in securities form part of the balance disclosed under Note 20 (Other Liabilities).*

5 Use of estimates and judgments (Cont'd)

b) Fair value of financial instruments carried at fair value(Cont'd)

(i) Control framework

Fair values are subject to a control framework that aims to ensure that they are either determined, or validated, by a function independent of the risk-taker.

For all financial instruments where fair values are determined by reference to externally quoted prices or observable pricing inputs to models, independent price determination or validation is utilised. In inactive markets, direct observation of a traded price may not be possible. In these circumstances, the Bank will source alternative market information to validate the financial instrument's fair value, with greater weight given to information that is considered to be more relevant and reliable. The factors that are considered in this regard are, inter alia:

- the extent to which prices may be expected to represent genuine traded or tradable prices;
- the degree of similarity between financial instruments;
- the degree of consistency between different sources;
- the process followed by the pricing provider to derive the data;
- the elapsed time between the date to which the market data relates and the balance sheet date; and
- the manner in which the data was sourced.

For fair values determined using valuation models, the control framework may include, as applicable, development or validation by independent support functions of (i) the logic within valuation models; (ii) the inputs to those models; (iii) any adjustments required outside the valuation models; and (iv) where possible, model outputs. Valuation models are subject to a process of due diligence and calibration before becoming operational and are calibrated against external market data on an on-going basis.

To this end, ultimate responsibility for the determination of fair values lies within the Finance function, which reports functionally to the HSBC Group Finance Director. Finance establishes the accounting policies and procedures governing valuation, and is responsible for ensuring that these comply with all relevant accounting standards.

(ii) Determination of fair value of financial instruments carried at fair value

Fair values are determined according to the following hierarchy:

- Level 1 – Quoted market price

  Financial instruments with quoted prices for identical instruments in active markets that the Bank can access at the measurement date.

- Level 2 – Valuation technique using observable inputs

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

- Level 3 – Valuation technique with significant unobservable inputs

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

  The judgment as to whether a market is active may include, but is not restricted to, the consideration of factors such as the magnitude and frequency of trading activity, the availability of prices and the size of bid/offer spreads. The bid/offer spread represents the difference in prices at which a market participant would be willing to buy compared with the price at which they would be willing to sell. In inactive markets, obtaining assurance that the transaction price provides evidence of fair value or determining the adjustments to transaction prices that are necessary to measure the fair value of the instrument requires additional work during the valuation process.

5 Use of estimates and judgments (Cont'd)

b) Fair value of financial instruments carried at fair value (Cont'd)

(iii) Valuation techniques

Valuation techniques incorporate assumptions about factors that other market participants would use in their valuations. A range of valuation techniques is employed, dependent upon the instrument type and available market data. Most valuation techniques are based upon discounted cash flow analysis, in which expected future cash flows are calculated and discounted to present value using a discounting curve. Prior to consideration of credit risk, the expected future cash flows may be known, as would be the case for the fixed leg of an profit rate swap, or may be uncertain and require projection, as would be the case for the floating leg of an profit rate swap. Projection uses market forward curves, if available. In option models, the probability of different potential future outcomes must be considered. In addition, the values of some products are dependent upon more than one market factor, and in these cases it will typically be necessary to consider how movements in one market factor may impact the other market factors. The model inputs necessary to perform such calculations include profit rate yield curves, exchange rates, volatilities, correlations, prepayment and default rates.

The majority of valuation techniques employ only observable market data. However, certain financial instruments are valued on the basis of valuation techniques that feature one or more significant market inputs that are unobservable, and for them the measurement of fair value is more judgmental. If, in the opinion of management an instrument in its entirety is classified as valued using significant unobservable inputs, a significant proportion of the instrument's inception profit ('day 1 gain or loss') or greater than 5% of the instrument's carrying value is driven by unobservable inputs. 'Unobservable' in this context means that there is little or no current market data available from which to determine the price at which an arm's length transaction would be likely to occur. It generally does not mean that there is no market data available at all upon which to base a determination of fair value (consensus pricing data may, for example, be used). All fair value adjustments are included within the levelling determination.

Structured notes issued and certain other hybrid instrument liabilities are included within trading liabilities and are measured at fair value. The credit spread applied to these instruments is derived from the spreads at which the Bank issues structured notes.

Gains and losses arising from changes in the credit spread of liabilities issued by the Bank reverse over the contractual life of the debt, provided that the debt is not paid at a premium or a discount.

Changes in fair value are generally subject to a profit and loss analysis process. This process disaggregates changes in fair value into three high level categories; (i) portfolio changes, such as new transactions or maturing transactions, (ii) market movements, such as changes in foreign exchange rates or equity prices, and (iii) other, such as changes in fair value adjustments, discussed below.

(iv) Fair value adjustments

Fair value adjustments are adopted when the Bank determines that there are additional factors that would be considered relevant by a market participant that are not incorporated within the valuation model. The Bank classifies fair value adjustments as either 'risk-related' or 'model-related'. The majority of these adjustments are related to Global Banking and Markets.

Movements in the level of fair value adjustments do not necessarily result in the recognition of profits or losses within the income statement such as when models are enhanced, fair value adjustments may no longer be required. Similarly, fair value adjustments will decrease when the related positions are unwound.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

5 Use of estimates and judgments (Cont'd)

b) Fair value of financial instruments carried at fair value (Cont'd)

(iv) Fair value adjustments (Cont'd)

- **Risk-related adjustments**

(i) Bid-offer

MFRS 13 requires use of the price within the bid-offer spread that is most representative of fair value. Valuation models will typically generate mid-market values. The bid-offer adjustment reflects the extent to which bid-offer cost would be incurred if substantially all residual net portfolio market risks were closed using available hedging instruments or by disposing of, or unwinding the position.

(ii) Uncertainty

Certain model inputs may be less readily determinable from market data, and/or the choice of model itself may be more subjective. In these circumstances, there exists a range of possible values that the financial instrument or market parameter may assume and an adjustment may be necessary to reflect the likelihood that in estimating the fair value of the financial instrument, market participants would adopt more conservative values for uncertain parameters and/or model assumptions than those used in the HSBC's Group valuation model.

(iii) Credit valuation adjustment (CVA)

The CVA is an adjustment to the valuation of over-the-counter (OTC) derivative contracts to reflect within fair value the possibility that the counterparty may default and the Bank may not receive the full market value of the transactions. Further detail is provided below.

(iv) Debit valuation adjustment (DVA)

The DVA is an adjustment to the valuation of over-the-counter derivative contracts to reflect within fair value the possibility that the Bank may default, and that the Bank may not pay full market value of the transactions.

(v) Funding fair value adjustment (FFVA)

The FFVA is calculated by applying future market funding spreads to the expected future funding exposure of any uncollateralised component of the OTC derivative portfolio. This includes the uncollateralised component of collateralised derivatives in addition to derivatives that are fully uncollateralised. The expected future funding exposure is calculated by a simulation methodology, where available and is adjusted for events that may terminate the exposure such as the default of the group or the counterparty. The FFVA and DVA are calculated independently.

- **Model-related adjustments**

(i) Model limitation

Models used for portfolio valuation purposes may be based upon a simplifying set of assumptions that do not capture all material market characteristics. Additionally, markets evolve, and models that were adequate in the past may require development to capture all material market characteristics in current market conditions. In these circumstances, model limitation adjustments are adopted. As model development progresses, model limitations are addressed within the valuation models and a model limitation adjustment is no longer needed.

(ii) Inception profit (Day 1 profit or loss reserves)

Inception profit adjustments are adopted where the fair value estimated by a valuation model is based on one or more significant unobservable inputs.

5 Use of estimates and judgments (Cont'd)

b) Fair value of financial instruments carried at fair value (Cont'd)

(iv) Fair value adjustments (Cont'd)

- **Credit valuation adjustment/ debit valuation adjustment methodology**

  The Bank calculates a separate CVA and DVA for each counterparty to which the Bank has exposure.

  The Bank calculates the CVA by applying the probability of default (PD) of the counterparty, conditional on the non-default of the Bank, to the expected positive exposure of the Bank to the counterparty and multiplying the result by the loss expected in the event of default. Conversely, the Bank calculates the DVA by applying the PD of the Bank, conditional on the non-default of the counterparty, to the expected positive exposure of the counterparty to the Bank, and multiplying the result by the loss expected in the event of default. Both calculations are performed over the life of the potential exposure.

  For most products, the Bank uses a simulation methodology to calculate the expected positive exposure to a counterparty. This incorporates a range of potential exposures across the portfolio of transactions with the counterparty over the life of the portfolio. The simulation methodology includes credit mitigants such as counterparty netting agreements and collateral agreements with the counterparty.

  The methodologies do not, in general, account for 'wrong-way risk'. Wrong-way risk arises when the underlying value of the derivative prior to any CVA is positively correlated to the PD by the counterparty. When there is significant wrong-way risk, a trade-specific approach is applied to reflect this risk in the valuation.

  With the exception of certain central clearing parties, the Bank includes all third-party counterparties in the CVA and DVA calculations and does not net these adjustments across the Bank's entities. During the year, the Bank refined the methodologies used to calculate the CVA and DVA to more accurately reflect credit mitigation. The Bank reviews and refines the CVA and DVA methodologies on an ongoing basis.

- **Valuation of uncollateralised derivatives**

  In line with evolving industry practice, funding fair value adjustment (FFVA) reflects the funding of uncollateralised derivative exposure at rates other than overnight indexed swap rate (OIS). As at 31 December 2016, the FFVA was -RM5.0m (2015: -RM4.9m) for the Bank, which has a one-off impact on trading revenue. This is an area in which a full industry consensus has not yet emerged. The Bank will continue to monitor industry evolution and refine the calculation methodology as necessary.

5 Use of estimates and judgments (Cont'd)

b) Fair value of financial instruments carried at fair value (Cont'd)

(v) Reconciliation of fair value measurements in Level 3 of the fair value hierarchy

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

	2016			2015		
	Derivative financial assets	**Derivative financial liabilities**	**Trading Liabilities**	Derivative financial assets	Derivative financial liabilities	Trading Liabilities
RM'000						
Balance at 1 January	**-**	**5,687**	**91,498**	2,561	4,582	292,381
Total gains or losses in profit or loss	**-**	**420[1]**	**(624)[2]**	(2,561)[1]	22,385[1]	(18,183)[2]
Issues	**-**	**-**	**-**	-	-	85,525
Settlements	**-**	**-**	**(12,146)**	-	-	(239,698)
Transfer out of Level 3	**-**	**(6,107)**	**(78,728)**	-	(21,280)	(28,527)
Balance at 31 December	**-**	**-**	**-**	-	5,687	91,498

[1] Denotes losses in the Profit or Loss
[2] Denotes gains in the Profit or Loss

Transfers between levels of the fair value hierarchy are deemed to occur at the end of the reporting period.

For derivative financial assets/liabilities, transfers out of level 3 were due to the maturity of the derivatives or as a result of early termination.

For trading liabilities, transfers out of level 3 resulted from maturity or early termination of the instruments.

For trading liabilities, realised and unrealised gains and losses are presented in profit or loss under "Net trading income'.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

5 Use of estimates and judgments (Cont'd)

b) Fair value of financial instruments carried at fair value (Cont'd)

(v) Reconciliation of fair value measurements in Level 3 of the fair value hierarchy (Cont'd)

Total gains or losses included in profit or loss for the financial year in the above tables are presented in the statements of comprehensive income as follows:

2016 **RM'000**	**Derivative financial assets**	**Derivative financial liabilities**	**Trading liabilities**
Total gains or losses included in profit or loss for the financial year ended:			
-Net trading income	**-**	**-**	**66,104**[1]
Total gains or losses for the year ended included in profit or loss for assets and liabilities held at the end of the financial year			
-Net trading income	**-**	**420**[1]	**(66,728)**[2]
2015 RM'000			
Total gains or losses included in profit or loss for the financial year ended:			
-Net trading income	(2,562)[1]	-	6,283[1]
Total gains or losses for the year ended included in profit or loss for assets and liabilities held at the end of the financial year			
-Net trading income	-	22,385[1]	(24,466)[2]

[1] Denotes losses in the Profit or Loss
[2] Denotes gains in the Profit or Loss

(vi) Quantitative information about significant unobservable inputs in Level 3 valuations

Level 3 fair values are estimated using unobservable inputs for the financial assets and liabilities. The following table shows the valuation techniques used in the determination of fair values within Level 3 for the current year, as well as the key unobservable inputs used in the valuation models.

Type of Financial Instrument	Valuation Technique	Key unobservable inputs	Range of estimates for unobservable input
Trading liabilities	Option model	Foreign currency volatility	**2016 : -** [1] 2015 : 4.91% - 20.47%
		Long term equity volatility	**2016 : -** [1] 2015 : 21.73%[2]

[1] During 2016, all Islamic structured products under Level 3 have been transferred out.
[2] Upper and lower ranges are the same.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

5 Use of estimates and judgments (Cont'd)

b) Fair value of financial instruments carried at fair value (Cont'd)

(vii) Key unobservable inputs to Level 3 financial instruments

- **Volatility**

Volatility is a measure of the anticipated future variability of a market price. Volatility tends to increase in stressed market conditions, and decrease in calmer market conditions. Volatility is an important input in the pricing of options. In general, the higher the volatility, the more expensive the option will be. This reflects both the higher probability of an increased return from the option, and the potentially higher costs that the Bank may incur in hedging the risks associated with the option. If option prices become more expensive, this will increase the value of the Bank's long option positions (i.e. the positions in which the Bank has purchased options), while the Bank's short option positions (i.e. the positions in which the Bank has sold options) will suffer losses.

Volatility varies by underlying reference market price, and by strike and maturity of the option. Certain volatilities, typically those of a longer-dated nature, are unobservable. The unobservable volatility is then estimated from observable data. For example, longer-dated volatilities may be extrapolated from shorter-dated volatilities.

The range of unobservable volatilities quoted in the table reflects the wide variation in volatility inputs by reference to market price. For example, foreign exchange volatilities for a pegged currency may be very low, whereas for non-managed currencies the foreign exchange volatility may be higher. As a further example, volatilities for deep-in-the money or deep-out-of-the-money equity options may be significantly higher than at-the-money options. For any single unobservable volatility, the uncertainty in the volatility determination is significantly less than the range quoted above.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

6 Cash and Short-Term Funds

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Cash and balances with banks and other financial institutions	**189,591**	369,010
Money at call and interbank placements maturing within one month	**2,170,000**	4,381,380
	2,359,591	4,750,390

7 Financial Assets Held-for-Trading

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
At fair value		
Money market instruments:		
Malaysian Government Islamic bonds	**488**	490
Unquoted:		
Sukuk	**-**	10,002
	488	10,492

Credit quality of financial assets held-for-trading based on the ratings of Standard & Poor's on the counterparty:

	Rating		
Money market instruments:			
Malaysian Government Islamic bonds	*A+ to A-*	**488**	490
Unquoted securities:			
Sukuk	- [1]	**-**	10,002
A+ to A-			
		488	10,492

[1] Rated separately by another rating agency

All the financial assets held-for-trading as disclosed above are not pledged to any counterparties.

8 Financial Investments Available-for-Sale

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
At fair value		
Money market instruments:		
Malaysian Government Islamic bonds	**1,368,574**	1,701,243

The maturity structure of money market instruments held as financial investments available-for-sale is as follows:

Maturing within one year	**180,224**	171,710
More than one year to three years	**732,449**	1,310,874
More than three years to five years	**435,846**	218,659
Over five years	**20,055**	-
	1,368,574	1,701,243

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

9 Financing and Advances

(i) By type and Shariah contracts

At amortised cost	Sale-based contracts			Lease-based contracts		Equity-based contracts		
	Commodity Murabahah	Bai Bithaman Ajil	Bai Al-Inah	Ijarah	Ijarah Thumma Al-Bai	Diminishing Musharakah	Ujrah	Total
31 Dec 2016	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
Cash line-i	97,840	-	-	-	-	-	-	97,840
Term financing:								
House financing	-	404	-	-	-	4,356,230	-	4,356,634
Hire purchase receivables	-	-	-	-	208,921	-	-	208,921
Lease receivables	-	-	-	2,738	-	-	-	2,738
Syndicated term financing	650,266	-	-	-	-	-	-	650,266
Other term financing	2,834,338	8,115	350	-	-	1,025,887	-	3,868,690
Trust receipts	462,235	-		-	-	-	-	462,235
Claims on customers under acceptance credits	504,375	-	-	-	-	-	-	504,375
Bills receivables	110,272	-	-	-	-	-	-	110,272
Staff financing-i	2,617	-	361	-	-	3,215	-	6,193
Credit cards-i	-	-	-	-	-	-	787,710	787,710
Revolving credit	950,161	-	-	-	-	-	-	950,161
Gross financing and advances	5,612,104	8,519	711	2,738	208,921	5,385,332	787,710	12,006,035
Less: Allowance for impaired financing								
Collective allowances for impairment								(200,015)
Individual allowances for impairment								(62,757)
Total net financing and advances								11,743,263

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

9 Financing and Advances (Cont'd)

(i) By type and Shariah contracts (Cont'd)

	Sale-based contracts			Lease-based contracts		Equity-based contracts		
31 Dec 2015	Commodity Murabahah RM'000	Bai Bithaman Ajil RM'000	Bai Al-Inah RM'000	Ijarah RM'000	Ijarah Thumma Al-Bai RM'000	Diminishing Musharakah RM'000	Ujrah RM'000	Total RM'000
Cash line-i	90,400	-	-	-	-	-	-	90,400
Term financing:								
House financing	-	1,179	-	-	-	4,207,587	-	4,208,766
Hire purchase receivables	-	-	-	-	229,552	-	-	229,552
Lease receivables	-	-	-	4,103	-	-	-	4,103
Syndicated term financing	954,559	-	-	-	-	-	-	954,559
Other term financing	2,818,469	25,973	31,784	-	-	992,306	-	3,868,532
Trust receipts	603,681	-	-	-	-	-	-	603,681
Claims on customers under acceptance credits	617,460	-	-	-	-	-	-	617,460
Bills receivables	216,510	-	-	-	-	-	-	216,510
Staff financing-i	3,468	-	775	-	-	3,266	-	7,509
Credit cards-i	-	-	-	-	-	-	569,358	569,358
Revolving credit	806,698	-	-	-	-	-	-	806,698
Gross financing and advances	6,111,245	27,152	32,559	4,103	229,552	5,203,159	569,358	12,177,128
Less: Allowance for impaired financing								
Collective allowances for impairment								(140,264)
Individual allowances for impairment								(68,647)
Total net financing and advances								11,968,217

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

9 Financing and Advances (Cont'd)

(ii) By type of customer

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Domestic non-bank financial institutions	**638,263**	670,298
Domestic business enterprises:		
Small medium enterprises	**1,821,064**	2,004,648
Others	**2,397,737**	2,944,504
Government and statutory bodies	**10,316**	13,566
Individuals	**5,901,851**	5,431,238
Other domestic entities	**1,466**	1,568
Foreign entities	**1,235,338**	1,111,306
	12,006,035	12,177,128

(iii) By profit rate sensitivity

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Fixed rate:		
House financing	**398**	1,135
Hire purchase receivables	**208,921**	229,552
Other financing	**2,784,299**	2,840,103
Variable rate:		
BR/BFR plus	**5,471,227**	5,277,948
Cost-plus	**3,541,190**	3,828,390
	12,006,035	12,177,128

(iv) By residual contractual maturity

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Maturing within one year	**4,356,186**	4,532,866
More than one year to three years	**654,513**	642,702
More than three years to five years	**1,111,456**	1,490,233
Over five years	**5,883,880**	5,511,327
	12,006,035	12,177,128

9 Financing and Advances (Cont'd)

(v) By sector

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Agriculture, hunting, forestry & fishing	**136,372**	624,260
Mining and quarrying	**218,194**	206,294
Manufacturing	**1,187,941**	1,306,244
Electricity, gas and water	**32,907**	14,772
Construction	**354,645**	597,155
Real estate	**821,854**	392,934
Wholesale & retail trade, restaurants & hotels	**816,323**	1,088,766
Transport, storage and communication	**186,721**	166,443
Finance, takaful and business services	**929,714**	1,035,462
Household - Retail	**6,536,695**	6,073,723
Others	**784,669**	671,075
	12,006,035	12,177,128

(vi) By purpose

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Purchase of landed property:		
Residential	**4,359,849**	4,212,033
Non-residential	**853,008**	840,581
Purchase of transport vehicles	**1,847**	2,122
Purchase of fixed assets excluding land & building	**366**	3,706
Consumption credit	**1,893,592**	1,588,371
Construction	**343,443**	586,283
Working capital	**3,943,120**	4,461,645
Other purpose	**610,810**	482,387
	12,006,035	12,177,128

(vii) By geographical distribution

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Northern Region	**1,405,240**	1,448,803
Southern Region	**1,569,412**	1,638,669
Central Region	**8,565,903**	8,609,131
Eastern Region	**465,480**	480,525
	12,006,035	12,177,128

Concentration by location for financing and advances is based on the location of the customer.
The Northern region consists of the states of Perlis, Kedah, Penang, Perak, Pahang, Kelantan and Terengganu.
The Southern region consists of the states of Johor, Malacca and Negeri Sembilan.
The Central region consists of the states of Selangor and the Federal Territory of Kuala Lumpur.
The Eastern region consists of the states of Sabah, Sarawak and the Federal Territory of Labuan.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

9 Financing and Advances (Cont'd)

(viii) Assets under Management

The details of assets under management in respect of the Restricted Investment Account (RPSIA) and Syndicated Investment Agency Financing (SIAF)/Investment Agency Account (IAA) financing are as below. The exposures and the corresponding risk weighted amount are reported in investors' financial statements.

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Under SIAF/IAA arrangement	**1,733,132**	1,573,615
Under RPSIA arrangement	**-**	19,918
Total net financing and advances	**1,733,132**	1,593,533

Principal amount	**31 Dec 2016 RM'000**	31 Dec 2015 RM'000
Irrevocable commitments to extend credit:		
Maturity not exceeding one year		
Under SIAF/IAA arrangement	**496,933**	180,273
Under RPSIA arrangement	**-**	858,598
Total commitments and contingencies	**496,933**	1,038,871

	Principal RM'000	**Risk weighted RM'000**
Total RWA for Credit Risk		
- **at 31 Dec 2016**		
Under SIAF/IAA arrangement	**1,832,519**	**1,832,519**
- at 31 Dec 2015		
Under SIAF/IAA arrangement	1,609,670	1,609,670
Under RPSIA arrangement	191,638	191,638
	1,801,308	1,801,308

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

9 Financing and Advances (Cont'd)

(viii) Assets under Management (Cont'd)

The RPSIA is with the Bank's holding company, HSBC Bank Malaysia Berhad (HBMY), and the contract is based on the Mudharabah principle where HBMY provides the funds, whilst the assets are managed by the Bank. The profits of the underlying assets are shared based on pre-agreed ratios, whilst risks on the financing are borne by HBMY. Hence, the underlying assets and allowances for impairment arising thereon, if any, are recognised and accounted for by HBMY. Effective 31 March 2015, SIAF/IAA replaces RPSIA for new financing and advances.

The SIAF/IAA arrangement is based on the Wakalah principle where HBMY, solely or together with other financial institutions provide the funds, whilst the assets are managed by the Bank (as the Wakeel or agent). However, in the arrangement, the profits of the underlying assets are recognised by HBMY and the other financial institutions proportionately in relation to the funding provided in the syndication arrangement. At the same time, risks on the financing are also proportionately borne by HBMY and the other financial institutions. Hence, the underlying assets and allowances for impairment arising thereon, if any, are proportionately recognised and accounted for by HBMY and the other financial institutions.

The recognition and derecognition treatments of the above are in accordance to Note 3(e) on financial instruments.

10 Impaired Financing

(i) Movements in impaired financing and advances

	31 Dec 2016	31 Dec 2015
	RM'000	RM'000
Balance at 1 January	**235,279**	162,227
Classified as impaired during the financial year	**358,706**	319,623
Reclassified as performing	**(122,829)**	(109,381)
Amount recovered	**(49,831)**	(54,894)
Amount written off	**(117,799)**	(82,296)
Balance at 31 December	**303,526**	235,279

(ii) Movements in allowance for impaired financing

	31 Dec 2016	31 Dec 2015
	RM'000	RM'000
Collective allowance for impairment		
Balance at 1 January	**140,264**	124,817
Made during the financial year	**211,487**	160,940
Amount released	**(58,264)**	(67,064)
Amount written off	**(93,472)**	(78,429)
Balance at 31 December	**200,015**	140,264

	31 Dec 2016	31 Dec 2015
	RM'000	RM'000
Individual allowance for impairment		
Balance at 1 January	**68,647**	43,821
Made during the financial year	**30,041**	45,829
Amount released	**(18,115)**	(27,717)
Amount written off	**(17,816)**	6,714
Balance at 31 December	**62,757**	68,647

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

10 Impaired Financing (Cont'd)

(iii) By contract

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Bai Bithaman Ajil *(deferred payment sale)*	**5**	69
Ijarah Thumma Al-Bai (AITAB) *(hire purchase)*	**5,730**	7,049
Murabahah *(cost-plus)*	**127,743**	102,339
Musharakah (*profit and loss sharing)*	**152,729**	110,720
Bai Al-Inah *(sell and buy back)*	**217**	2,776
Ujrah *(fee-based)*	**17,102**	12,326
	303,526	235,279

(iv) By sector

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Manufacturing	**4,038**	21,093
Construction	**204**	204
Wholesale & retail trade, restaurants & hotels	**12,309**	9,672
Transport, storage and communication	**3,665**	5,443
Finance, takaful and business services	**23,346**	5,527
Household - Retail	**259,346**	192,687
Others	**618**	653
	303,526	235,279

(v) By purpose

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Purchase of landed property:		
Residential	**135,067**	94,984
Non-residential	**10,887**	10,255
Purchase of transport vehicles	**146**	133
Purchase of fixed assets excluding land & building	**358**	358
Consumption credit	**121,217**	95,770
Construction	**204**	204
Working capital	**35,647**	33,575
	303,526	235,279

(vi) By geographical distribution

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Northern Region	**47,713**	54,102
Southern Region	**30,606**	30,267
Central Region	**212,643**	141,764
Eastern Region	**12,564**	9,146
	303,526	235,279

11 Derivative Financial Instruments

Details of derivative financial instruments outstanding are as follows:

Derivative financial instruments measured at their fair values together with their corresponding contract/notional amounts:

	Contract / Notional Amount			Positive Fair Value			Negative Fair Value		
	Up to 1 Year	>1 - 5 Years	Total	Up to 1 Year	>1 - 5 Years	Total	Up to 1 Year	>1 - 5 Years	Total
31 Dec 2016	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
Trading derivatives:									
Foreign exchange contracts									
- Forwards	2,582,361	-	2,582,361	111,609	-	111,609	112,797	-	112,797
- Swaps	-	2,159,793	2,159,793	-	261,215	261,215	-	264,349	264,349
- Options	9,718	345,197	354,915	1,018	4,789	5,807	1,018	4,789	5,807
Profit rate related contracts									
- Swaps	1,200,000	4,770,174	5,970,174	470	14,075	14,545	384	8,906	9,290
- Options	-	189,444	189,444	-	2,545	2,545	-	135	135
Equity related contracts									
- Options purchased	765,236	109,766	875,002	27	-	27	95,176	2,180	97,356
Sub- total	4,557,315	7,574,374	12,131,689	113,124	282,624	395,748	209,375	280,359	489,734
Hedging Derivatives:									
Fair Value Hedge									
Profit rate related contracts									
- Swaps	90,000	190,000	280,000	-	-	-	59	962	1,021
Sub- total	90,000	190,000	280,000	-	-	-	59	962	1,021
Total	4,647,315	7,764,374	12,411,689	113,124	282,624	395,748	209,434	281,321	490,755

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

11 Derivative Financial Instruments (Cont'd)

	Contract / Notional Amount			Positive Fair Value			Negative Fair Value		
31 Dec 2015	Up to 1 Year RM'000	>1 - 5 Years RM'000	Total RM'000	Up to 1 Year RM'000	>1 - 5 Years RM'000	Total RM'000	Up to 1 Year RM'000	>1 - 5 Years RM'000	Total RM'000
Trading derivatives:									
Foreign exchange contracts									
- Forwards	2,389,269	-	2,389,269	59,414	-	59,414	54,748	-	54,748
- Swaps	-	1,676,892	1,676,892	-	228,113	228,113	-	232,103	232,103
- Options	48,046	349,125	397,171	-	4,918	4,918	-	4,918	4,918
Profit rate related contracts									
- Swaps	1,201,265	6,114,917	7,316,182	2,221	10,996	13,217	1,760	15,869	17,629
- Options	-	250,891	250,891	-	849	849	-	2,908	2,908
Equity related contracts									
- Options purchased	192,724	948,669	1,141,393	83	306	389	70,618	90,106	160,724
Sub- total	3,831,304	9,340,494	13,171,798	61,718	245,182	306,900	127,126	345,904	473,030
Hedging Derivatives:									
Fair Value Hedge									
Profit rate related contracts									
- Swaps	-	280,000	280,000	-	399	399	-	201	201
Sub- total	-	280,000	280,000	-	399	399	-	201	201
Total	3,831,304	9,620,494	13,451,798	61,718	245,581	307,299	127,126	346,105	473,231

Included in the net non-profit income is the net gains/(losses) arising from fair value hedges during the financial year as follows:

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Losses on hedging instruments	**(1,075)**	(632)
Gains on the hedged items attributable to the hedged risk	**654**	646
Net (losses)/ gains from fair value hedges	**(421)**	14

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

12 Other Assets

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Income receivable	**12,972**	12,037
Profit receivable	**6,059**	15,814
Prepayments	**72**	912
Amount due from holding company/related companies	**45,132**	209,358
Other receivables	**15,806**	3,490
	80,041	241,611

13 Statutory deposits with Bank Negara Malaysia

The non-profit bearing statutory deposits are maintained with Bank Negara Malaysia in compliance with Section 26(2)c and 26(3) of the Central Bank of Malaysia Act 2009, the amounts of which are determined at set percentages of total eligible liabilities.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

14 Equipment

2016	Office equipment, fixtures and fittings	Computer equipment	Motor vehicles	Total
	RM'000	RM'000	RM'000	RM'000
Cost				
Balance at 1 January	35,069	18,426	299	53,794
Additions	1,975	3	-	1,978
Disposals	-	(150)	-	(150)
Balance at 31 December	37,044	18,279	299	55,622
Accumulated depreciation				
Balance at 1 January	30,007	13,439	60	43,506
Charge for the financial year	3,083	1,886	60	5,029
Disposals	-	(150)	-	(150)
Balance at 31 December	33,090	15,175	120	48,385
Net book value at 31 December	3,954	3,104	179	7,237

2015	Office equipment, fixtures and fittings	Computer equipment	Motor vehicles	Total
	RM'000	RM'000	RM'000	RM'000
Cost				
Balance at 1 January	34,938	17,632	221	52,791
Additions	131	794	299	1,224
Written off	-	-	(221)	(221)
Balance at 31 December	35,069	18,426	299	53,794
Accumulated depreciation				
Balance at 1 January	25,081	11,327	169	36,577
Charge for the financial year	4,926	2,112	68	7,106
Written off	-	-	(177)	(177)
Balance at 31 December	30,007	13,439	60	43,506
Net book value at 31 December	5,062	4,987	239	10,288

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

15 Intangible assets

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Computer software		
Cost		
Balance at 1 January	**5,053**	5,093
Written off	**-**	(40)
Balance at 31 December	**5,053**	5,053
Accumulated depreciation		
Balance at 1 January	**5,053**	5091
Charge for the financial year	**-**	2
Written off	**-**	(40)
Balance at 31 December	**5,053**	5,053
Net book value at 31 December	**-**	-

16 Deferred Tax Assets

The amounts, prior to offsetting are summarised as follows:

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Deferred tax assets	**11,044**	7,581
Deferred tax liabilities	**(649)**	(2,033)
	10,395	5,548

Deferred tax assets and liabilities are offset where there is a legally enforceable right to set-off current tax assets against current tax liabilities.

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Deferred tax assets		
- settled more than 12 months	**5,040**	2,800
- settled within 12 months	**6,004**	4,781
Deferred tax liabilities		
- settled more than 12 months	**(298)**	(1,730)
- settled within 12 months	**(351)**	(303)
	10,395	5,548

The recognised deferred tax assets and liabilities (before offsetting) are as follows:

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Equipment capital allowances	**(649)**	(449)
Available-for-sale reserve	**2,067**	(1,562)
Provision for accrued expenses	**6,462**	7,457
Other temporary differences	**-**	124
Deferred income	**2,449**	-
Lease receivables	**66**	(22)
	10,395	5,548

16 Deferred Tax Assets (Cont'd)

The movements in temporary differences during the financial year are as follows:

2016	**Balance at 1 January RM'000**	**Recognised in profit or loss RM'000**	**Recognised in other comprehensive income RM'000**	**Balance at 31 December RM'000**
Available-for-sale reserve	**-**	**-**	**2,067**	**2,067**
Provision for accrued expenses	**7,457**	**(995)**	**-**	**6,462**
Deferred income	**-**	**2,449**	**-**	**2,449**
Lease receivables	**-**	**66**	**-**	**66**
Other temporary differences	**124**	**(124)**	**-**	**-**
Deferred Tax Assets	**7,581**	**1,396**	**2,067**	**11,044**
Equipment capital allowances	**(449)**	**(200)**	**-**	**(649)**
Lease receivables	**(22)**	**22**	**-**	**-**
Available-for-sale reserves	**(1,562)**	**-**	**1,562**	**-**
Deferred Tax Liabilities	**(2,033)**	**(178)**	**1,562**	**(649)**
Net Deferred Tax Assets	**5,548**	**1,218**	**3,629**	**10,395**
2015				
Available-for-sale reserve	2,049	-	(2,049)	-
Provision for accrued expenses	6,994	463	-	7,457
Deferred income	-	-	-	-
Lease receivables	-	-	-	-
Other temporary differences	23	101	-	124
Deferred Tax Assets	9,066	564	(2,049)	7,581
Equipment capital allowances	(1,273)	824	-	(449)
Lease receivables	(36)	14	-	(22)
Available-for-sale reserves	-	-	(1,562)	(1,562)
Deferred Tax Liabilities	(1,309)	838	(1,562)	(2,033)
Net Deferred Tax Assets	7,757	1,402	(3,611)	5,548

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

17 Tax Recoverable

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Tax recoverable	**10,285**	5,162

18 Deposits From Customers

(i) By type of deposit

At amortised cost	**31 Dec 2016 RM'000**	31 Dec 2015 RM'000
Non-Mudharabah Fund		
Demand deposits		
- Wadiah	**1,902,318**	1,857,231
Savings deposits		
- Wadiah	**1,627,182**	1,589,421
Fixed return investment deposits		
- Murabahah	**5,007,808**	5,799,059
- Qard	**129,452**	-
Islamic repurchase agreements		
- Bai Al-Inah	**59,783**	140,412
	8,726,543	9,386,123

The maturity structure of term deposits is as follows:

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Due within six months	**4,376,774**	4,906,663
More than six months to one year	**735,158**	848,285
More than one year to three years	**19,710**	42,063
More than three years to five years	**5,618**	2,048
	5,137,260	5,799,059

(ii) By type of customer

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Government and statutory bodies	**6,429**	8,848
Business enterprises	**2,026,165**	2,379,984
Individuals	**4,583,883**	5,065,914
Others	**2,110,066**	1,931,377
	8,726,543	9,386,123

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

19 Deposits and Placements from Banks and Other Financial Institutions

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Non-Mudharabah Fund		
Licensed banks	**1,923,186**	2,833,307
Bank Negara Malaysia	**28,416**	49,614
Other financial institutions	**-**	1,277,168
	1,951,602	4,160,089

Included in deposits and placements from banks and other financial institutions are placements from the Bank's parent company, HSBC Bank Malaysia Berhad, of RM1.9 billion (31 Dec 2015: RM2.8 billion).

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

20 Other Liabilities

	Note	**31 Dec 2016 RM'000**	31 Dec 2015 RM'000
At amortised cost			
Amounts due to holding company/ related companies		**36,472**	88
Profit payable			
- Structured products		**4,182**	5,375
- Others		**61,262**	74,233
Deferred income		**11,286**	11,376
Marginal deposit		**22,761**	18,457
Accrued expenses		**26,235**	30,349
Other creditors	(a)	**53,528**	66,840
		215,726	206,718
At fair value			
Structured products, at fair value			
- Wakalah with Commodity Wa'ad	(b)	**969,409**	1,268,657
		1,185,135	1,475,375

Structured products are measured at fair value over the life of the instruments. Structured products are deposits with embedded derivatives, of which both profit paid and fair valuation on the structured products are recorded in other operating income, as per accounting policy in Note 3(h), and respective fair value on trading liabilities is shown in Note 5(b).

(a) Other creditors and accruals

Included in other creditors and accruals is excess compensation balance and profit earned from inadvertent Shariah non-compliant activities. The contribution was distributed to the Non-Governmental Organisations approved by the Shariah Committee during the financial year.

Source and use of charity funds

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Source of charity funds		
Balance at 1 January	**70**	165
Shariah non-compliant income for the financial year	**114**	135
Use of charity funds		
Contribution to non-profit organisations	**(93)**	(230)
Tax expense on Shariah non-compliant income	**(87)**	-
Balance at 31 December	**4**	70

(b) Movement in structured products

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Balance at 1 January	**1,268,657**	-
Reclassified from deposits from customers	**-**	1,788,427
New placement during the financial year	**239,166**	2,724,356
Redemption during the financial year	**(605,818)**	(3,108,048)
Fair value mark-to-market	**67,404**	(136,078)
Balance at 31 December	**969,409**	1,268,657

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

21 Multi-Currency Sukuk Programme

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Multi-Currency Sukuk Programme (MCSP)	**1,756,001**	1,749,823

The Bank issued the following series of 5-year unsecured Sukuk under its RM3 billion MCSP.

Issuance under MCSP	Nominal Value RM'000	Issue Date	Maturity Date	Carrying Value 31 Dec 2016 RM'000	Carrying Value 31 Dec 2015 RM'000
At amortised cost					
1st series at amortised cost	500,000	28 Sept 2012	28 Sept 2017	**500,000**	500,000
At fair value					
2nd series	500,000	16 Oct 2014	16 Oct 2019	**502,835**	500,641
3rd series	750,000	27 Mar 2015	27 Mar 2020	**753,166**	749,182
	1,250,000			**1,256,001**	1,249,823
	1,750,000			**1,756,001**	1,749,823

Movement in MCSP

	2nd series 31 Dec 2016 RM'000	2nd series 31 Dec 2015 RM'000	3rd series 31 Dec 2016 RM'000	3rd series 31 Dec 2015 RM'000
Balance at 1 January	**500,641**	501,854	**749,182**	-
New issuance during the financial year	**-**	-	**-**	750,000
Change in fair value other than from own credit risk	**4,282**	1,374	**7,565**	(7,020)
Change in fair value from own credit risk	**(2,088)**	(2,587)	**(3,581)**	6,202
Balance at 31 December	**502,835**	500,641	**753,166**	749,182

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
The cumulative change in fair value due to changes in own credit risk	**(5,669)**	3,615

22 Subordinated Commodity Murabahah Financing

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Subordinated Commodity Murabahah Financing, at amortised costs		
- First tranche issued on 25 June 2014	**348,508**	333,515
- Second tranche issued on 30 June 2015	**297,757**	284,946
	646,265	618,461

The unsecured Subordinated Commodity Murabahah financing comprise of two tranches of Basel III compliant Tier 2 subordinated financing of USD equivalent of RM250 million each from the Bank's immediate holding company, HSBC Bank Malaysia Berhad (HBMY). The tenor for both the Subordinated Commodity Murabahah financing is 10 years from the utilisation date with profit payable quarterly in arrears.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

23 Share Capital

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Authorised:		
600 million ordinary shares of RM0.50 each	**300,000**	300,000
Issued and fully paid:		
100 million ordinary shares of RM0.50 each		
Balance at 1 January/31 December	**50,000**	50,000

24 Reserves

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Non-distributable		
Share premium	**610,000**	610,000
Statutory reserve	**50,000**	50,000
Available-for-sale reserve	**(6,547)**	4,946
Capital Contribution reserve	**403**	1,058
Regulatory reserves	**34,000**	34,000
	687,856	700,004
Distributable		
Retained profits	**783,295**	701,902
	1,471,151	1,401,906

The statutory reserve is maintained in compliance with Section 12 of the Islamic Financial Services Act 2013 and is not distributable as cash dividends.

The capital contribution reserve is maintained to record the amount relating to share options granted to employees of the Bank directly by HSBC Holdings plc.

The regulatory reserve is maintained in compliance with paragraph 13 of BNM's policy document on classification and Impairment Provisions and impairment for financing and subsequent circular issued in February 2014, to maintain, in aggregate, collective impairment allowance and regulatory reserve of no less than 1.2% of gross financing and advances, net of individual impairment allowance. The regulatory reserve is debited against retained profit.

The Malaysian Finance Act 2007 introduced the single tier tax system with effect from 1 January 2008. Under this system, tax on a company's profits is a final tax and dividends are tax exempt in the hands of shareholders.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

25 Income Derived from Investment of Depositors' Funds and Others

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Income derived from investment of:		
(i) general investment deposits	**442,956**	484,448
(ii) specific investment deposits	**31,151**	47,313
(iii) others	**212,160**	186,725
	686,267	718,486

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
(i) Income derived from investment of general investment deposits		
Finance income:		
Financing and advances		
- Profit earned other than recoveries from impaired financing	**351,682**	368,451
- Recoveries from impaired financing	**10,407**	9,630
Financial investments available-for-sale	**31,211**	56,570
Money at call and deposit with financial institutions	**54,394**	64,178
	447,694	498,829
Other operating income		
Realised gains from dealing in foreign currency	**19,610**	14,664
Unrealised losses from dealing in foreign currency	**(3,569)**	(8,405)
Gains from sale of financial assets held-for-trading and other financial instruments	**873**	8,931
Unrealised gains from revaluation of financial assets held-for-trading	**304**	1,709
Net profit paid for financial assets held-for-trading and other financial instruments	**(24,125)**	(25,545)
Realised gains from trading in derivatives	**2,809**	4,543
Unrealised losses from trading in derivatives	**(382)**	(10,285)
Other (losses)/gains	**(258)**	7
	(4,738)	(14,381)
	442,956	484,448

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

25 Income Derived from Investment of Depositors' Funds and Others (Cont'd)

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
(ii) Income derived from investment of specific investment deposits		
Finance income:		
Financing and advances		
- Profit earned other than recoveries from impaired financing	**27,384**	36,437
	27,384	36,437
Other operating income		
Fees and commission	**1,013**	3,689
Realised gains from dealing in foreign currency	**2,787**	7,192
Unrealised losses from dealing in foreign currency	**(33)**	(5)
	3,767	10,876
	31,151	47,313
The above fees and commissions were derived from the following major contributors:		
Guarantee fees	**357**	1,440
Service charges and fees	**554**	2,245
(iii) Income derived from investment of others		
Finance income:		
Financing and advances		
- Profit earned other than recoveries from impaired financing	**168,443**	141,873
- Recoveries from impaired financing	**4,985**	3,729
Financial investments available-for-sale	**14,949**	21,173
Money at call and deposit with financial institutions	**26,053**	25,304
	214,430	192,079
Other operating income		
Realised gains from dealing in foreign currency	**9,392**	5,574
Unrealised losses from dealing in foreign currency	**(1,709)**	(2,649)
Gains from sale of financial assets held-for-trading and other financial instruments	**418**	3,495
Unrealised gains from revaluation of financial assets held-for-trading	**146**	601
Net profit paid from financial assets held-for-trading and other financial instruments	**(11,555)**	(9,862)
Realised gains from trading in derivatives	**1,345**	1,715
Unrealised losses from trading in derivatives	**(183)**	(4,234)
Other (losses)/gains	**(124)**	6
	(2,270)	(5,354)
	212,160	186,725

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

26 Income Derived from Investment of Shareholder's Funds

	31 Dec 2016 RM'000	31 Dec 2015 RM'000 (Restated)
Finance income:		
Financing and advances		
- Profit earned other than recoveries from impaired financing	**53,406**	46,025
- Recoveries from impaired financing	**1,580**	1,205
Financial investments available-for-sale	**4,740**	7,015
Money at call and deposit with financial institutions	**8,260**	8,067
	67,986	62,312
Other operating income		
Fees and commission	**55,290**	60,665
Realised gains from dealing in foreign currency	**2,978**	1,826
Unrealised losses from dealing in foreign currency	**(542)**	(1,001)
Gains from sale of financial assets held-for-trading and other financial instruments	**133**	1,120
Unrealised gains from revaluation of financial assets held-for-trading	**46**	209
Net profit paid from financial assets held-for-trading and other financial instruments	**(3,664)**	(3,193)
Realised gains from trading in derivatives	**427**	565
Unrealised losses from trading in derivatives	**(58)**	(1,308)
Shared-service fees from holding company	**3,023**	3,297
Net gains on disposal of financial assets available-for-sale	**6,853**	232
Net gains/(losses) on financial instruments designated at fair value through profit or losses	**4,187**	(1,839)
Other income	**70**	259
	68,743	60,832
	136,729	123,144

The above fees and commissions were derived from the following major contributors:

Service charges and fees	**19,470**	24,925
Cards	**24,178**	29,273
Agency fees	**7,242**	8,484

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

27 Impairment Losses on Financing

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Impairment charges on financing:		
(a) Individual impairment		
- Made during the financial year	**30,041**	45,829
- Written back	**(18,115)**	(27,717)
(b) Collective impairment		
- Made during the financial year	**211,487**	160,940
- Written back	**(58,264)**	(67,064)
Impaired financing		
- Recovered during the year	**(31,865)**	(32,229)
- Written off	**3,581**	2,728
	136,865	82,487

28 Income Attributable to Depositors

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Non-Mudharabah Fund		
- Deposits from customers	**203,120**	229,496
- Deposits and placements of banks and other financial institutions	**58,862**	60,693
- Others	**89,166**	77,104
Mudharabah Fund		
- Deposits and placements of banks and other financial institutions	**-**	8,216
	351,148	375,509

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

29 Operating Expenses

	31 Dec 2016 RM'000	31 Dec 2015 RM'000 (Restated)
Personnel expenses	**41,047**	47,134
Promotion and marketing related expenses	**10,200**	10,638
Establishment related expenses	**19,006**	20,893
General administrative expenses	**163,106**	151,808
	233,359	230,473
Personnel expenses		
Salaries, allowances and bonuses	**32,483**	37,711
Employees Provident Fund contributions	**5,655**	6,466
Other staff related costs	**2,909**	2,957
	41,047	47,134
Promotion and marketing related expenses	**10,200**	10,638
Establishment related expenses		
Depreciation of equipment	**5,029**	7,106
Amortisation of intangible assets	**-**	2
Information technology costs	**2,669**	2,911
Rental of premises	**7,922**	8,163
Utilities	**1,897**	1,880
Others	**1,489**	831
	19,006	20,893
General administrative expenses		
Group recharges	**132,606**	127,551
Auditors' remuneration		
- Statutory audit fees	**100**	100
- Audit related fees	**198**	158
- Other services	**8**	69
Professional fees	**1,748**	2,834
Communication	**1,230**	1,347
Others	**27,216**	19,749
	163,106	151,808

Included in professional fees are fees paid to the Shariah Committee members of the Bank:

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Fees	**404**	399
Assoc. Prof. Dr. Younes Soualhi	**91**	91
Khairul Anuar bin Ahmad	**78**	76
Assoc. Prof. Dr. Muhammad Yusuf Saleem Ghulam Nabi	**81**	77
Prof. Dr. Obiyathulla Ismath Bacha	**77**	78
Prof. Dr Abdul Rahim Abdul Rahman	**77**	77

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

30 Income Tax Expense

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Malaysian income tax		
- Current year	**21,850**	32,832
- Prior year	**(401)**	(331)
Total current tax recognised in profit or loss	**21,449**	32,501
Deferred tax:		
Origination and reversal of temporary differences		
- Current year	**(1,218)**	(1,402)
Total income tax expense	**20,231**	31,099

A numerical reconciliation between tax expense and the accounting profit multiplied by the applicable tax rate is as follows:

	RM'000	RM'000
Profit before tax	**101,624**	153,161
Income tax using Malaysian tax rates	**24,390**	38,290
Non-deductible expenses	**3,096**	1,549
Tax exempt income	**(6,854)**	(8,409)
Over provision in respect of prior years	**(401)**	(331)
Tax expense	**20,231**	31,099

The corporate tax rate will be reduced to 24% with effect Year of Assessment (YA) 2016 (25% for Year of Assessment 2015). Consequently, deferred tax assets and liabilities are measured using these tax rates.

31 Earnings per share

The earnings per ordinary share have been calculated based on profit for the year and 100,000,000 number of ordinary shares of RM0.50 each in issue during the financial year.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

32 Significant Related Party Transactions and Balances

For the purpose of these financial statements, parties are considered to be related to the Bank if:

a. the Bank has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial or operational decisions, or vice versa, or

b. where the Bank and the party are subject to common control or common significant influence. Related parties may be individuals or other entities.

The related parties of the Bank comprise:

i the Bank's immediate parent bank, holding bank, and ultimate holding company (hereinafter collectively referred to as parent);

ii subsidiary and associated companies of the Bank's parent companies; and

iii key management personnel who are defined as those person having authority for planning, directing and controlling the activities of the Bank. Key personnel include all members of the Board of Directors of HSBC Amanah Malaysia Berhad. and certain members of Senior Management of the Bank. Transactions, arrangements and agreement are entered into by the Bank with companies that may be controlled/jointly controlled by Key Management Personnel of the Bank and their close family members.

(a) The significant transactions and outstanding balances of the Bank with parent banks and other related companies are as follows:

	31 Dec 2016			31 Dec 2015		
	Parent **RM'000**	***Other related companies*** **RM'000**	***Key management personnel*** **RM'000**	*Parent* RM'000	*Other related companies* RM'000	*Key management personnel* RM'000
Income						
Finance income from financing and advances	**-**	**-**	**2**	-	-	183
Fees and commission	**-**	**5,621**	**-**	1	11,620	-
Other income	**3,023**	**5**	**-**	3,297	5	-
	3,023	**5,626**	**2**	3,298	11,625	183
Expenditure						
Profit attributable to deposits and placements from banks and other financial institutions	**73,542**	**3,025**	**-**	68,494	10,952	-
Profit attributable to deposits from customers	**-**	**-**	**4**	-	-	2
Fees and commission	**30**	**285**	**-**	30	200	-
Operating expenses	**128,375**	**4,231**	**-**	123,267	4,284	-
	201,947	**7,541**	**4**	191,791	15,436	2
Amount due from						
Deposits and placements with banks and other financial institutions	**-**	**79,553**	**-**	-	280,205	-
Financing and advances	**-**	**-**	**2,889**	-	-	7,326
Derivative financial assets	**18,806**	**4**	**-**	16,773	1,353	-
Other assets	**45,132**	**-**	**-**	209,358	1,042	-
	63,938	**79,557**	**2,889**	226,131	282,600	7,326
Amount due to						
Deposits and placements from banks and other financial institutions	**2,569,451**	**59,091**	**-**	3,451,768	1,358,893	-
Deposits from customers	**-**	**-**	**1,023**	-		912
Derivative financial liabilities	**477,434**	**2**	**-**	461,565	1	-
Other liabilities	**40,377**	**1,374**	**-**	10,785	2,324	-
	3,087,262	**60,467**	**1,023**	3,924,118	1,361,218	912

All transactions between the Bank and its related parties are made in the ordinary course of business.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

32 Significant Related Party Transactions and Balances (Cont'd)

(b) Key Management Personnel Compensation

The key management personnel compensation are as follows:

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Directors of the Bank:		
- Fees	**470**	515
- Remuneration	**-**	1,783
- Other short term employee benefits (including estimated monetary value of benefits-in-kind)	**-**	731
Total short-term employee benefits	**470**	3,029
- Share-based payments	**-**	822
	470	3,851
Other key management personnel:		
- Short-term employee benefits	**935**	-
Total key management personnel compensation	**1,405**	3,851

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

32 Significant Related Party Transactions and Balances (Cont'd)

(b) Key Management Personnel Compensation (Cont'd)

2016

RM'000	Salaries and bonuses	Other short-term employee benefits	Benefits-in-kind	Fees	Total
Non-Independent Executive Director					
Louisa Cheang Wai Wan	-	-	-	-	-
Mukhtar Malik Hussain	-	-	-	-	-
Independent Non-Executive Directors					
Dr.Mohamed Ashraf bin Mohamed Iqbal	-	-	-	**106**	**106**
Adil Ahmad	-	-	-	**98**	**98**
Albert Quah Chei Jin [1]	-	-	-	**38**	**38**
Azlan bin Abdullah	-	-	-	**101**	**101**
Lee Choo Hock [2]	-	-	-	**69**	**69**
Mohamed Ross bin Mohd Din [4]	-	-	-	**34**	**34**
Seow Yoo Lin [3]	-	-	-	**24**	**24**
	-	-	-	**470**	**470**
CEO					
Arsalaan Ahmed [5]	**205**	**106**	**4**	-	**315**

[1] Appointed on 5 September 2016

[2] Appointed on 30 May 2016

[3] Resigned on 14 March 2016

[4] Retired on 13 April 2016

[5] Appointed on 17 October 2016

2015

RM'000	Salaries and bonuses	Other short-term employee benefits	Benefits-in-kind	Fees	Total
Executive Director					
Mohamed Rafe bin Mohamed Haneef (CEO) [1]	1,783	579	152	-	2,514
Non Executive Directors					
Louisa Cheang Wai Wan	-	-	-	-	-
Mukhtar Malik Hussain	-	-	-	-	-
Adil Ahmad	-	-	-	88	88
Azlan bin Abdullah	-	-	-	99	99
Mohamed Ashraf bin Mohamed Iqbal	-	-	-	102	102
Mohamed Ross bin Mohd Din	-	-	-	113	113
Seow Yoo Lin	-	-	-	113	113
	1,783	579	152	515	3,029

[1] Resigned on 31 December 2015

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

32 Significant Related Party Transactions and Balances (Cont'd)

(b) Key management personnel compensation (Cont'd)

Total value of remuneration awards for the financial year

	31 Dec 2016		31 Dec 2015	
	Unrestricted RM'000	**Deferred RM'000**	Unrestricted RM'000	Deferred RM'000
Fixed remuneration				
Cash	**491**	**-**	1,370	-
Variable remuneration				
Cash	**160**	**-**	116	-
	651	**-**	1,486	-

Number of officers having received a variable remuneration during the financial year: 2 (2015: 1)

	31 Dec 2016		31 Dec 2015	
	Number	**Amount RM'000**	Number	Amount RM'000
Outstanding deferred remuneration				
Cash	**-**	**-**	1	276
Shares and share-linked instruments	-	-	1	708
		-		984
Deferred remuneration paid out	-	-	1	465

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

33 Credit exposure to connected parties

The credit exposures of the Bank to connected parties, as defined by Bank Negara Malaysia's Guidelines on Credit Transactions and Exposures with Connected Parties' are as follows:

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Aggregate value of outstanding credit exposures to connected parties	**836,894**	547,758
As a percentage of total credit exposures	**5.18%**	3.41%
Aggregate value of outstanding credit exposures to connected parties which is non-performing or in default	**-**	-
As a percentage of total credit exposures	**-**	-

34 Capital Adequacy

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Tier 1 capital		
Paid-up ordinary share capital	**50,000**	50,000
Share premium	**610,000**	610,000
Retained profits	**783,296**	701,902
Other reserves	**75,789**	91,565
Regulatory adjustments	**(46,978)**	(37,639)
Total Common Equity Tier 1 (CET1) and Tier 1 capital	**1,472,107**	1,415,828
Tier 2 capital		
Subordinated Commodity Murabahah financing	**646,265**	618,461
Collective impairment allowance (unimpaired portion) & regulatory reserves	**135,261**	118,212
Total Tier 2 capital	**781,526**	736,673
Capital base	**2,253,633**	2,152,501
CET1 and Tier 1 Capital ratio	**12.553%**	11.911%
Total Capital ratio	**19.218%**	18.108%

The total capital and capital adequacy ratios have been computed based on the Standardised Approach in accordance with the Capital Adequacy Framework for Islamic Banks (CAFIB). The Bank has adopted the Standardised Approach for Credit Risk and Market Risk, and the Basic Indicator Approach for Operational Risk.

Breakdown of risk-weighted assets (RWA) in the various categories of risk weights:

	31 Dec 2016		31 Dec 2015	
	Principal RM'000	**Risk-weighted RM'000**	Principal RM'000	Risk-weighted RM'000
Total RWA for credit risk	**19,594,222**	**10,820,917**	22,406,281	10,885,513
Total RWA for market risk	**-**	**11,396**	-	104,374
Total RWA for operational risk	**-**	**894,490**	-	897,064
	19,594,222	**11,726,803**	22,406,281	11,886,951

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

35 Commitments and Contingencies

The table below shows the contracts or underlying principal amounts, positive fair value of derivative contracts, credit equivalent amounts and risk weighted amounts of unmatured off-balance sheet transactions at the statement of financial position date. The underlying principal amounts indicate the volume of business outstanding and do not represent amounts at risk.

These commitments and contingencies are not secured over the assets of the Bank.

Principal amount	**31 Dec 2016 RM'000**	31 Dec 2015 RM'000
Direct credit substitutes	**535,818**	622,855
Transaction-related contingent items	**1,113,122**	1,089,395
Short-term self-liquidating trade-related contingencies	**111,027**	172,151
Irrevocable commitments to extend credit		
- Maturity not exceeding one year	**3,685,008**	3,056,937
- Maturity exceeding one year	**2,041,247**	1,818,014
Unutilised credit card lines	**2,251,942**	1,678,518
Equity related contracts		
- Less than one year	**765,236**	192,724
- One year to less than five years	**109,766**	948,669
Profit rate related contracts		
- Less than one year	**1,290,000**	1,201,265
- One year to less than five years	**5,149,618**	6,645,808
Foreign exchange related contracts		
- Less than one year	**2,592,079**	2,437,315
- One year to less than five years	**2,504,990**	2,026,017
	22,149,853	21,889,668

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

36 Profit Rate Risk

The Bank is exposed to various risks associated with the effects of fluctuations in the prevailing levels of market profit rates on its financial position and cash flows. The following table summarises the Bank's exposure to the profit rates risk. The assets and liabilities at carrying amount are allocated to time bands by reference to the earlier of the next contractual repricing dates and maturity dates.

	Non-trading book								Effective
31 Dec 2016	**Up to 1 month RM'000**	**>1 - 3 months RM'000**	**>3 - 12 months RM'000**	**1 - 5 years RM'000**	**Over 5 years RM'000**	**Non-profit sensitive RM'000**	**Trading book RM'000**	**Total RM'000**	**profit rate %**
ASSETS									
Cash and short-term funds	2,251,658	-	-	-	-	107,933	-	2,359,591	3.16
Financial assets held-for-trading	-	-	-	-	-	-	488	488	5.95
Financial investments available-for-sale	-	-	180,224	1,168,295	20,055	-	-	1,368,574	3.51
Financing and advances									
- performing	2,824,706	7,697,033	145,381	813,867	221,522	-	-	11,702,509	5.30
- impaired [1]	-	-	-	-	-	240,769	-	240,769	-
- collective allowance	-	-	-	-	-	(200,015)	-	(200,015)	-
Derivative financial assets	-	-	-	-	-	-	395,748	395,748	-
Other assets	-	-	-	-	-	80,041	-	80,041	-
Total Financial Assets	5,076,364	7,697,033	325,605	1,982,162	241,577	228,728	396,236	15,947,705	
Deposits from customers	5,107,103	1,767,337	1,225,760	32,571	-	593,772	-	8,726,543	2.43
Deposits and placements from banks and other financial institutions	559,368	86,830	1,248,600	32,391	-	24,413	-	1,951,602	2.69
Bills and acceptances payable	-	-	-	-	-	23,632	-	23,632	-
Multi-Currency Sukuk Programme	-	-	500,000	1,256,001	-	-	-	1,756,001	3.95
Subordinated Commodity Murabahah Financing	-	-	-	-	646,265	-	-	646,265	2.80
Derivative financial liabilities	-	59	-	962	-	-	489,734	490,755	-
Other liabilities	-	-	-	-	-	189,493	969,409	1,158,902	3.07
Total Financial Liabilities	5,666,471	1,854,226	2,974,360	1,321,925	646,265	831,310	1,459,143	14,753,700	
Total profit sensitivity gap	(590,107)	5,842,807	(2,648,755)	660,237	(404,688)	(602,582)	(1,062,907)	1,194,005	

[1] This is arrived at after deducting individual impairment allowance from impaired financing.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

36 Profit rate risk (Cont'd)

31 Dec 2015	Non-trading book: Up to 1 month RM'000	>1 - 3 months RM'000	>3 - 12 months RM'000	1 - 5 years RM'000	Over 5 years RM'000	Non-profit sensitive RM'000	Trading book RM'000	Total RM'000	Effective profit rate %
ASSETS									
Cash and short-term funds	4,662,526	-	-	-	-	87,864	-	4,750,390	3.29
Financial assets held-for-trading	-	-	-	-	-	-	10,492	10,492	3.29
Financial investments available-for-sale	-	-	171,710	1,529,533	-	-	-	1,701,243	3.54
Financing and advances									
- performing	2,942,903	7,598,180	430,346	936,844	33,576	-	-	11,941,849	5.26
- impaired [1]	-	-	-	-	-	166,632	-	166,632	-
- collective allowance	-	-	-	-	-	(140,264)	-	(140,264)	-
Derivative financial assets	-	-	-	399	-	-	306,900	307,299	-
Other assets	-	-	-	-	-	241,611	-	241,611	-
Total Financial Assets	7,605,429	7,598,180	602,056	2,466,776	33,576	355,843	317,392	18,979,252	
LIABILITIES AND EQUITY									
Deposits from customers	5,182,972	1,977,410	1,405,652	44,111	-	775,978	-	9,386,123	2.60
Deposits and placements from banks and other financial institutions	820,779	735,392	1,679,300	879,219	-	45,399	-	4,160,089	2.20
Bills and acceptances payable	-	-	-	-	-	14,904	-	14,904	-
Multi-Currency Sukuk Programme	-	-	-	1,749,823	-	-	-	1,749,823	4.00
Derivative financial liabilities	-	-	-	201	-	-	473,030	473,231	-
Subordinated Commodity Murabahah Financing	-	-	-	-	618,461	-	-	618,461	2.45
Other Liabilities	-	-	-	-	-	176,555	1,268,657	1,445,212	2.90
Total Financial Liabilities	6,003,751	2,712,802	3,084,952	2,673,354	618,461	1,012,836	1,741,687	17,847,843	
Total profit sensitivity gap	1,601,678	4,885,378	(2,482,896)	(206,578)	(584,885)	(656,993)	(1,424,295)	1,131,409	

[1] This is arrived at after deducting individual impairment allowance from impaired financing.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

37 Liquidity risk

The following tables summarise the Bank's exposure to liquidity risk. The asset and liabilities at carrying amount are allocated to time bands by reference to the remaining contractual maturity and/or their behavioural profile.

31 Dec 2016	Non-trading book: Up to 1 month RM'000	>1 - 3 months RM'000	>3 - 12 months RM'000	1 - 5 years RM'000	Over 5 years RM'000	Non-specific maturity RM'000	Trading book RM'000	Total RM'000
ASSETS								
Cash and short-term funds	2,359,591	-	-	-	-	-	-	2,359,591
Financial assets held-for-trading	-	-	-	-	-	-	488	488
Financial investments available-for-sale	-	-	180,224	1,168,295	20,055	-	-	1,368,574
Financing and advances	2,160,491	1,740,491	415,573	1,706,522	5,720,186	-	-	11,743,263
Derivative financial assets	-	-	-	-	-	-	395,748	395,748
Others	47,582	-	1,298	8,828	395	375,317	-	433,420
Total Assets	4,567,664	1,740,491	597,095	2,883,645	5,740,636	375,317	396,236	16,301,084
LIABILITIES AND EQUITY								
Deposits from customers	5,700,875	1,767,337	1,225,760	32,571	-	-	-	8,726,543
Deposits and placements from banks and other financial institutions	583,781	86,830	1,248,600	32,391	-	-	-	1,951,602
Bills and acceptances payable	23,632	-	-	-	-	-	-	23,632
Multi-Currency Sukuk Programme	-	-	500,000	1,256,001	-	-	-	1,756,001
Subordinated Commodity Murabahah Financing	-	-	-	-	646,265	-	-	646,265
Derivative financial liabilities	-	59	-	962	-	-	489,734	490,755
Others	52,421	12,285	23,242	14,161	204	113,413	969,409	1,185,135
Total Liabilities	6,360,709	1,866,511	2,997,602	1,336,086	646,469	113,413	1,459,143	14,779,933
Equity	-	-	-	-	-	1,521,151	-	1,521,151
Total Liabilities and Equity	6,360,709	1,866,511	2,997,602	1,336,086	646,469	1,634,564	1,459,143	16,301,084
Net maturity mismatches	(1,793,045)	(126,020)	(2,400,507)	1,547,559	5,094,167	(1,259,247)	(1,062,907)	-
Off balance sheet liabilities	7,787,944	2,793,902	3,404,638	8,153,424	9,945	-	-	22,149,853

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

37 Liquidity risk (Cont'd)

31 Dec 2015	Non-trading book							
	Up to 1 month RM'000	>1 - 3 months RM'000	>3 - 12 months RM'000	1 - 5 years	Over 5 years RM'000	Non-specific maturity RM'000	Trading book RM'000	Total RM'000
ASSETS								
Cash and short-term funds	4,750,390	-	-	-	-	-	-	4,750,390
Financial assets held-for-trading	-	-	-	-	-	-	10,492	10,492
Financial investments available-for-sale	-	-	171,710	1,529,533	-	-	-	1,701,243
Financing and advances	1,888,585	1,639,415	954,754	2,103,147	5,382,316	-	-	11,968,217
Derivative financial assets	-	-	-	399	-	-	306,900	307,299
Others	210,500	-	834	10,053	8	370,876	-	592,271
Total Assets	6,849,475	1,639,415	1,127,298	3,643,132	5,382,324	370,876	317,392	19,329,912
LIABILITIES AND EQUITY								
Deposits from customers	5,958,950	1,977,410	1,405,652	44,111	-	-	-	9,386,123
Deposits and placements from banks and other financial institutions	866,178	735,392	1,679,300	879,219	-	-	-	4,160,089
Bills and acceptances payable	14,904	-	-	-	-		-	14,904
Multi-Currency Sukuk Programme	-	-	-	1,749,823		-	-	1,749,823
Subordinated Commodity Murabahah Financing	-	-	-	-	618,461	-	-	618,461
Derivative financial liabilities	-	-	-	201	-	-	473,030	473,231
Others	21,454	13,047	20,332	24,577	145	127,163	1,268,657	1,475,375
Total Liabilities	6,861,486	2,725,849	3,105,284	2,697,931	618,606	127,163	1,741,687	17,878,006
Equity	-	-	-	-	-	1,451,906	-	1,451,906
Total Liabilities and Equity	6,861,486	2,725,849	3,105,284	2,697,931	618,606	1,579,069	1,741,687	19,329,912
Net maturity mismatches	(12,011)	(1,086,434)	(1,977,986)	945,201	4,763,718	(1,208,193)	(1,424,295)	-
Off balance sheet liabilities	8,097,118	857,436	2,907,306	10,025,117	2,691	-	-	21,889,668

37 Liquidity risk (Cont'd)

The balances in the tables below will not agree directly with the balances in the statement of financial position as the table incorporates, on an undiscounted basis, all cash flows relating to principal and future coupon payments. In addition, financing and other credit-related commitments and financial guarantees and similar contracts are generally not recognised on the statement of financial position.

Cash flows payable in respect of customer accounts are primarily contractually repayable on demand or at short notice. However, in practice, short term deposit balances remain stable as inflows and outflows broadly match and a significant portion of financing commitments expire without being drawn upon.

i) Cash flows payable by the Bank under financial liabilities by remaining contractual maturities

RM'000	**On Demand**	**Due within 3 months**	**Due between 3 months to 12 months**	**Due between 1 and 5 years**	**Due after 5 years**	**Total**
At 31 Dec 2016						
Non-derivative liabilities						
Deposits by customers	**3,589,284**	**3,927,926**	**1,237,287**	**28,469**	**-**	**8,782,966**
Deposits and placements from banks and other financial institutions	**-**	**675,121**	**1,273,791**	**35,876**	**-**	**1,984,788**
Bills and acceptances payable	**23,632**	**-**	**-**	**-**	**-**	**23,632**
Multi-Currency Sukuk Programme	**-**	**19,761**	**531,679**	**1,344,921**	**-**	**1,896,361**
Subordinated Commodity Murabahah financing	**-**	**4,881**	**12,817**	**81,342**	**704,204**	**803,244**
Other liabilities	**69,866**	**71,048**	**960,284**	**1,221,006**	**83,553**	**2,405,757**
Financing and other credit-related commitments	**7,097,593**	**323,559**	**553,909**	**3,136**	**-**	**7,978,197**
Financial guarantees and similar contracts	**111,366**	**724,837**	**527,905**	**385,914**	**9,945**	**1,759,967**
	10,891,741	**5,747,133**	**5,097,672**	**3,100,664**	**797,702**	**25,634,912**
Derivative liabilities						
Gross settled derivatives						
- Inflow	**-**	**(490,907)**	**(708,050)**	**(1,008,001)**	**-**	**(2,206,958)**
- Outflow	**-**	**538,080**	**879,628**	**1,261,361**	**-**	**2,679,069**
Net settled derivatives	**-**	**(11,925)**	**6,554**	**14,719**	**-**	**9,348**

RM'000	On Demand	Due within 3 months	Due between 3 months to 12 months	Due between 1 and 5 years	Due after 5 years	Total
At 31 Dec 2015						
Non-derivative liabilities						
Deposits by customers	3,587,064	4,382,985	1,439,915	49,845	-	9,459,809
Deposits and placements from banks and other financial institutions	-	1,610,379	1,707,008	956,590	-	4,273,977
Bills and acceptances payable	14,904	-	-	-	-	14,904
Multi-Currency Sukuk Programme	-	19,870	41,247	1,896,361	-	1,957,478
Subordinated Commodity Murabahah financing	-	4,037	12,487	64,350	684,908	765,782
Other liabilities	38,455	200,816	83,116	1,990,488	96,858	2,409,733
Financing and other credit-related commitments	5,953,651	133,109	462,519	4,189	-	6,553,468
Financial guarantees and similar contracts	715,109	55,316	710,850	400,436	2,691	1,884,402
	10,309,183	6,406,512	4,457,142	5,362,259	784,457	27,319,553
Derivative liabilities						
Gross settled derivatives						
- Inflow	-	(443,397)	(289,954)	(846,981)	-	(1,580,332)
- Outflow	-	528,394	327,823	1,140,086	-	1,996,303
Net settled derivatives	-	1,122	(317)	18,628	-	19,433

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

38 Collateral

In the normal course of business, the Bank sells assets to raise liabilities and accepts assets for resale. Assets sold and received are mainly via repurchase agreements and reverse repurchase agreements. Collateral is accepted and pledged on derivative contracts, mainly in the form of cash.

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Carrying amount of assets pledged as collateral		
- Collateral pledged for repurchase agreements	**59,783**	140,412

39 Fair values of financial assets and liabilities not measured at fair value

The fair value of each financial asset and liabilities presented in the statement of financial position of the Bank approximates the carrying amount as at the reporting date except for the following:

	31 Dec 2016 Carrying amount RM'000	**31 Dec 2016 Fair Value RM'000**	31 Dec 2015 Carrying amount RM'000	31 Dec 2015 Fair Value RM'000
Financial Assets				
Financing and advances	**11,743,263**	**11,749,726**	11,968,217	11,982,719
Financial Liabilities				
Deposits from customers	**8,726,543**	**8,723,002**	9,386,123	9,386,266
Deposits and placements from banks and other financial institutions	**1,951,602**	**1,951,545**	4,160,089	4,159,370
Multi-Currency Sukuk Programme	**1,756,001**	**1,754,751**	1,749,823	1,747,423
Subordinated Commodity Murabahah Financing	**646,265**	**745,014**	618,461	610,090

The methods and assumptions used in estimating the fair values of financial instruments other than those already mentioned in Note 3(e) are as follows:

Cash and short-term funds
Deposits and placements with banks and other financial institutions
Bills and acceptances payable

The carrying amounts approximate fair values due to their relatively short-term nature.

Financing and advances
For personal and commercial financing which mature or reprice after six months, fair value is principally estimated by discounting anticipated cash flows (including profit at contractual rates). Performing financing are grouped to the extent possible, into homogenous pools segregated by maturity within each pool. In general, cash flows are discounted using current market rates for instruments with similar maturity, repricing and credit risk characteristics. For impaired financing, the fair value is the carrying value of the financing, net of individual impairment allowances. Collective impairment allowances are deducted from the fair value of financing.

Deposits from customers
Deposits and placements from banks and other financial institutions
Deposits, placements and obligations which mature or reprice after six months are grouped by residual maturity. Fair value is estimated using discounted cash flows, applying either market rates, where applicable, or current rates offered for deposits of similar remaining maturities. The fair value of a deposit repayable on demand is approximated by its carrying value.

Multi-Currency Sukuk Programme
Subordinated Commodity Murabahah Financing
The fair value of subordinated bonds issued at cost were estimated based on discounted cash flows using rates currently offered for debt instruments of similar remaining maturities and credit grading.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

39 Fair Values of Financial Assets and Liabilities not measured at fair value (Cont'd)

The fair value of each financial asset and liabilities presented in the statement of financial position of the Bank approximates the carrying amount as at the reporting date except for the following (Cont'd):

31 Dec 2016	Level 1 RM'000	Level 2 RM'000	Level 3 RM'000	Total fair value RM'000	Total carrying amount RM'000
Financial Assets					
Financing and advances	-	-	**11,749,726**	**11,749,726**	**11,743,263**
Financial Liabilities					
Deposits from customers	-	**8,723,002**	-	**8,723,002**	**8,726,543**
Deposits and placements from banks and other financial institutions	-	**1,951,545**	-	**1,951,545**	**1,951,602**
Multi-Currency Sukuk Programme	-	**1,754,751**	-	**1,754,751**	**1,756,001**
Subordinated Commodity Murabahah Financing	-	**745,014**	-	**745,014**	**646,265**
31 Dec 2015					
Financial Assets					
Financing and advances	-	-	11,982,719	11,982,719	11,968,217
Financial Liabilities					
Deposits from customers	-	9,386,266	-	9,386,266	9,386,123
Deposits and placements from banks and other financial institutions	-	4,159,370	-	4,159,370	4,160,089
Multi-Currency Sukuk Programme	-	1,747,423	-	1,747,423	1,749,823
Subordinated Commodity Murabahah Financing	-	610,090	-	610,090	618,461

40 Lease commitments

The Bank has lease commitments in respect of rented premises and hired equipment, all of which are classified as operating leases. A summary of the non-cancellable long term commitments net of sub-leases (if any) are as follows:

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Less than one year	**6,951**	6,855
Between one and three years	**2,736**	5,585
Between three and five years	**2**	17
	9,689	12,457

41 Capital commitments

	31 Dec 2016 RM'000	31 Dec 2015 RM'000
Capital expenditure commitments:		
- Authorised and contracted, but not provided for	-	-
- Authorised but not contracted for	-	650
	-	650

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

42 Equity-based compensation

The Bank participated in the following cash settled share compensation plans operated by the HSBC Group for the acquisition of HSBC Holdings plc shares.

a) Savings-Related Share Option Schemes
The Savings-Related Share Option Schemes aims to align the interests of all employees with the creation of shareholder value. under which eligible HSBC employees are granted options to acquire HSBC Holdings ordinary shares. Employees may make monthly contributions up to £250 (or its equivalent in RM) over a period of one, three or five years with the option to use the savings to acquire shares. Alternatively the employee may elect to have the savings repaid in cash. The last grant of options under this plan was in 2012. The options are exercisable within three months following the first anniversary of the commencement of a one-year savings contract or within six months following either the third or the fifth anniversary of the commencement of three-year or five-year savings contracts, respectively. The exercise price is set at a 20% discount to the market value immediately preceding the date of invitation. The cost of the awards is amortised over the vesting period.

Movements in the number of share options held by employees are as follows:

	31 Dec 2016 Number ('000)	**Weighted average exercise price £**	31 Dec 2015 Number ('000)	Weighted average exercise price £
Balance at 1 January	**-**	**-**	7	4.27
Exercised in the financial year	**-**	**-**	(5)	4.37
Lapsed in the financial year	**-**	**-**	(2)	3.91
Balance at 31 December	**-**		-	-
Options vested at 31 December	**-**		5	
Compensation cost recognised during the financial year	**(13)**		(3)	

The weighted average remaining contractual life for the share options is nil (2015: 0.09 years), as no options outstanding at the end of the financial year ended 31 December 2016.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

42 Equity-based compensation (Cont'd)

b) Restricted Share Plan and Share Match Schemes

The HSBC Holdings Restricted Share Plan is intended to align the interests of executives with those of shareholders by linking executive awards to the creation of superior shareholder value. This is achieved by focusing on predetermined targets. An assessment of performance over the relevant period ending on 31 December is used to determine the amount of the award to be granted. Deferred awards generally require employees to remain in employment over the vesting period and are not subject to performance conditions after the grant date. Deferred share awards generally vest over a period of three years. Vested shares may be subject to a retention requirement (restriction) post-vesting. The cost of the conditional awards is recognised through an annual charge based on the likely level of vesting of shares, apportioned over the period of service to which the award relates.

The Share Match Schemes was first introduced in Malaysia in 2014. Eligible HSBC employees will acquire HSBC Holdings ordinary shares. Shares are purchased in the market each quarter up to a maximum value of £750 or the equivalent in local currency over a period of one year. Matching awards are added at a ratio of one free share for every three purchased. Matching awards vest subject to continued employment and the retention of the purchased shares for a maximum period of two years and nine months.

	31 Dec 2016 Number ('000)	31 Dec 2015 Number ('000)
Balance at 1 January	**24**	26
Additions during the financial year	**3**	26
Lapsed in the year	**(21)**	(28)
Balance at 31 December	**6**	24
Compensation cost recognised during the financial year	**(576)**	368

The weighted average purchase price for all shares purchased by HSBC for awards under the Restricted Share Plan and the Share Match Schemes is £4.89 (2015: £5.51). The weighted average fair value of the HSBC share at 31 December 2016 was £5.50 (2015: £5.76). The weighted average remaining vesting period as at 31 December 2016 for shares granted during the year was 1.82 years (2015: 4.03 years).

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

43 Shariah Advisors

In line with Bank Negara Malaysia's Guideline on Shariah Governance Framework for Islamic Financial Institution, the following Shariah Scholars were appointed:

1) Assoc. Prof. Dr. Younes Soualhi
Assoc. Prof. Dr. Younes Soualhi is currently a Senior Researcher in International Shariah Research Academy. He holds a Bachelor, Master and Phd in Usul al-Fiqh from the Emir Abdul Qadir University for Islamic Sciences, Algeria, IIUM and University Malaya respectively. He also holds a diploma in Human Sciences from IIUM.

2) Assoc. Prof. Dr. Muhammad Yusuf Saleem Ghulam Nabi
Assoc. Prof. Dr. Muhammad Yusuf Saleem Ghulam Nabi is currently Associate Professor in International Centre for Education of Islamic Finance (INCEIF). He holds a Bachelor of Law (LLB), Master of Comparative Law and Doctor of Philosophy (Law) from IIUM.

3) Dr. Ziyaad Mahomed
Dr. Ziyaad Mahomed is currently a Shariah Advisor in Zinergy Consultants T/A IFISA, South Africa. He holds a PhD in Islamic Finance from INCEIF, BA (Hons) Business (Finance) from Anglia Ruskin University, United Kingdom, and a Chartered Islamic Finance Professional (CIFP) holder from INCEIF. He is also an MBA and Certificate in Islamic Law holder from MANCOSA and University of Kwazulu Natal, South Africa, respectively.

4) Khairul Anuar bin Ahmad
Khairul Anuar bin Ahmad is currently Lecturer in Selangor International Islamic University College. He holds a Bachelor and Master of Shariah from University of Malaya.

5) Prof. Dr Abdul Rahim Abdul Rahman
Prof. Dr. Abdul Rahim Abdul Rahman is currently Professor at the Faculty of Economics and Muamalat, Islamic Science University of Malaysia (USIM). He holds a Bachelor in Finance and Accounting from University of East London, and Master of Accounting and Management Sciences and Phd in Accounting for Islamic Institution from University of Southampton, United Kingdom.

6) Prof. Dr. Obiyathulla Ismath Bacha
Prof. Dr. Obiyathulla Ismath Bacha is currently Professor of Finance in INCEIF. He holds a Bachelor of Social Science from Science University of Malaysia (USM), Master of Arts (Economics), Master of Business Administration and Doctor of Business Administration with specialisation in Finance from Boston University.

NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

44 Comparative Figures

Restatement of Comparative Figures

The presentation and classification of items in the financial statements are consistent with the previous financial year except those listed below. Comparatives for net fee commission income, other operating expenses and income from Islamic banking operations were restated to conform to the current financial year's presentation. There was no significant impact to the financial performance and ratios in relation to the financial year 31 December 2016. The Bank's prior year profit and loss and retained profits brought forward are not affected by these reclassifications.

Statement of Profit or Loss and Other Comprehensive Income	31 Dec 2015	
	RM'000	RM'000
	As restated	As previously stated
a) Operating Expenses	**230,473**	243,319
(of which the affected components are disclosed below) :		
Promotion and marketing related expenses	**10,638**	23,484
b) Income Derived from Investment of Shareholder's Funds	**123,144**	135,990
(of which the affected components are disclosed below) :		
Fees and commission	**60,665**	73,511