

ZA BANK LIMITED

REPORT OF DIRECTORS AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2023

ZA BANK LIMITED

**FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2023**

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ZA BANK LIMITED

REPORT OF DIRECTORS

The directors submit their report together with the audited financial statements of ZA Bank Limited (the “Bank”) for the year ended 31 December 2023.

Principal activities

The Bank is a licensed bank authorized under the Banking Ordinance in Hong Kong. The principal activities of the Bank are to provide banking services.

Improved profitability and financial excellence

With a commitment to building a fully-fledged digital bank to serve customers’ holistic financial needs, the strategic focus on quality growth and operational efficiency has led the Bank to stay on course to achieve better profitability.

The significant progress in innovating products and deepening customer engagement have translated into another year of robust financial performance. A rise in net interest margin (NIM) and total assets have boosted the Bank’s net interest income up by 36% year-over-year, alongside a solid growth in net fee and commission income.

Customer deposits grew 28% year-over-year, primarily driven by increased engagement with new products and features in addition to our debit card proposition, against a backdrop of interest rate hikes. The Bank’s loan book also expanded by 9% during the year.

Thanks to a prudent, data-driven approach to portfolio management, the Bank once again reported a narrowed net loss of HK\$399 million, down notably by 20% from a year earlier.

Banking for Web3

The Bank announced the “Banking for Web3” agenda in April 2023, and has since provided essential business banking services for over 80 Web3 companies. The Bank is also serving as a settlement bank for licensed virtual asset trading platforms (VATPs) in Hong Kong to facilitate fiat-currency deposits and withdrawals.

With the new licensing regime for VATPs coming into force in June 2023, the Bank is in active preparation for partnering with Hong Kong-licensed VATPs to empower retail investors to trade virtual assets by using fiat currencies in the ZA Bank App.

Maximising wealth with minimised costs

The Bank has further strengthened its wealth management proposition in 2023. With over 100 products managed by top international fund managers, including Allianz Global Investors, Invesco and J.P. Morgan Asset Management, the Bank’s investment fund services achieved an 8-fold growth in total assets under management over the course of the year.

In November 2023, the Hong Kong Securities and Futures Commission lifted the previous conditions on the Bank’s licence registration of Type 1 (dealing in securities) regulated activity under which the Bank shall only carry on business of dealing in collective investment schemes. The Bank has successfully launched U.S. stock trading services in February 2024.

Leveraging the power of technology and a cost-effective infrastructure, the Bank has successfully saved users over HKD 100 million in investment fund subscription fees, and millions of HKD in remittance fees for its Global Transfer function powered by Wise.

Supporting SME community with technology

The Bank officially launched the express online business account opening service in April. Our digitalised business banking offerings seek to address a major pain point for local SMEs and serve their financial needs in a challenging environment.

ZA BANK LIMITED

REPORT OF DIRECTORS (Continued)

Principal activities (Continued)

From local trust to global recognition

Our continuous efforts to build a future bank are highly recognised by the market. The Bank was named Virtual Bank of the Year for retail customers in Hong Kong for two consecutive years in The Asset Triple A Digital Awards 2023 and 2024. The ZA Bank App topped the Sia Partners' 2023 International Mobile Banking Benchmark in Asia and ranked 6th globally. As of December 2023, the App was also the top-rated retail banking app on Google Play in Hong Kong. These accolades serve as a testament to the Bank's unwavering dedication to shaping the future of banking and delivering unparalleled user experiences.

Results and appropriations

The results of the Bank for the year are set out in the statement of comprehensive income on page 8.

The directors do not recommend the payment of any dividend.

Share capital

The shares issued are used to strengthen the capital adequacy of the bank. Details of the shares issued in the year ended 31 December 2023 are set out in note 21 to the financial statements.

The directors, including executive director ("ED"), non-executive directors ("NED") and independent non-executive directors ("INED") of the Bank during the year and up to the date of this report were:

OU Yaping (NED) - Chairman
IU Man Chung (ED) – Chief Executive (appointed on 1 February 2023)
NG Chung Ho (ED)
OU Jin Yi Hugo (NED)
XIAO Feng (NED)
XU Wei (NED) (appointed on 6 November 2023)
ZHANG Shengman (INED)
HUANG Ming Xiang (INED)
LO Kin Ching, Joseph (INED)
ZHU Qi (INED)
HSU Rockson (ED) – Chief Executive (resigned on 1 February 2023)

HSU Rockson has stepped down as Chief Executive and Executive Director of the Bank to pursue new opportunities.

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

Directors' material interests in transactions, arrangements and contracts that are significant in relation to the Bank's business

No transactions, arrangements or contracts to which the Bank, any of its parent company, its subsidiary undertakings or subsidiary undertakings of its parent company was a party and in which a director of the Bank had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

ZA BANK LIMITED

REPORT OF DIRECTORS (Continued)

Directors' interests in the shares, underlying shares and debentures of the Bank or any specified undertaking of the Bank

ZhongAn Technologies International Group Limited ("ZATI"), the sole shareholder of the parent company, and certain subsidiaries of ZATI maintain share schemes or plans which subsisted at the end of the year or at any time during the year, under which eligible participants of the Bank may be granted share options/restricted share units for acquisition of shares of the respective companies concerned.

During the year, Mr. IU Man Chung and Mr. NG Chung Ho, directors of the Bank, was granted share options of ZATI for acquisition of shares of the company concerned.

Apart from the above, at no time during the year was the Bank, any of its parent company, its subsidiary undertakings or subsidiary undertakings of its parent company a party to any arrangement to enable the directors of the Bank (including their spouse and children under 18 years of age) to acquire benefits by means of the acquisition of shares in, or debentures of, the company or any other body corporate.

Management contracts

No contracts concerning the management and administration of the whole or any substantial part of the business of the Bank were entered into or existed during the year.

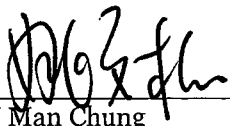
Permitted indemnity provision

A permitted indemnity provision (as defined in section 469 of the Hong Kong Companies Ordinance) for the benefit of the directors of the Bank is currently in force and was in force throughout the year.

Auditors

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

On behalf of the Board



IU Man Chung
Director and Chief Executive

Hong Kong, 26 March 2024



Independent Auditor's Report

To the Member of ZA Bank Limited
(incorporated in Hong Kong with limited liability)

Opinion

What we have audited

The financial statements of ZA Bank Limited (the "Bank"), which are set out on pages 8 to 66, comprise:

- the statement of financial position as at 31 December 2023;
- the statement of comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the cash flow statement for the year then ended; and
- the notes to the financial statements, comprising material accounting policy information and other explanatory information.

Our opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Bank as at 31 December 2023, and of its financial performance and its cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") and have been properly prepared in compliance with the Hong Kong Companies Ordinance.

Basis for Opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing ("HKSA") issued by the HKICPA. Our responsibilities under those standards are further described in the Auditor's 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

We are independent of the Bank in accordance with the HKICPA's Code of Ethics for Professional Accountants ("the Code"), and we have fulfilled our other ethical responsibilities in accordance with the Code.

Independent Auditor's Report

To the Member of ZA Bank Limited (Continued)
(incorporated in Hong Kong with limited liability)

Other Information

The directors are responsible for the other information. The other information comprises the information included in the report of directors, but does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements 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, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements 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 Directors and the Audit Committee for the Financial Statements

The directors are responsible for the preparation of the financial statements that give a true and fair view in accordance with HKFRSs issued by the HKICPA and the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, 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.

The Audit Committee is responsible for overseeing the Bank's financial reporting process.

Independent Auditor's Report

To the Member of ZA Bank Limited (Continued)
(incorporated in Hong Kong with limited liability)

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. We report our opinion solely to you, as a body, in accordance with Section 405 of the Hong Kong Companies Ordinance, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSAs 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 HKSAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, 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.
- 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.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- 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 auditor's report to the related disclosures in the financial statements 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 auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.



羅兵咸永道

Independent Auditor's Report

To the Member of ZA Bank Limited (Continued)
(incorporated in Hong Kong with limited liability)

Auditor's Responsibilities for the Audit of the Financial Statements (Continued)

We communicate with the Audit Committee 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.

A handwritten signature in black ink, appearing to read 'Francis Ho', is written over a light blue horizontal line.

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 26 March 2024

ZA BANK LIMITED
FINANCIAL STATEMENTS

STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2023

(All amounts in Hong Kong dollar thousands unless otherwise stated)

	Notes	Year ended 31 December 2023	Year ended 31 December 2022
Interest income	5	559,247	276,400
Interest expense	5	(296,940)	(84,146)
Net interest income		<u>262,307</u>	<u>192,254</u>
Fee and commission income	6	141,327	138,031
Fee and commission expense	6	(55,853)	(56,391)
Net fee and commission income		<u>85,474</u>	<u>81,640</u>
Net gain/(loss) from other financial instruments	7	13,711	(23,314)
Other income		4,437	5,524
Operating expenses	8	(654,181)	(705,435)
Operating loss before impairment losses		<u>(288,252)</u>	<u>(449,331)</u>
Credit impairment losses on loans and advances to customers		(102,914)	(27,948)
Credit impairment losses on other financial assets		(7,910)	(21,290)
Loss before income tax		<u>(399,076)</u>	<u>(498,569)</u>
Income tax	10	-	-
Net loss for the year		<u>(399,076)</u>	<u>(498,569)</u>
Other comprehensive income			
<i>Items that may be reclassified subsequently to profit or loss</i>			
- Changes in the fair value of debt instruments measured at FVOCI, net of tax		173,552	(334,816)
Total comprehensive loss for the year		<u>(225,524)</u>	<u>(833,385)</u>

The above statement of comprehensive income should be read in conjunction with the accompanying notes.

ZA BANK LIMITED
FINANCIAL STATEMENTS

STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2023

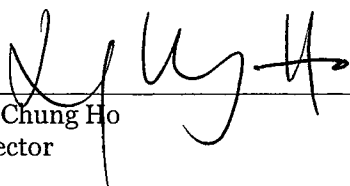
(All amounts in Hong Kong dollar thousands unless otherwise stated)

	Notes	2023	2022
ASSETS			
Cash and balances with banks	12	827,707	862,372
Placements with and advances to banks	13	128,862	134,272
Loans and advances to customers	14	5,318,601	4,880,747
Investment securities measured at FVOCI	15	7,473,496	5,569,008
Intangible assets	16	39,074	45,299
Fixed assets	17	432	1,252
Other assets	18	141,885	115,048
Total assets		13,930,057	11,607,998
LIABILITIES			
Deposits from customers	19	11,695,320	9,171,742
Other accounts and accruals	20	284,596	277,225
Total liabilities		11,979,916	9,448,967
EQUITY			
Share capital	21	4,100,000	4,100,000
Reserves		(161,012)	(351,198)
Accumulated losses		(1,988,847)	(1,589,771)
Total equity		1,950,141	2,159,031
Total liabilities and equity		13,930,057	11,607,998

The above statement of financial position should be read in conjunction with the accompanying notes.

The financial statements on pages 8 to 66 were approved by the board of directors on 26 March 2024 and were signed on its behalf.


 IU Man Chung
 Director


 NG Chung Ho
 Director

ZA BANK LIMITED
FINANCIAL STATEMENTS

STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2023

(All amounts in Hong Kong dollar thousands unless otherwise stated)

	Note	Share capital	Financial assets at FVOCI reserve	Share-based payment reserve	Accumulated losses	Total equity
Balance at 1 January 2022		3,600,000	(30,306)	1,223	(1,091,202)	2,479,715
Issue of ordinary shares	21	500,000	-	-	-	500,000
Net loss for the year		-	-	-	(498,569)	(498,569)
Share-based payment expenses	9,22	-	-	12,701	-	12,701
Other comprehensive income						
- Change in the fair value of debt instruments measured at FVOCI, net of tax		-	(334,816)	-	-	(334,816)
Balance at 31 December 2022 and 1 January 2023		4,100,000	(365,122)	13,924	(1,589,771)	2,159,031
Issue of ordinary shares	21	-	-	-	-	-
Net loss for the year		-	-	-	(399,076)	(399,076)
Share-based payment expenses	9,22	-	-	16,634	-	16,634
Other comprehensive income						
- Change in the fair value of debt instruments measured at FVOCI, net of tax		-	173,552	-	-	173,552
Balance at 31 December 2023		4,100,000	(191,570)	30,558	(1,988,847)	1,950,141

The above statement of changes in equity should be read in conjunction with the accompanying notes.

ZA BANK LIMITED
FINANCIAL STATEMENTS

CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2023

(All amounts in Hong Kong dollar thousands unless otherwise stated)

	Notes	Year ended 31 December 2023	Year ended 31 December 2022
OPERATING ACTIVITIES			
Loss before income tax		(399,076)	(498,569)
Adjustment for:			
Depreciation and amortization expense	8	19,260	11,812
Interest income from investment securities measured at FVOCI		(232,630)	(135,538)
Interest expense arising from lease liabilities	11	87	18
Change in expected credit losses		110,824	49,238
Share-based payment expenses	9,22	16,634	12,701
Net (gain)/loss from other financial instruments		(8,380)	23,314
Change in operating assets and liabilities:			
Decrease in placement with and advances to banks with original maturity beyond 3 months		50,577	498,192
Increase in other assets	18	(29,707)	(23,466)
Increase in loans and advances to customer	14	(540,768)	(2,392,384)
Increase in deposits from customers	19	2,523,578	2,105,919
Increase in other accounts and accruals	20	9,861	20,549
Net cash inflow/(outflow) to operating activities		1,520,260	(328,214)
INVESTING ACTIVITIES			
Purchase of investment securities measured at FVOCI		(17,656,197)	(2,836,137)
Proceeds from disposal and maturity of investment securities at FVOCI		16,039,632	1,756,390
Payments for intangible assets	16	(8,598)	(38,732)
Purchase of fixed assets	17	(79)	(858)
Interest received from investment securities measured at FVOCI		118,205	137,987
Net cash outflow to investing activities		(1,507,037)	(981,350)
FINANCING ACTIVITIES			
Proceeds from issue of ordinary shares	21	-	500,000
Principal and interest elements of lease payments	11	(3,254)	(2,144)
Net cash (outflow)/inflow from financing activities		(3,254)	497,856
Net increase/(decrease) in cash and cash equivalents		9,969	(811,708)
Cash and cash equivalents at the beginning of the financial year		946,068	1,769,416
Effect of exchange rate changes on cash and cash equivalents		547	(11,640)
Cash and cash equivalents at end of year		956,584	946,068

ZA BANK LIMITED
FINANCIAL STATEMENTS

CASH FLOW STATEMENT (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2023

(All amounts in Hong Kong dollar thousands unless otherwise stated)

	Notes	Year ended 31 December 2023	Year ended 31 December 2022
Cash and cash equivalents comprise:			
Cash and balances with banks	12	827,708	862,372
Placements with and advances to banks with original maturity of 3 months or less	13	128,876	83,696
		<u>956,584</u>	<u>946,068</u>

The above cash flow statement should be read in conjunction with the accompanying notes.

ZA BANK LIMITED
FINANCIAL STATEMENTS

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2023

(All amounts in Hong Kong dollar thousands unless otherwise stated)

1. General information

The Bank was officially launched on 24 March 2020 with principal activities of providing banking services to its customers. It is incorporated in Hong Kong as a limited company under the Hong Kong Companies Ordinance (Cap. 622) (“HKCO”). The address of its registered office is Unit 1301, Level 13, IT Street, Cyberport 3, 100 Cyberport Road, Hong Kong. The Bank provides banking services.

The Bank is a wholly-owned subsidiary of ZhongAn Financial Services Limited (the “parent company”). During the period from 1 January 2023 to 14 August 2023, the Bank was a subsidiary of ZhongAn Online P&C Insurance Co., Ltd. (the “ZA Online”), incorporated in the People’s Republic of China and listed on the Main Board of the Stock Exchange of Hong Kong. From 14 August 2023, the Bank is jointly controlled entity of ZA Online and Sinolink Worldwide Holdings Limited, incorporated in Bermuda and listed on the Main Board of the Stock Exchange of Hong Kong.

2. Summary of material accounting policies

This note provides a list of the material accounting policies adopted in the preparation of these financial statements. These policies have been consistently applied to all the years presented, unless otherwise stated.

The preparation of financial statements in conformity with Hong Kong Financial Reporting Standards (“HKFRS”) requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Bank’s accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in note 4.

2.1 Basis of preparation

(i) Compliance with HKFRS and HKCO

The financial statements of the Bank have been prepared in accordance with HKFRSs and requirements of the HKCO.

(ii) Historical cost convention

The financial statements have been prepared on a historical cost basis, except for investment securities measured at FVOCI.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2023

(All amounts in Hong Kong dollar thousands unless otherwise stated)

2. Summary of material accounting policies (Continued)

2.1 Basis of preparation (Continued)

(iii) New standards and amended standard adopted by the Bank

A number of new or amended standards that are relevant to the Bank and became applicable for the accounting period beginning on 1 January 2023. The Bank did not have to change its accounting policies or make retrospective adjustments as a result of adopting these standards.

Amendments to HKAS 8	Definition of Accounting Estimates
Amendments to HKAS 1 and HKFRS Practice Statement 2	Disclosure of Accounting Policies
Amendments to HKAS 1	Classification of Liabilities as Current or Non-current
Amendments to HKAS 12	Deferred Tax Relate to Assets and Liabilities Arising from a Single Transaction

(iv) New standards and amendments to standards that have been issued but are not effective:

		Effective for accounting periods beginning
Amendments to HKAS 1	Classification of Liabilities as Current or Non-current	1 January 2024
Amendments to HKFRS 16	Lease Liability in a Sale and Leaseback	1 January 2024
Amendments to HKAS 7 and HKFRS 7	Supplier finance arrangements	1 January 2024
Amendments to HKFRS 10 and HKAS 28	Sale or Contribution of Assets between an Investor and its Associate or Joint Ventures	To be determined

These standards are not expected to have a material impact on the entity in the current or future reporting periods and on foreseeable future transactions.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2023

(All amounts in Hong Kong dollar thousands unless otherwise stated)

2. Summary of material accounting policies (Continued)

2.2 Foreign currency translation

(i) Functional and presentation currency

Items included in the financial information are measured using the currency of the primary economic environment in which the Bank operates (“the functional currency”). The financial statements are presented in Hong Kong dollar, which is the Bank’s functional currency and presentation currency.

(ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies at year end exchange rates are generally recognized in profit or loss.

Foreign exchange gains and losses that relate to borrowings and all other foreign exchange gains and losses are presented in the statement of comprehensive income on a net basis within other income.

2.3 Interest income

Interest income is recognised in the statements of comprehensive income for all financial assets carried at amortised cost and fair value through other comprehensive income, and financial liabilities using the effective interest method. Similar interest income arising from non-derivative financial assets and liabilities carried at fair value through profit or loss are determined using similar method, but excluding their transaction costs. Interest income recognised is calculated based on the gross carrying amount of the financial asset unless it is a POCI financial asset, for which the original credit-adjusted effective interest rate is applied to the amortised cost of the financial asset; or the financial asset is credit-impaired (Stage 3), in which case interest income is calculated based on the amortised cost (i.e. the gross carrying amount less loss allowance) of the financial asset.

2.4 Fee and commission income

Fees and commissions income are recognized on an accrual basis when the service has been provided to customers.

Interchange fee

For debit card interchange activities, the Bank provides its customers with card processing services (i.e. authorization and settlement of transactions executed with the Bank’s cards) where it is entitled to an interchange fee for each transaction (i.e., when a cardholder purchases goods and services from merchants using the Bank’s card). The fees are based on the number of transactions processed and include both consideration at a fixed percentage of the underlying cardholder transaction and estimation of variable consideration, in which the Bank considers the sum of probability-weighted amounts in a range of possible consideration amounts.

Others

Loan fees for servicing a loan are recognized as fee income. Commissions and fees arising from negotiating, or participating in the negotiation of, a transaction for a third party are recognized when the act is completed.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2023

(All amounts in Hong Kong dollar thousands unless otherwise stated)

2. Summary of material accounting policies (Continued)

2.5 Operating expenses

Operating expenses consist primarily of employee benefit expense and advertising and promotion expense which are associated with the general operation of the Bank. Accounting policies of employee benefit expense is disclosed in note 2.12. Advertising and promotion expense includes but not limited to costs incurred from promotion, branding, customers acquisition and debit card reward programs to cardholders which are recognized as incurred.

2.6 Impairment of non-financial assets

Assets are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely independent of the cash inflows from other assets or groups of assets (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at the end of each reporting period.

2.7 Leases

Leases are recognized as a right-of-use asset and a corresponding liability at the date at which the leased asset is available for use by the Bank.

Assets and liabilities arising from a lease are initially measured on a present value basis. Lease liabilities include the net present value of the following lease payments:

- fixed payments (including in-substance fixed payments), less any lease incentives receivable
- variable lease payment that are based on an index or a rate, initially measured using the index or rate as at the commencement date. The lease payments are discounted using the interest rate implicit in the lease. If that rate cannot be readily determined, which is generally the case for leases in the Bank, the lessee's incremental borrowing rate is used, being the rate that the individual lessee would have to pay to borrow the funds necessary to obtain an asset of similar value to the right-of-use asset in a similar economic environment with similar terms, security and conditions. The interest expense is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

Lease payments are allocated between principal and finance cost. The finance cost is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

Right-of-use assets are measured at cost comprising the following:

- the amount of the initial measurement of lease liability
- any lease payments made at or before the commencement date less any lease incentives received
- any initial direct costs, and
- restoration costs.

Depreciation are calculated on the straight-line basis over the lease term.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2023

(All amounts in Hong Kong dollar thousands unless otherwise stated)

2. Summary of material accounting policies (Continued)

2.8 Financial assets

(i) Recognition and derecognition

Financial assets are recognized when the Bank becomes a party to the contractual provisions of the instrument. Regular way purchases and sales of financial assets are recognized on trade-date, the date on which the Bank commits to purchase or sell the asset.

(ii) Measurement

At initial recognition, the Bank measures a financial asset at its fair value plus, in the case of a financial asset not at FVPL, transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVPL are expensed in profit or loss.

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

Debt instruments

Subsequent measurement of debt instruments depends on the Bank's business model for managing the asset and the cash flow characteristics of the asset. There are three measurement categories into which the Bank classifies its debt instruments:

- Amortised cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortised cost. Interest income from these financial assets is included in finance income using the effective interest rate method. Any gain or loss arising on derecognition is recognised directly in profit or loss and presented in other gains/(losses) together with foreign exchange gains and losses. Impairment losses are presented as separate line item in the consolidated statements of comprehensive income.
- FVOCI: Assets that are held for collection of contractual cash flows and for selling the financial assets, where the assets' cash flows represent solely payments of principal and interest, are measured at FVOCI. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest income and foreign exchange gains and losses which are recognised in profit or loss. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss and recognised in other gains/(losses). Interest income from these financial assets is included in finance income using the effective interest rate method. Foreign exchange gains and losses are presented in other gains/(losses) and impairment expenses are presented as separate line item in the consolidated statements of comprehensive income.
- FVPL: Assets that do not meet the criteria for amortised cost or FVOCI are measured at FVPL. A gain or loss on a debt investment that is subsequently measured at FVPL is recognised in profit or loss and presented net within other gains/(losses) in the period in which it arises.

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2. Summary of material accounting policies (Continued)

2.8 Financial assets (Continued)

(iii) Impairment

The Bank assesses on a forward looking basis the expected credit losses associated with its short-term bank deposits, cash and cash equivalents, loans and advances to customers and investments. The impairment methodology applied depends on whether there has been a significant increase in credit risk. At initial recognition, allowance is required for expected credit loss resulting from default events that are possible within the next 12 months. In the event of a significant increase in credit risk, allowance is required for expected credit loss resulting from all possible default events over the expected life of the financial instrument. For financial assets that is credit-impaired at the reporting date, the Bank measure the expected credit loss as the difference between the asset's gross carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate.

(iv) Modification of financial assets

If the terms of a financial asset are modified, the Bank evaluates whether the cash flows of the modified asset are substantially different. If the cash flows are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognized, and a new financial asset is recognized at fair value. If the terms are not substantially different, the renegotiation or modification does not result in derecognition, the financial asset continues to be subject to the same assessments for significant increase in credit risk relative to initial recognition and credit-impairment.

(v) Derecognition other than on a modification

Financial assets, or a portion thereof, are derecognized when the contractual rights to receive the cash flows from the assets have expired, or when they have been transferred and either (i) the Bank transfers substantially all the risks and rewards of ownership, or (ii) the Bank neither transfers nor retains substantially all the risks and rewards of ownership and the Bank has not retained control. The Bank enters into transactions where it retains the contractual rights to receive cash flows from assets but assumes a contractual obligation to pay those cash flows to other entities and transfers substantially all of the risks and rewards. These transactions are accounted for as "pass through" transfers that result in derecognition if the Bank:

- i. has no obligation to make payments unless it collects equivalent amounts from the assets;
- ii. is prohibited from selling or pledging the assets; and
- iii. has an obligation to remit any cash it collects from the assets without material delay.

Collateral furnished by the Bank under standard repurchase agreements and securities lending and borrowing transactions are not derecognized because the Bank retains substantially all the risks and rewards on the basis of the predetermined repurchase price, and the criteria for derecognition are therefore not met.

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2. Summary of material accounting policies (Continued)

2.8 Financial assets (Continued)

(vi) Write off

The Bank writes off financial assets, in whole or in part, when it has exhausted all practical recovery efforts and has concluded there is no reasonable expectation of recovery. Indications that there is no reasonable expectation of recovery include (i) ceasing enforcement activity and (ii) where the Bank's recovery method is foreclosing on collateral and the value of the collateral is such that there is no reasonable expectation of recovering in full.

2.9 Financial liabilities

(i) Recognition and derecognition

Financial liabilities are recognized when the Bank becomes a party to the contractual provisions of the instrument. Regular way purchases and sales of financial liabilities are recognized on trade-date, the date on which the Bank commits to purchase or sell the liabilities.

(ii) Classification and subsequent measurement

At initial recognition, the Bank measures a financial liability at its fair value, net of transaction costs incurred (if any) and subsequently at AC using the effective interest method.

2.10 Cash and cash equivalents

For the purpose of presentation in the statement of cash flows, cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, other short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

2.11 Share capital

Ordinary shares are classified in equity when there is not any obligation to transfer cash or other assets to the holders.

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

2.12 Employee benefit expense

(i) Short-term obligations

Liabilities for wages and salaries, including bonus and annual leave that are expected to be settled wholly within 12 months after the end of the period in which the employees render the related service are recognized in respect of employees' services up to the end of the reporting period and are measured at the amounts expected to be paid when the liabilities are settled. The liabilities are presented as current employee benefit obligations in the balance sheet.

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2. Summary of material accounting policies (Continued)

2.12 Employee benefit expense (Continued)

(ii) Defined contribution schemes

The employees of the Bank participate in various defined contribution pension plans principally organized by municipal and provincial governments. Contributions to defined contribution schemes, such as the Mandatory Provident Fund (“MPF”) Scheme, are expensed as incurred. The Bank has no other significant legal or constructive obligations for retirement benefits beyond the said contributions, which are expensed as incurred.

The Bank pays early retirement benefits to those employees who accept early retirement arrangements approved by management. Early retirement benefits are paid to those employees who voluntarily retire before the normal retirement date. The related benefit payments are made from the date of early retirement through the normal retirement date. The Bank records a liability for the present value of its early retirement obligation when employees retire early.

2.13 Share-based payments

The Bank granted an equity-settled share-based compensation plan, under which the Bank receives services from employees as consideration for equity instruments of the intermediate holding company of the Bank. The fair value of the employee services received in exchange for the grant of the equity instruments is recognised as an expense. The total amount to be expensed is determined by reference to the fair value of the equity instruments granted:

- Including any market performance conditions;
- Excluding the impact of any service and non-market performance vesting conditions; and
- Including the impact of any non-vesting conditions.

At the end of each reporting period, the Bank revises its estimates of the number of equity instruments that are expected to vest based on the non-marketing performance and service conditions. It recognises the impact of the revision to original estimates, if any, in the statement of comprehensive income, with a corresponding adjustment to equity.

If the terms of an equity-settled award are modified, at a minimum an expense is recognised as if the terms had not been modified. An additional expense is recognised for any modification that increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee, as measured at the date of modification.

If an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new award are treated as if they were a modification of the original award, as described in the previous paragraph.

2.14 Provisions

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount has been reliably estimated. Provisions are not recognised for future losses.

2.15 Other payables

These amounts represent other accruals for expenses incurred prior to the end of financial year which are unpaid. The amounts are unsecured. They are recognized initially at their fair value and subsequently measured at AC using the effective interest method.

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2. Summary of material accounting policies (Continued)

2.16 Current and deferred income tax

The income tax expense or credit for the period is the tax payable on the current period's taxable income based on the applicable income tax rate for each jurisdiction adjusted by changes in deferred tax assets and liabilities attributable to temporary differences and to unused tax losses.

Current income tax

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting period in the countries where the Bank operates and generates taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax

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

Deferred tax assets are recognized only if it is probable that future taxable amounts will be available to utilize those temporary differences and losses.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets and liabilities and when the deferred tax balances relate to the same taxation authority.

Current tax assets and tax liabilities are offset where the Bank has a legally enforceable right to offset and intends either to settle on a net basis, or to realize the asset and settle the liability simultaneously.

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2. Summary of material accounting policies (Continued)

2.17 Intangible assets

Expenditure on maintaining computer software is recognized as an expense in the period in which it is incurred. Expenditure on development activities is capitalized if the product or process is technically and commercially feasible and the Bank has sufficient resources and the intention to complete development. The expenditure capitalized includes the costs of materials, direct labor, and an appropriate proportion of overheads and borrowing costs, where applicable. Capitalized development costs are stated at cost less accumulated amortization and impairment losses. Other development expenditure is recognized as an expense in the period in which it is incurred. Other intangible assets that are acquired by the Bank are stated at cost less accumulated amortization (where the estimated useful life is finite) and impairment losses.

Amortization methods and periods

The Bank amortizes intangible assets with a limited useful life using the straight-line method over the following periods:

- Software 3-5 years

Intangible assets are not amortized while their useful lives are assessed to be indefinite. Any conclusion that the useful life of an intangible asset is indefinite is reviewed annually to determine whether events and circumstances continue to support the indefinite useful life assessment for that asset. If they do not, the change in the useful life assessment from indefinite to finite is accounted for prospectively from the date of change and in accordance with the policy for amortization of intangible assets with finite lives as set out above.

2.18 Fixed assets

Equipment are stated at historical cost less depreciation. Depreciation are calculated on the straight-line basis over 3 years to write off the assets over their estimated useful lives.

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. The carrying amount of any component accounted for as a separate asset is derecognized when replaced. All other repairs and maintenance are charged to profit or loss during the reporting period in which they are incurred.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in profit or loss.

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3. Financial risk management

This note explains the Bank's exposure to financial risks and how these risks could affect the Bank's future financial performance.

3.1 Financial risk factors

The Bank conducts its business activities and operations by identifying, assessing, measuring, monitoring and reporting the key inherent risks. By effectively managing such risks, the Bank intends to strike a balance between the amount and types of risks the Bank is willing to take, and the level of return the Bank aims to achieve.

The Bank has a risk governance and management framework in place to ensure the risk inherent in the business activities is being managed properly, to comply with the regulatory requirement set out by the regulators and to assess the adequacy of internal capital accordingly. These objectives are delivered through means of properly defined risk appetite in accordance with the Bank's business strategies, risk policies that established controls and limits to identify, assess, monitor and remedy the risk and formulated through clear procedures for execution of these policies.

The governance structure covers three layers including the board of directors and its subordinate committees, the senior management and the functional committees and the three lines of defence formed from risk management units.

The board of director has the ultimate responsibility for overseeing the risk governance of the Bank and is responsible for ensuring an effective organizational risk management framework in place for both business and regulatory purposes. The Board has the final authority to determine the optimal risk appetite in the interest of shareholder and formulate the appropriate risk management strategy and enforce the correct risk culture within the organization. For effective management, the Board has delegated authority to several Board-level committees to carry out risk management tasks. The Board-level committees include Audit Committee, Nomination Committee, Remuneration Committee and Risk Committee ("RC"). Risk Committee is responsible for reviewing material issues escalated by management-level committee and to monitor the Bank's risk management strategies, key risk policies and risk appetite on a regular basis.

The Board has also established Executive Committee ("EXCO"), which is a management-level committee to review the overall business objectives of the Bank and business strategies and business plans. In addition, senior management also established several management-level committees under the committees delegated by the Board to oversee the governance of the Bank and provide oversight of various risk disciplines. The management-level committees include New Product Committee, Model Governance Committee, Disciplinary Committee, Technology and Cyber Resilience Committee, Asset & Liability Management Committee ("ALCO"), Regulatory and Financial Crime Compliance Committee, Credit Committee, Risk Management Committee ("RMC"), Wealth Management Committee and Bancassurance Committee. They are responsible for the risk management tasks including reviewing and approving policies in accordance with the regulatory requirement and business strategies regularly, initiating new risk management strategies and measures in response to the launch of new product and services, and regulatory change and providing advice on material risk-related activities to the Board-level committee.

The Bank implements a "three lines of defence" approach to ensure effective risk management across the Bank. Frontline business units act as the first line of defence for risk management and are responsible for soliciting business in compliance with the risk policies and procedures, assuring the risk level of their business within the internal risk limits.

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

Various risk management units represent the second line of defence which are independent of the business units and are responsible for day-to-day management tasks including identifying, assessing and monitoring the risk in the business, reporting the implementation of risk procedures and the risk profiles of the business to the functional committee and providing support to senior management for decision-making.

Internal audit acts as the third line of defence and is responsible for conducting independent checking on the adequacy of internal policies and the execution of the procedures and controls. They are also responsible for reporting to the senior management, providing recommendations to improve the internal policies and procedures.

The Bank adopts the risk approach set out by the Hong Kong Monetary Authority (“HKMA”) in managing risk with eight types of principle risks including credit risk, market risk, interest rate risk, liquidity risk, operational risk, technology risk, reputation risk, and strategic risk. The Bank establishes various risk limits and indicators in the risk appetite and reports it to the senior management and the Board regularly. Any breaches on these limits is reported to the senior management and the Board, and remediation actions are to be carried out accordingly.

Our risk culture is reflected in the risk tolerance level stipulated in Risk Appetite Statement (“RAS”) which specifies the limits of major risk areas. RAS is approved by the board and fully communicated to the RC, EXCO and Core Bank Team. Its daily enforcement is regularly reviewed by RMC.

Reports of risk management are regularly reported by the respective risk management and function units to the management-level committees, RMC, EXCO and RC for reviews. Hits of Early Warning Indicators (“EWI”) and breaches of internal and/or external limit will lead to risk mitigation actions submitted to appropriate management level and board level committee for approvals.

Stress testing is an essential tool for the Bank’s overall risk management. The Bank regularly applies stress testing techniques to assess the risk tolerance level of the Bank under stress scenarios on individual risk disciplines covering the Bank’s major portfolios and applies risk mitigation strategy and contingency plans accordingly.

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk

Risk management

Credit risk is the potential that a borrower or counterparty will fail to meet its obligations with agreed terms. Credit risk exists throughout the activities of the Bank, including in the banking book, and both on- and off-balance sheet transactions. The credit risk exposure principally arises from investment in debt securities, lending of personal loan, commercial loan and corporate loan.

The Bank has formulated a comprehensive set of policies and procedures that outlines the governance framework and appropriate credit limits to manage and monitor the credit risk that may arise from different credit portfolios in both portfolio level and individual level. The policies cover various areas including credit risk governance structure, customer selection criteria, customer acceptance criteria and post-approval monitoring. The principal objectives of such mechanism are:

- To analyse the credit risks of various credit portfolios, geographic locations of borrowers and types of loans, etc.;
- To forecast and monitor any changes in the credit rating and risk return dynamics in each credit portfolio;
- To evaluate the components and allocations of the credit portfolios regularly and make timely adjustments in case of changes in the economic environment/industry situations; and
- To implement effective capital and resources allocation over different types of credit-related activities, mainly through the re-balancing and controlling of the portfolios and the migration of the overall portfolio's credit risk hedging.

The overall credit risk is managed through a hierarchy of approval authorities of the Bank.

The Bank has established a comprehensive monitoring process and intends to manage the risk level in the credit portfolio that aligns with the Bank's risk appetite and identify any early warning signal of credit deterioration. Various metrics are adopted to assess and monitor the quality of credit exposure in both acquisition stage and post-approval stage. Accounts are classified into different risk levels based on their latest credit status and history. Loan facilities that miss the scheduled payment are managed separately with proper follow-up action. In addition to the condition of the customers, the quality of credit exposure may deteriorate due to adverse economic environment.

The Bank monitors the performance of key macro-economic indicators. The Bank also applies stress testing technique periodically to assess the vulnerability of the credit portfolio under adverse market condition. Ad hoc stress assessment will also be conducted when market seems to deteriorate.

The quality of the overall credit portfolio is assessed and monitored monthly by a few key indicators including 30 days-past-due ratio and gross credit charge-off amount in a calendar year. Senior management of the Bank is alerted if the indicators breach the limit defined in risk appetite. Remedial action may be taken if necessary.

The Bank also aims at holding a credit portfolio that has diversified characteristics to minimize the concentration risk. The Bank identifies credit concentration risk by nature of products, geography, customer, counterparty and industry. The Bank aims to pursue a diversified credit portfolio, with no concentration on a single customer and industry.

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

Expected credit loss (“ECL”) measurement

As explained in note 2.8(iii), the Bank assesses on a forward-looking basis the ECL associated with its cash and amounts due from banks and other financial institutions, loans and advances to customers including commitments, and investment securities measured at FVOCI. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

Under HKFRS 9, ECL exposures are classified into three stages:

- Stage 1 applies when there is no significant increase in credit risk since initial recognition. 12-month ECL is required for assets classified in stage 1.
- Stage 2 applies when a significant increase in credit risk has occurred on an individual or collective basis since initial recognition, with no objective evidence of credit event. Lifetime ECL calculation is required for assets classified in stage 2.
- Stage 3 applies when there is objective evidence of credit impairment. Lifetime ECL calculation is required for assets classified in stage 3.

Significant credit deterioration criteria have to be defined for assessing significant increases in credit risk, primarily based on the key requirements summarized below:

- Risk of default occurring at reporting time is compared against that of initial recognition
- Days past due exceeds 30 days
- Credit exhibits a deterioration in repayment ability
- Number of external rating notches downgraded three notches or more
- When the borrower is reported as Special Mention according to the loan classification of the HKMA. The decision to classify the loans is based on the borrower’s repayment ability and likelihood of individual counterparties defaulting.

When a financial instrument has objective evidence of impairment, such as default (considered to be default if it is 90 days past due), debt restructuring, inability of obtaining full repayment of principal on due date, bankruptcy of borrowers, it is classified as stage 3 exposure. Discounted cash flows model is conducted to estimate the expected credit loss of such exposures.

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

Calculation of ECL

The Bank has adopted to use the statistical model approach, under which stage 1 and stage 2 ECL is calculated as a function of probability of default (“PD”), loss given default (“LGD”), exposure at default (“EAD”) and expected life. To recognize ECL for financial instruments and incorporate forward-looking elements into the model, historical, current and forward-looking data are used in ECL calculation model.

Point-in-Time (“PiT”) PD is adopted in the ECL estimation. The Bank takes into account both qualitative and quantitative criteria while determining the approach for each product type.

LGD measures the loss severity in case of default, i.e. how much the Bank expects to lose as a percentage of EAD when an account goes into default. It considers both secured portion and unsecured portion of the facility.

EAD is the amount that an entity is exposed to at the time of a loan’s default. Financial assets measured at amortized cost, fair value through other comprehensive income, loan commitment and financial guarantee contract are subject to impairment under HKFRS 9. We categorized these exposures into: 1) On-balance sheet financial assets; 2) Undrawn exposures, which can be further separated into i) Irrevocable; ii) Revocable retail; and iii) Revocable non-retail. The value of credit conversion factor (“CCF”) reflects the expected amount of undrawn amount to be drawn. The Bank uses regulatory CCF, i.e. 50% and adjusted by internal loss experience and expert judgment if available. For syndicated loan, due to expert judgement towards its committed nature, a higher CCF is expected and thus CCF of 100% is adopted.

From time to time, the Bank has established three macroeconomic scenarios for the ECL estimation. In the uncertain macroeconomic outlook, more weight is placed on a downside scenario. The Bank continues to revisit and validate these macroeconomic scenarios in response to the changes of macro-environment. The final ECL is the probability weight-average result of these scenarios discounted to the date of the statement of financial position. The discount rate used is the effective interest rate.

Other assets are measured as either 12 months expected credit losses or lifetime expected credit losses, depending on whether there has been a significant increase in credit risk since initial recognition. In making this assessment, the Bank considers both quantitative and qualitative information that is reasonable and supportable, including historical experience and forward-looking information that is available.

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

Incorporation of forward-looking information into the ECL models

HKFRS 9 requires an estimate of forward-looking ECL which is typically obtained through the use of forecasted macroeconomic factors (“MEFs”).

The Bank has developed three scenarios for macro-economic factors:

Scenario	Underlying assumptions of the scenario
Base	The base scenario is based on a set of macroeconomic forecasts which formulate a “base case” view of the most probable future direction of relevant economic variables.
Good	This scenario is determined by making reference to the “base” scenario and reflects positive uncertainties by incorporating upside variations to the “base” scenario macroeconomic forecasts.
Bad	This scenario is determined by making reference to the “base” scenario and reflects negative uncertainties by incorporating downside variations to the “base” scenario macroeconomic forecasts.

The Bank has considered the current economic performance, the market forecast and the management judgment on the economic outlook and assigned probability weighting to Good, Base and Bad Scenarios:

	31 December 2023	31 December 2022
Good	30%	15%
Base	40%	45%
Bad	30%	40%

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

Incorporation of forward-looking information into the ECL models (Continued)

At 31 December 2023

The significant assumptions used for ECL estimations for the retail exposure are as follows:

		2024	5 years'
	Scenario	Forward- looking (Year end)	average (2024-2028)
Hong Kong Forecast Factors			
Hong Kong Unemployment Rate (%)	Good	2.50	2.79
	Base	3.00	3.12
	Bad	4.45	4.01
Property Price Index – Private Retail (Base Year: 1999)	Good	598.80	704.45
	Base	577.71	673.32
	Bad	505.40	601.14

The significant assumptions used for ECL estimations for the wholesale exposure are as follows:

		2024	5 years'
	Scenario	Forward- looking (Year end)	average (2024-2028)
Hong Kong Forecast Factors			
Real Gross Domestic Product Growth Rate (%)	Good	7.42	3.53
	Base	3.97	2.31
	Bad	-5.80	0.93
Hong Kong Industrial Production: Manufacturing Index (Base Year: 2010)	Good	104.15	104.98
	Base	98.42	97.12
	Bad	82.54	87.31
Change in Hong Kong General Government Balance to GDP Ratio (%)	Good	0.16	1.03
	Base	-0.60	0.18
	Bad	-3.05	-1.64

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

Incorporation of forward-looking information into the ECL models (Continued)

At 31 December 2023 (Continued)

		2024	5 years'
	Scenario	Forward- looking (Year end)	average (2024-2028)
Mainland China Forecast Factors			
China Government Expenditure, Total (CNY Billion)	Good	29,468.57	36,093.37
	Base	32,522.92	36,446.53
	Bad	33,437.78	35,329.92
China Unemployment Rate (%)	Good	3.66	3.75
	Base	4.05	4.04
	Bad	4.94	4.81

At 31 December 2022

The significant assumptions used for ECL estimations for the retail exposure are as follows:

		2023	5 years'
	Scenario	Forward- looking (Year end)	average (2023-2027)
Hong Kong Forecast Factors			
Hong Kong Unemployment Rate (%)	Good	3.21	3.16
	Base	3.74	3.48
	Bad	5.17	4.35
Property Price Index – Private Retail (Base Year: 1999)	Good	573.00	661.17
	Base	543.66	627.86
	Bad	458.76	546.33

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

Incorporation of forward-looking information into the ECL models (Continued)

At 31 December 2022 (Continued)

The significant assumptions used for ECL estimations for the wholesale exposure are as follows:

		2023	
	Scenario	Forward- looking (Year end)	5 years' average (2023-2027)
Hong Kong Forecast Factors			
Real Gross Domestic Product Growth Rate (%)	Good	6.40	3.14
	Base	4.74	2.54
	Bad	-1.74	1.36
Hong Kong Industrial Production: Manufacturing Index (Base Year: 2010)	Good	129.63	127.83
	Base	116.69	117.58
	Bad	82.04	94.23
Change in Hong Kong General Government Balance to GDP Ratio (%)	Good	3.40	1.31
	Base	2.83	0.78
	Bad	-2.89	-2.41
Mainland China Forecast Factors			
China Government Expenditure, Total (CNY Billion)	Good	26,702.86	32,541.24
	Base	29,355.42	32,671.26
	Bad	30,164.73	31,565.71
China Unemployment Rate (%)	Good	3.55	3.72
	Base	4.00	4.01
	Bad	5.03	4.78

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3 Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

Management Overlay

The Bank has applied management overlay in its ECL estimation as at 31 December 2023 to supplement the limitations of existing ECL models which may not be able to fully reflect the obligor specific circumstance and potential credit deterioration of certain loan exposures. The amount of the management overlay represented approximately 0.09% of the overall loan exposures. The Bank did not apply any management overlay as at 31 December 2022.

Sensitivity analysis

As at 31 December 2023 and 2022, sensitivity analysis is conducted for the impact of impairment allowance results against the forward-looking macroeconomic variables on the basis that (i) Good scenario weight increases by 10% and Base scenario weight is lowered by 10%; (ii) Bad scenario weight increases by 10% and Base scenario weight is lowered by 10%; as follows:

	2023	2022
Good +10% and base -10%	(827)	(483)
Bad +10% and base -10%	3,948	3,270

Credit Risk Grading

In order to fulfil the requirements of probability weighted forward-looking ECL, PiT PD is adopted in the ECL estimation. The Bank took into account both qualitative and quantitative criteria while determining the approach for each product type. Three approaches were developed to capture the specific risk characteristics of products:

Exposure other than retail and commercial loans:

The principle of risk factor approach is to convert through-the-cycle ("TTC") PD, i.e. historical long-term average transition matrix, to PiT PD, i.e. transition matrix in a particular year reflecting the current economic situation at that time.

- Z risk factor approach for treasury investments and corporate loans: Due to insufficient internal default data, the Bank built the PD model using external credit data i.e. transition matrix for treasury and corporate portfolios.

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FOR THE YEAR ENDED 31 DECEMBER 2023

(All amounts in Hong Kong dollar thousands unless otherwise stated)

3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

Credit Risk Grading (Continued)

Retail loans:

Based on external aggregated default data, point in time PD for each rating is calculated.

- Default curve extrapolation approach: Due to insufficient internal data in personal instalment loans and revolving facilities, the Bank leveraged the aggregated retail loan default rate data by rating and developed the PD model using the curve extrapolation approach for unsecured personal loans.

Commercial loans:

- Moody's off-the-shelf PIT PD Converter and GCorr Macro model are applied in commercial loans. They provide model estimation by region and industry in point-in-time and forward-looking adjustment, the data used are specific and applicable to instruments within specific country and industry.

Write-off policy

The Bank writes off financial assets, in whole or in part, when it has exhausted all practical recovery efforts and has concluded there is no reasonable expectation of recovery.

The Bank may write-off financial assets that are still subject to enforcement activity. The outstanding contractual amounts of such assets written off during the years ended 31 December 2023 and 2022 were approximately HK\$78,906,000 and HK\$16,101,000 respectively. The Bank still seeks to recover amounts it is legally owned in full, but which have been partially written off due to no reasonable expectation of full recovery.

Credit risk exposure

As at 31 December 2023 and 2022, credit risk arises mainly from cash and amounts due from bank and other financial institutions, loans and advances to customers including commitments, investment securities measured at FVOCI, and other assets.

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

The following tables contain analysis of the credit risk exposure of financial instruments. The gross carrying amount/exposure of financial assets below also represents the Bank's maximum exposure to credit risk on these assets.

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(All amounts in Hong Kong dollar thousands unless otherwise stated)

3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

Credit risk exposure (Continued)

Maximum exposure to credit risk before collateral held or other credit enhancements (Continued)

Financial assets subject to impairment

At 31 December 2023

	Gross carrying amount/exposure			Total	ECL allowance	Net
	Pass	Special mention	Sub-standard or below			
Loans and advances to customers						
-Stage 1	5,077,570	-	-	5,077,570	(56,694)	5,020,876
-Stage 2	-	255,232	-	255,232	(12,101)	243,131
-Stage 3	-	-	97,523	97,523	(42,929)	54,594
Investment securities measured at FVOCI						
-Stage 1	7,551,225	-	-	7,551,225	(4,606)	7,546,619
-Stage 2	80,237	-	-	80,237	(1,334)	78,903
-Stage 3	-	-	-	-	-	-
Cash and amounts due from banks						
-Stage 1	956,489	-	-	956,489	(15)	956,474
-Stage 2	-	-	-	-	-	-
-Stage 3	-	-	-	-	-	-
Credit commitments						
-Stage 1	386,230	-	-	386,230	(1,452)	384,778
-Stage 2	-	115	-	115	(17)	98
-Stage 3	-	-	173	173	-	173
Other assets						
-Stage 1	126,088	-	-	126,088	-	126,088
-Stage 2	-	-	-	-	-	-
-Stage 3	-	-	-	-	-	-
Total	14,177,839	255,347	97,696	14,530,882	(119,148)	14,411,734

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NOTES TO THE FINANCIAL STATEMENTS
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(All amounts in Hong Kong dollar thousands unless otherwise stated)

3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

Credit risk exposure (Continued)

Maximum exposure to credit risk before collateral held or other credit enhancements (Continued)

Financial assets subject to impairment (Continued)

At 31 December 2022

	Gross carrying amount/exposure			Total	ECL allowance	Net
	Pass	Special mention	Sub-standard or below			
Loans and advances to customers						
-Stage 1	4,777,951	-	-	4,777,951	(35,383)	4,742,568
-Stage 2	-	143,361	-	143,361	(5,078)	138,283
-Stage 3	-	-	6,588	6,588	(6,588)	-
Investment securities measured at FVOCI						
-Stage 1	5,841,710	-	-	5,841,710	(6,437)	5,835,273
-Stage 2	53,232	-	-	53,232	(378)	52,854
-Stage 3	-	-	38,988	38,988	(31,190)	7,798
Cash and amounts due from banks						
-Stage 1	996,581	-	-	996,581	(2)	996,579
-Stage 2	-	-	-	-	-	-
-Stage 3	-	-	-	-	-	-
Credit commitments						
-Stage 1	330,575	-	-	330,575	(1,001)	329,574
-Stage 2	-	14,563	-	14,563	(478)	14,085
-Stage 3	-	-	56	56	-	56
Other assets						
-Stage 1	100,157	-	-	100,157	-	100,157
-Stage 2	-	-	-	-	-	-
-Stage 3	-	-	-	-	-	-
Total	12,100,206	157,924	45,632	12,303,762	(86,535)	12,217,227

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(All amounts in Hong Kong dollar thousands unless otherwise stated)

3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

Collateral and other credit enhancements

The Bank employs a range of policies and practices to mitigate credit risk. The most common of these methods is the taking of collateral for funds advanced. The Bank has internal guidelines on the acceptability of specific classes of collateral for credit risk mitigation. Guideline is in place to govern the management of collateral acceptable by the Bank and the guideline is reviewed periodically.

The Bank prepares a valuation of the collateral obtained as part of the loan origination process. This assessment is reviewed periodically. The principal collateral types for loans and advances are:

- Mortgages over properties;
- Charges over land; and
- Charges over bank deposits.

In addition to the above, the Bank will also seek for guarantee where appropriate. To minimise credit loss, the Bank will seek additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances which are partially secured or unsecured.

As of 31 December 2023, impaired loans and advances are partially covered by collateral whereas impaired loans and advances as at December 2022 are not covered by collateral. For the exposures of balances with central banks, placements with and advances to banks and investment securities measured at FVOCI, it is typically unsecured and uncollateralized. For loans and advances to customers as of 31 December 2023 and 31 December 2022, 50.2% and 36.4% of the exposures are covered by collateral and other security, respectively.

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(All amounts in Hong Kong dollar thousands unless otherwise stated)

3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

The following tables explain the changes in the loss allowance between the beginning and the end of the annual period due to these factors:

Loans and advances to customers

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total
Loss allowance as at 1 January 2022	29,733	246	4,685	34,664
Transfer to Stage 1	88	(88)	-	-
Transfer to Stage 2	(630)	630	-	-
Transfer to Stage 3	(12,469)	(3)	12,472	-
Changes in ECL from financial assets originated, purchased, derecognized and model parameters change	18,661	4,293	4,993	27,947
Write-offs	-	-	(16,101)	(16,101)
Recoveries	-	-	539	539
Loss allowance as at 31 December 2022 and 1 January 2023	35,383	5,078	6,588	47,049
Transfer to Stage 1	-	-	-	-
Transfer to Stage 2	(742)	742	-	-
Transfer to Stage 3	(39,153)	(1,904)	41,057	-
Changes in ECL from financial assets originated, purchased, derecognized and model parameters change	61,206	8,185	33,524	102,915
Write-offs	-	-	(38,933)	(38,933)
Recoveries	-	-	693	693
Loss allowance as at 31 December 2023	56,694	12,101	42,929	111,724

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(All amounts in Hong Kong dollar thousands unless otherwise stated)

3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

The following tables explain the changes in the loss allowance between the beginning and the end of the annual period due to these factors:

Treasury investments

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total
Loss allowance as at 1 January 2022	1,760	15,564	-	17,324
Transfer to Stage 1	-	-	-	-
Transfer to Stage 2	(113)	113	-	-
Transfer to Stage 3	-	(15,564)	15,564	-
Changes in ECL from financial assets originated, purchased, derecognized and model parameters change	4,790	265	15,626	20,681
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Loss allowance as at 31 December 2022 and 1 January 2023	6,437	378	31,190	38,005
Transfer to Stage 1	-	-	-	-
Transfer to Stage 2	(51)	51	-	-
Transfer to Stage 3	-	-	-	-
Changes in ECL from financial assets originated, purchased, derecognized and model parameters change	(1,780)	905	8,783	7,908
Write-offs	-	-	(39,973)	(39,973)
Recoveries	-	-	-	-
Loss allowance as at 31 December 2023	<u>4,606</u>	<u>1,334</u>	<u>-</u>	<u>5,940</u>

For the purpose of this disclosure, ECL of financial assets measured at FVOCI is included in loss allowance.

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

The following tables explain the changes in the gross exposure (gross carrying amount or exposure) between the beginning and the end of the annual period due to these factors:

Loans and advances to customers

	Stage 1 Gross exposure	Stage 2 Gross exposure	Stage 3 Gross exposure	Total
As at 1 January 2022	2,545,368	944	4,685	2,550,997
Transfer to Stage 1	262	(262)	-	-
Transfer to Stage 2	(142,192)	142,192	-	-
Transfer to Stage 3	(20,765)	(11)	20,776	-
Net change in exposure	2,395,278	498	(2,772)	2,393,004
Write-offs	-	-	(16,101)	(16,101)
	<hr/>	<hr/>	<hr/>	<hr/>
As at 31 December 2022 and 1 January 2023	4,777,951	143,361	6,588	4,927,900
Transfer to Stage 1	-	-	-	-
Transfer to Stage 2	(129,869)	129,869	-	-
Transfer to Stage 3	(125,404)	(10,098)	135,502	-
Net change in exposures	554,892	(7,900)	(5,634)	541,358
Write-offs	-	-	(38,933)	(38,933)
	<hr/>	<hr/>	<hr/>	<hr/>
As at 31 December 2023	<u>5,077,570</u>	<u>255,232</u>	<u>97,523</u>	<u>5,430,325</u>

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(All amounts in Hong Kong dollar thousands unless otherwise stated)

3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(i) Credit risk (Continued)

The following tables explain the changes in the gross exposure (gross carrying amount or exposure) between the beginning and the end of the annual period due to these factors:

Treasury investments

	Stage 1 Gross exposure	Stage 2 Gross exposure	Stage 3 Gross exposure	Total
As at 1 January 2022	4,832,489	39,303	-	4,871,792
Transfer to Stage 1	-	-	-	-
Transfer to Stage 2	(53,900)	53,900	-	-
Transfer to Stage 3	-	(38,988)	38,988	-
Net change in exposure	1,063,121	(983)	-	1,062,138
Write-offs	-	-	-	-
	<hr/>	<hr/>	<hr/>	<hr/>
As at 31 December 2022 and 1 January 2023	5,841,710	53,232	38,988	5,933,930
Transfer to Stage 1	-	-	-	-
Transfer to Stage 2	(28,564)	28,564	-	-
Transfer to Stage 3	-	-	-	-
Net change in exposures	1,738,079	(1,559)	985	1,737,505
Write-offs	-	-	(39,973)	(39,973)
	<hr/>	<hr/>	<hr/>	<hr/>
As at 31 December 2023	<u>7,551,225</u>	<u>80,237</u>	<u>-</u>	<u>7,631,462</u>

The management considers the loss allowance of credit commitments is insignificant. Cash and amounts due from banks and other financial institutions and other assets are classified in Stage 1 with no stage transition during the year.

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(All amounts in Hong Kong dollar thousands unless otherwise stated)

3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(ii) Liquidity risk

Management of liquidity risk

Liquidity risk is the risk that the Bank cannot meet its financial obligations when they fall due without incurring significant loss. This may be caused by market disruption or liquidity event whereby the Bank is unable to liquidate assets or to obtain funding to meet its liquidity needs. Liquidity risk arises from various areas including deposits withdrawal either on demand or at contractual maturity.

The Bank aims to maintain a diversified and stable funding sources with an appropriate mix of liabilities including customer deposits. Appropriate amount of high-quality liquid assets is held in order to obtain funding and the sources of liquefiable assets is diversified in accordance with the Investment Management Policy (previously known as Debt Investment Securities Policy) to avoid concentration on assets with similar natures. The Bank seeks to maintain a diversified and stable source of funding to avoid over-reliance on a funding category or a small group of fund providers through setting up monitoring on funding concentration and setting up appropriate funding strategy and structure in the budgeting process.

The Bank has formulated Liquidity Risk Management policy that outlines the liquidity risk management framework according to the requirements of HKMA's Supervisory Policy Manuals ("SPM") "Regulatory Framework for Supervision of Liquidity Risk (LM1)" and "Sound Systems and Controls for Liquidity Risk Management (LM2)". The purpose of the policy is to ensure sufficient cash flows to meet all financial obligation and to comply with regulatory requirement.

The Bank has established a governance framework to oversee the overall liquidity risk. The board of directors is ultimately responsible for ensuring an effective liquidity risk management framework. The EXCO is delegated by the board of directors to provide guidance on the Bank's liquidity risk related activities and reviewing the liquidity risk profile and risk appetite of the Bank. A management committee namely ALCO is set up under the EXCO and is responsible for reviewing relevant liquidity reports regularly, reviewing material changes to liquidity risk models and model assumptions, overseeing the development and maintenance of Contingency Funding Plan ("CFP") and reviewing liquidity risk management controls such as limits and indicators in light of liquidity risk appetite of the Bank on a regular basis.

Different functional departments work closely to implement liquidity risk management controls, to monitor the liquidity position of the Bank and to comply with regulatory requirement. Treasury is responsible for liquidity management but not limited to:

- Manage liquidity risk management including intraday liquidity and implement liquidity risk; management strategies;
- Manage and control the funding in different currencies;
- Advise ALCO on latest market movement and expectation related to liquidity;
- Propose funding strategy and structure in the budget process for ALCO endorsement and approval; and
- Defining and implementing funds transfer pricing ("FTP") across all lines of business.

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(All amounts in Hong Kong dollar thousands unless otherwise stated)

3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(ii) Liquidity risk (Continued)

Management of liquidity risk (Continued)

Finance Department is responsible for coordinating the liquidity risk disclosure process, measuring and monitoring liquidity risk and advising ALCO in establishing limits and indicator, liquidity risk reporting for senior management review and compiling regulatory reports of liquidity position of the Bank.

The Bank has established a set of liquidity risk management limits and indicators to identify, assess, monitor and control liquidity risk, along with ongoing monitoring processes based on regulatory requirements and risk appetite. The Bank has also set up policies to govern such liquidity risk limits and indicators under regulatory requirements. The liquidity risk limits include statutory limits and internal risk limits and these limits are reviewed and approved by ALCO.

The Bank applies cash flow analysis to assess the adequacy of the Bank's liquidity position under both normal and stress scenarios. The Bank seeks to maintain sufficient liquidity to cover the project cash outflow under various stress scenarios.

In case of any breaches to the statutory limits and internal risk limits, different authorized parties in the governance framework including ALCO, EXCO and the board of directors if necessary, will be informed and remedial action will be executed.

The intraday cash inflows and outflows are continuously being monitored during business day to ensure payment obligation can be met at all time. The Bank holds cash and other eligible securities as intra liquidity reserve.

The Bank has established a CFP which details clear strategies to identify the occurrence of a liquidity event and the operational procedures for addressing emergency funding situation so that the impact of such adverse situation to the Bank is minimized. The CFP is reviewed and approved by the ALCO and revised upon changing business and market conditions. The details of the implementation of the plan is documented including the procedures, action plans to estimate the potential funding capacity need and responsibilities of relevant parties. The plan sets out the deployable funding sources, funding measures, potential step to meet critical payment, operational procedures and the estimated time to monetarize assets.

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(ii) Liquidity risk (Continued)

Management of liquidity risk (Continued)

Maturities of financial liabilities

The tables below analyze the Bank's financial liabilities into relevant maturity groupings based on their remaining contractual maturities.

Remaining contractual maturities of financial liabilities	On demand or less than 6 months	One year or less but more than 6 months	More than one year	Total contractual cash flows	Carrying amount
At 31 December 2023					
Deposit from customers	11,643,603	87,572	-	11,731,175	11,695,320
Other accounts and accruals	262,542	-	-	262,542	262,542
Lease liabilities	508	508	1,863	2,879	2,830
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
Total	11,906,653	88,080	1,863	11,996,596	11,960,692
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>
At 31 December 2022					
Deposit from customers	8,690,786	537,606	-	9,228,392	9,171,742
Other accounts and accruals	243,613	-	-	243,613	243,613
Lease liabilities	2,011	508	2,880	5,399	5,308
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
Total	8,936,410	538,114	2,880	9,477,404	9,420,663
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(iii) Market risk

Market risk is the risk of valuation loss or reduction in expected earnings stemming from adverse fluctuations in exchange rates, interest rates, credit spread, implied volatility and cross-currency basis spreads. The risk can exist in both non-trading and trading activities. Currently, the Bank does not involve in trading book business and market risk predominantly arises from the Bank's treasury activities. The major types of market risk come into three forms, interest rate risk, currency risk and price risk, and the risk mainly comes from the Bank's debt securities portfolio held as investment and/or liquidity management.

The Bank has formulated Market Risk Management Policy and Investment Management Policy (previously known as Debt Investment Securities Policy) that outlines the governance structure and measurements and controls of market risk in the Bank.

The policy details a clear strategy to manage different types of market risk that the Bank is exposed to. A market risk framework for different types of risk is established to clearly define risk profiles to ensure it is consistent with the overall risk appetite. Risk limits are developed and reviewed, at least annually and monitored by the Risk Management Department in conjunction with the Treasury Department. Price risk in transactions and open positions is monitored by the risk limits established.

The board of directors is ultimately responsible for ensuring an appropriate organization structure is in place for managing market risk. Market risk oversight rests with the Risk Management Department which in turn reports to the RMC.

The Bank timely identifies, measures, monitors and controls the market risk of the Bank. All transactions are captured for market risk measurements. Reports regarding market risk limits are produced and reviewed regularly.

(a) Foreign exchange risk

The Bank is exposed to foreign exchange risk, primarily United States dollar ("USD") and Renminbi ("RMB"). The Bank's exposure to foreign currency risk at the end of the reporting period was as follows:

	31 December 2023		31 December 2022	
	RMB HK\$'000	USD HK\$'000	RMB HK\$'000	USD HK\$'000
Assets				
Cash and balances with banks	44,188	54,815	63,800	111,497
Placements with and advances to banks	128,876	-	33,606	-
Loans and advances to customers	-	48,666	-	12,825
Investment securities measured at FVOCI	22,571	5,699,346	69,537	4,458,826
Other assets	1,218	95,992	450	81,167
Liabilities				
Deposits from customers	194,767	857,654	167,390	209,804
Other accounts and accruals	2,825	11,972	2,206	4,914

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(iii) Market risk (Continued)

(a) Foreign exchange risk (Continued)

Sensitivity

The Bank's functional currency is Hong Kong dollars ("HKD"). The Bank is exposed to foreign currency risk through certain transactions that are predominately denominated in USD. As the HKD is pegged to the USD, the Bank considers the risk of movements in exchange rates between the HKD and the USD to be mostly within 1% and the net impact to loss before tax and equity would be +-HK\$50,292,000.

The Bank is exposed to RMB and no sensitivity analysis is prepared as the management considered that the effect is insignificant due to the insignificant net position.

(b) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Bank's financial assets and liabilities exposed to interest rate risk primarily are cash and amounts due from banks and other financial institutions, loans and advances to customers, investment securities measured at FVOCI and deposits from customers.

The below assumed changes in interest rates are considered to be reasonably possible based on of current market conditions and represent management's assessment of a reasonably possible change in interest rate over the next twelve-month period.

Sensitivity

As at 31 December 2023 and 2022, if the interest rates of the Bank's interest rate sensitive assets and liabilities had been increased/decreased by 50 basis points at the end of the year with the assumption that the fair value of variable rate and managed rate assets and liabilities are not impacted by the interest rate change and all other variables were held constant, the associated effects driven by the interest rate sensitive assets and liabilities from these changes on the Bank's loss before income tax and equity are approximately:

Years end	Interest rate	(Increase)/ Decrease in loss before tax	Increase/ (Decrease) on equity
31 December 2023	+50 basis point	23,978	(13,390)
	-50 basis point	(23,978)	13,390
31 December 2022	+50 basis point	13,499	(14,346)
	-50 basis point	(13,499)	14,346

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(iv) Fair value estimation

The following tables present the carrying value of the Bank's financial assets and financial liabilities recognized at fair value on a recurring basis, classified according to the fair value hierarchy.

At 31 December 2023	Level 2	Total
Investment securities measured at FVOCI		
- Debt securities	7,473,496	7,473,496
	<u>7,473,496</u>	<u>7,473,496</u>
At 31 December 2022		
Investment securities measured at FVOCI		
- Debt securities	5,569,008	5,569,008
	<u>5,569,008</u>	<u>5,569,008</u>

There were no significant transfers of financial assets or liabilities between different levels of fair value hierarchy classifications.

Level 1: The fair value of financial instruments traded in active markets (such as publicly traded derivatives, and equity securities) is based on quoted market prices at the end of the reporting period. The quoted market price used for financial assets held by the Bank is the current bid price. These instruments are included in level 1. Independent price verification is performed by Risk Management Department.

Level 2: The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined using valuation techniques which maximize the use of observable market data and rely as little as possible on entity-specific estimates. If all significant inputs required to fair value an instrument are observable, the instrument is included in level 2.

Level 3: If one or more of the significant inputs is not based on observable market data, the instrument is included in level 3.

For financial assets and financial liabilities not carried at fair value on the financial statements, the Bank has ascertained that their fair values were the reasonable approximation of the carrying amounts at year end due to short-term nature or repricing of variable rate instruments.

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3. Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(v) **Financial instruments by category**

The Bank's financial instruments include the following:

	2023	2022
Financial assets at AC		
- Cash and balances with banks	827,707	862,372
- Placements with and advances to banks	128,862	134,272
- Loans and advances to customers	5,318,601	4,880,747
- Other assets	126,088	100,157
Financial assets at FVOCI		
- Investment securities measured at FVOCI	7,473,496	5,569,008
	<u>13,874,754</u>	<u>11,546,556</u>
Financial liabilities at AC		
- Deposits from customers	11,695,320	9,171,742
- Other accounts and accruals	265,372	248,921
	<u>11,960,692</u>	<u>9,420,663</u>

3.2 Capital management

The Bank established the Capital Management Policy that outlines the governance structure and the capital management framework according to HKMA's SPM on "Overview of Capital Adequacy Regime for Locally Incorporated Authorized Institutions" ("CA-G-1") and "Supervisory Review Process" ("CA-G-5"). The objective of policy is to maintain a strong capital position to support the Bank's business strategy and serve as a buffer to absorb losses.

The Bank implements a hierarchy of authorities to manage the capital position. The board of directors oversees the effectiveness of the Bank's capital framework and ensures an appropriate organization structure for capital management.

Treasury Department coordinates with the Asset and Liability Management ("ALM") team from Finance Department to implement the capital management strategy. Treasury Department is responsible for maintaining sufficient capital level which complies with the Capital Adequacy Ratio ("CAR") while retaining flexibility to take advantage of future investment opportunities. ALM team is responsible for monitoring CAR and different capital limits, including common equity tier 1 ratio, tier 1 capital ratio, total capital ratio and leverage ratio and performing independent assessment on the Bank's capital management activities and monitoring capital position. Finance department is responsible for reporting the limits utilization and any limit breaches to senior management. Finance Department and Treasury Department report to ALCO in relation to the monitoring of capital management.

The Bank defines a clear framework to assess and monitor the adequacy of the internal capital level, the Bank meets these objectives through the establishment of internal minimum capital requirements and a strong capital management governance framework.

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4. Critical estimates and judgements

The preparation of financial information requires the use of accounting estimates which, by definition, will seldom equal the actual results. Management also needs to exercise judgement in applying the Bank's accounting policies.

Estimates and judgements are continually evaluated. They are based on historical experience and other factors, including expectations of future events that may have a financial impact on the Bank and that are believed to be reasonable under the circumstances.

Impairment of financial assets

The loss allowances for financial assets are based on assumptions about risk of default and expected loss rates. The Bank uses judgement in making these assumptions and selecting the inputs to the impairment calculation, based on the existing market conditions as well as forward-looking estimates at the end of each reporting period. Details of the key assumptions and inputs used are disclosed in note 3.

Incentives

As disclosed in note 2.5, the Bank has reward programs on its debit card to provide incentives to cardholders as promotion purpose. Management judgment is required to determine the customers in the Bank's debit card business. Some of the factors are considered by management in making the judgement, including but not limited to the operational model of debit card business, effective contracts with relevant parties and design of the incentive program.

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5. Net interest income

(a) Interest income

	Year ended 31 December 2023	Year ended 31 December 2022
Interest income arising from:		
- financial assets measured at AC	326,617	140,862
- financial assets measured at FVOCI	232,630	135,538
	<u>559,247</u>	<u>276,400</u>

(b) Interest expense

	Year ended 31 December 2023	Year ended 31 December 2022
Interest expense arising from:		
- financial liabilities measured at AC	296,853	84,128
- lease liabilities (note 11)	87	18
	<u>296,940</u>	<u>84,146</u>

6. Net fee and commission income

	Year ended 31 December 2023	Year ended 31 December 2022
Cards	115,954	116,569
Loan	6,907	8,700
Agency services	12,856	8,994
Others	5,610	3,768
	<u>141,327</u>	<u>138,031</u>
Fee and commission income	141,327	138,031
Less: fee and commission expense		
- processing and handling fee	(55,853)	(56,391)
	<u>85,474</u>	<u>81,640</u>

7. Net gain/(loss) from other financial instruments

	Year ended 31 December 2023	Year ended 31 December 2022
Net gain/(loss) from disposal of investment securities at FVOCI	469	(5,175)
Exchange gain/(loss)	13,242	(18,139)
	<u>13,711</u>	<u>(23,314)</u>

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8. Operating expenses

	Year ended 31 December 2023	Year ended 31 December 2022
Employee benefit expense (note 9)	427,147	358,186
Advertising and promotion expense	68,198	178,375
Software and IT equipment	61,335	57,788
Legal and professional fees	19,882	32,412
Rental expense	17,209	19,532
Service fee	9,790	13,723
Depreciation and amortization expense	19,260	11,812
Auditors' remuneration	3,460	2,615
Administrative expenses and others	27,900	30,992
	<u>654,181</u>	<u>705,435</u>

9. Employee benefit expense (including director's emolument)

	Year ended 31 December 2023	Year ended 31 December 2022
Salaries, staff welfare and insurance cost	407,414	342,800
Pension costs – defined contribution plans	3,099	2,685
Share-based payments	16,634	12,701
	<u>427,147</u>	<u>358,186</u>

10. Income tax

Hong Kong profits tax has been provided at the effective rate of 16.5% (2022: 16.5%) on the estimated assessable profits arising in Hong Kong during the year.

(a) Income tax expense

	Year ended 31 December 2023	Year ended 31 December 2022
Total current tax expense	<u>-</u>	<u>-</u>

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10. Income tax (Continued)

(b) Numerical reconciliation of income tax expense to prima facie tax payable

	Year ended 31 December 2023	Year ended 31 December 2022
Loss before income tax	(399,076)	(498,569)
Tax at the Hong Kong tax rates of 16.5%	(65,847)	(82,264)
Income not subject to tax	(5,428)	(3,304)
Expense not deductible for tax purpose	12,848	4,054
Unused tax losses for which no deferred tax asset was recognised	58,427	81,514
	<u> </u>	<u> </u>
Income tax expense	<u> </u>	<u> </u>

(c) Deferred income tax

The movement in net deferred income tax liabilities/(assets) for each of the years are as follow:

	Accelerated tax depreciation/ amortisation	Tax losses	Provision	Total
As at 1 January 2022	2,503	-	(2,503)	-
Charged/(credited) to statements of comprehensive income	1,229	-	(1,229)	-
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
As at 31 December 2022 and 1 January 2023	3,732	-	(3,732)	-
Charged/(credited) to statements of comprehensive income	895	-	(895)	-
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
As at 31 December 2023	<u> </u>	<u> </u>	<u> </u>	<u> </u>

As at 31 December 2023 and 2022, the Bank had estimated unused tax losses of approximately HK\$1,893,308,596 and HK\$1,539,220,651 respectively available for offset against future profits. The unused tax losses can be carried forward and all tax losses do not expire under current tax legislation. No deferred tax assets have been recognised in respect of such losses due to unpredictability of future profit streams.

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11. Leases

This note provides information for leases where the Bank is a lessee.

(i) *Amounts recognized in the statement of financial position*

The statement of financial position shows the following amounts relating to leases:

	2023	2022
Right-of-use assets		
- Building	3,872	6,048
- Equipment	-	694
	<u>3,872</u>	<u>6,742</u>
	2023	2022
Lease liabilities		
- Current	988	2,479
- Non-current	1,842	2,829
	<u>2,830</u>	<u>5,308</u>

(ii) *Amounts recognized in the statement of comprehensive income*

The statement of comprehensive income shows the following amounts relating to leases:

	Year ended 31 December 2023	Year ended 31 December 2022
Depreciation charge of right-of-use assets	3,559	1,975
Interest expense (note (5b))	87	18

(iii) *Supplementary information*

	Year ended 31 December 2023	Year ended 31 December 2022
Additions to the right-of-use assets	689	6,970
Total cash outflow for leases	3,254	2,144

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12. Cash and balances with banks

	2023	2022
Cash on hand	95	65
Balances with central bank	713,637	656,078
Balances with other banks	113,976	206,230
Less: expected credit loss allowances – stage 1	(1)	(1)
	<u>827,707</u>	<u>862,372</u>

As at 31 December 2023 and 2022, there were no impaired, overdue or rescheduled balances with bank.

13. Placements with and advances to banks

	2023	2022
Placements with and advances to banks maturing within one month	128,876	134,273
Less: expected credit loss allowances – stage 1	(14)	(1)
	<u>128,862</u>	<u>134,272</u>

As at 31 December 2023 and 2022, there were no impaired, overdue or rescheduled placements with and advances to banks.

14. Loans and advances to customers

	2023	2022
Gross loans and advances to customers	5,430,325	4,927,796
Less: expected credit loss allowances		
- Stage 1	(56,694)	(35,383)
- Stage 2	(12,101)	(5,078)
- Stage 3	(42,929)	(6,588)
	<u>5,318,601</u>	<u>4,880,747</u>

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15. Investment securities measured at FVOCI

	2023	2022
Debt securities	<u>7,473,496</u>	<u>5,569,008</u>
	2023	2022
Type of issuer		
- Sovereign	1,012,818	-
- Banks and other financial institutions	4,706,001	3,178,055
- Corporates	<u>1,754,677</u>	<u>2,390,953</u>
	<u>7,473,496</u>	<u>5,569,008</u>

16. Intangible assets

	Software	Total
Cost		
At 1 January 2022	22,892	22,892
Additions	38,732	38,732
Exchange differences	106	106
	<u>61,730</u>	<u>61,730</u>
At 31 December 2022 and 1 January 2023	61,730	61,730
Additions	8,598	8,598
Exchange differences	(18)	(18)
	<u>70,310</u>	<u>70,310</u>
At 31 December 2023	70,310	70,310
Accumulated amortization		
At 1 January 2022	9,042	9,042
Amortization for the year	7,146	7,146
Exchange differences	243	243
	<u>16,431</u>	<u>16,431</u>
At 31 December 2022 and 1 January 2023	16,431	16,431
Amortization for the year	14,802	14,802
Exchange differences	3	3
	<u>31,236</u>	<u>31,236</u>
At 31 December 2023	31,236	31,236
Net book value at 31 December 2022	<u>45,299</u>	<u>45,299</u>
Net book value at 31 December 2023	<u>39,074</u>	<u>39,074</u>

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17. Fixed assets

	Equipment	Total
Cost		
At 1 January 2022	5,541	5,541
Additions	858	858
	<hr/>	<hr/>
At 31 December 2022 and 1 January 2023	6,399	6,399
Additions	79	79
	<hr/>	<hr/>
At 31 December 2023	6,478	6,478
	<hr/>	<hr/>
Accumulated depreciation		
At 1 January 2022	2,456	2,456
Depreciation for the year	2,691	2,691
	<hr/>	<hr/>
At 31 December 2022 and 1 January 2023	5,147	5,147
Depreciation for the year	899	899
	<hr/>	<hr/>
At 31 December 2023	6,046	6,046
	<hr/>	<hr/>
Net book value at 31 December 2022	1,252	1,252
	<hr/>	<hr/>
Net book value at 31 December 2023	432	432
	<hr/>	<hr/>

18. Other assets

	2023	2022
Deposits	92,080	79,799
Receivable from card business	20,270	14,487
Prepaid expenses	11,925	8,149
Right-of-use assets (note 11)	3,872	6,742
Others	13,738	5,871
	<hr/>	<hr/>
	141,885	115,048
	<hr/>	<hr/>

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19. Deposits from customers

	2023	2022
Saving deposits	3,607,482	2,863,403
Time deposits	8,087,838	6,308,339
	<u>11,695,320</u>	<u>9,171,742</u>

20. Other accounts and accruals

	2023	2022
Accounts payable and accruals	168,317	133,060
Amounts due to related parties (note 25)	72,477	88,328
Deferred revenue	16,256	25,325
Accruals for employee benefit	23,249	23,725
Lease liabilities (note 11)	2,830	5,308
Others	1,467	1,479
	<u>284,596</u>	<u>277,225</u>

21. Share capital

	2023 Shares	2022 Shares	2023	2022
Ordinary shares				
Fully Paid	4,100,000,000	4,100,000,000	4,100,000	4,100,000

On 25 May 2022, 20 September and 30 December 2022, the Bank respectively issued 250,000,000 ordinary shares, 200,000,000 ordinary shares and 50,000,000 ordinary shares to the parent company at HK\$250,000,000, HK\$200,000,000 and HK\$50,000,000 for cash. All the cash was paid up on the date of issuance.

No ordinary shares were issued during 2023.

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22. Share-based payments

(i) Share Option Schemes

The shareholders of the ZA Online has approved and adopted the ZhongAn Technologies International Group Limited (“ZATI”) share option scheme (the “Scheme”) at the extraordinary general meeting held on 29 December 2020. The purpose for the Scheme is to enable ZATI, the intermediate holding company, to grant share options to its eligible participants, including eligible participants of the Bank (the “Bank Grantees”), to acquire shares of ZATI.

The board of directors of ZATI (or through its administration committee) shall determine the exercise price for the share option with reference to the respective net asset value per underlying share of ZATI at the time of grant.

The vesting of the share options under the Scheme shall be subject to the fulfilment of all terms and conditions for the grant of such share options made to the Bank Grantees as set out in the relevant offer letter provided that (a) the grantee shall be continuously employed through the vesting date, the awarded share options shall vest in accordance with the vesting schedule as stipulated in the relevant offer lettered in the offer letter; and (b) other conditions (if any) as determined by the respective board of directors of ZATI in its absolute discretion.

The maximum aggregate number of shares of ZATI which may be issued upon exercise of all outstanding share options granted and yet to be exercised under the Scheme must not exceed 10% of the issued share capital of ZATI (“Scheme Limit”) as at the adoption date of the Scheme, subject to adjustment in the event of specified capitalization events from time to time as described in the Scheme.

The Scheme shall be valid and effective for a period of 10 years commencing from the adoption date.

On 31 December 2020, ZATI granted 23,400,900 share options to the Bank Grantees (the “first batch”). On 25 June 2021, ZATI granted 4,300,000 share options to the Bank Grantees (the “second batch”). On 20 January 2022, ZATI granted 2,500,000 share options to the Bank Grantees (the “third batch”). On 1 June 2023, ZATI granted 3,900,000 share options to the Bank Grantees (the “forth batch”).

Set out below are summaries of options granted under the plan and outstanding:

	2023		2022	
	Average exercise price per share option HK\$	Number of options	Average exercise price per share option HK\$	Number of options
As at 1 January	1.36	20,364,000	1.34	22,322,250
Granted during the year	1.50	3,900,000	1.50	2,500,000
Exercised during the year	-	-	1.34	(375,000)
Forfeited during the year	1.37	(7,382,000)	1.34	(4,083,250)
As at 31 December	1.39	16,882,000	1.36	20,364,000
Vested and exercisable as at 31 December	1.35	9,373,388	1.34	9,659,775

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22. Share-based payments (Continued)

(i) Share Option Schemes (Continued)

Share options outstanding at the end of the year have the following expiry date and exercise prices:

Grant Date	Expiry Date	Exercise Price	31 December 2023	31 December 2022
31 December 2020	30 December 2030	HK\$1.34	10,282,000	16,264,000
25 June 2021	24 June 2031	HK\$1.34	1,600,000	1,600,000
20 January 2022	19 January 2032	HK\$1.50	2,500,000	2,500,000
1 June 2023	1 June 2033	HK\$1.50	2,500,000	-
			16,882,000	20,364,000

Weighted average remaining contractual life of options outstanding at end of year	7.57 years	8.18 years
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Based on fair value of the underlying shares, the directors have used binominal pricing model to determine the fair value of the share options as of the grant date.

First batch key assumptions are set out as below:

Dividend rate (%)	0.00
Volatility (%)	26.81
Risk-free interest rate (%)	0.54
Life of options (in years)	10
Estimate share price at grant date according to sum-of-the-parts approach (in HKD)	0.71
Exercise price (in HKD)	1.34

Second batch key assumptions are set out as below:

Dividend rate (%)	0.00
Volatility (%)	39.62
Risk-free interest rate (%)	1.12
Life of options (in years)	10
Estimate share price at grant date according to sum-of-the-parts approach (in HKD)	1.53
Exercise price (in HKD)	1.34

Third batch key assumptions are set out as below:

Dividend rate (%)	0.00
Volatility (%)	42.57
Risk-free interest rate (%)	1.62
Life of options (in years)	10
Estimate share price at grant date according to sum-of-the-parts approach (in HKD)	4.56
Exercise price (in HKD)	1.5

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22. Share-based payments (Continued)

(i) Share Option Schemes (Continued)

Forth batch key assumptions are set out as below:

Dividend rate (%)	0.00
Volatility (%)	44.9
Risk-free interest rate (%)	3.4
Life of options (in years)	10
Estimate share price at grant date according to sum-of-the-parts approach (in HKD)	4.40
Exercise price (in HKD)	1.5

(ii) Restricted Share Unit Schemes

On 15 September 2020, ZATI adopted a restricted share unit scheme (the "RSU Scheme"). The purpose for the RSU scheme is to enable ZATI to grant restricted shares units ("RSUs") of ZATI to its eligible participants, including the eligible participants of the Bank (the "Bank RSU Grantees"), as incentives or rewards for their contribution to the growth of the ZATI and to provide ZATI with a more flexible means to reward, remunerate, compensate and/or provide benefits to the eligible participants of the RSU Scheme.

The board of directors of ZATI (or through its administration committee) shall determine the consideration of the RSUs ("Grant Price") at the time of grant.

The vesting of the RSUs under the RSU Scheme shall be subject to the fulfillment of all terms and conditions for the grant of such RSUs made to the Bank RSU Grantees as set out in the relevant offer letter provided that (a) the grantee shall be continuously employed through the vesting date, the awarded RSUs shall vest in accordance with the vesting schedule as stipulated in the relevant offer letter; and (b) other conditions (if any) as determined by the respective board of directors of ZATI in its absolute discretion.

The maximum aggregate number of shares of the ZATI which may be allotted and issued under the RSU Scheme must not exceed 10% of the issued share capital of ZATI ("RSU Scheme Limit") as at the adoption date of the RSU Scheme, subject to adjustment in the event of specified capitalization events from time to time as described in the RSU Scheme.

The RSU Scheme shall be valid and effective for a period of 10 years commencing from the adoption date of the RSU Scheme.

On 8 April 2022, ZATI granted 10,700,000 RSUs to the Bank RSU Grantees ("First Batch RSU"). On 1 December 2022, ZATI granted 3,550,000 RSUs to the Bank RSU Grantees ("Second Batch RSU").

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22. Share-based payments (Continued)

(ii) Restricted Share Unit Schemes (Continued)

Set out below are summaries of RSUs granted under the plan and outstanding:

	Average exercise price per RSUs HK\$	Number of RSUs
As at 1 January 2022	-	-
Granted during the year	1.50	14,250,000
Exercised during the year	-	-
Forfeited during the year	1.50	(950,000)
		<hr/>
As at 31 December 2022 and 1 January 2023	1.50	13,300,000
Granted during the year	-	-
Exercised during the year	-	-
Forfeited during the year	1.50	(1,600,000)
		<hr/>
As at 31 December 2023	1.50	11,700,000
		<hr/> <hr/>
Vested and exercisable as at 31 December 2023	1.50	2,925,000
Vested and exercisable as at 31 December 2022	-	-

RSUs outstanding at the end of the year have the following expiry date and exercise prices:

Grant Date	Expiry Date	Exercise Price	31 December 2023	31 December 2022
8 April 2022	7 April 2032	HK\$1.50	8,250,000	9,750,000
1 December 2022	30 November 2032	HK\$1.50	3,450,000	3,550,000
			<hr/>	<hr/>
			11,700,000	13,300,000
			<hr/> <hr/>	<hr/> <hr/>
Weighted average remaining contractual life of RSUs outstanding at end of year			8.47 years	9.45 years

Based on fair value of the underlying shares, the directors have used binominal pricing model to determine the fair value of the RSUs as of the grant date.

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22. Share-based payments (Continued)

(ii) Restricted Share Unit Schemes (Continued)

First Batch RSU key assumptions are set out as below:

Dividend rate (%)	0.00
Volatility (%)	41.63
Risk-free interest rate (%)	2.48
Life of RSUs (in years)	10
Estimate RSU price at grant date according to sum-of-the-parts approach (in HKD)	3.29
Grant price (in HKD)	1.5

Second Batch RSU key assumptions are set out as below:

Dividend rate (%)	0.00
Volatility (%)	43.32
Risk-free interest rate (%)	3.45
Life of RSUs (in years)	10
Estimate RSU price at grant date according to sum-of-the-parts approach (in HKD)	5.15
Grant price (in HKD)	1.5

The total expenses recognized in the statement of comprehensive income for share option schemes and restricted share unit schemes is disclosed in note 9.

23. Commitments

	2023	2022
Credit commitments with an original maturity of:		
- 1 year or over	-	14,500
- unconditionally cancellable	386,518	330,694
	<u>386,518</u>	<u>345,194</u>

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24. Note to cash flow statement

(i) Non-cash investing activities

Non-cash investing activities disclosed in other note is:

- *Acquisition of right-of-use assets – note 11*

(ii) Net debt reconciliation

This section sets out an analysis of net debt and the movements in net debt for each of the periods presented.

	2023	2022
Cash and cash equivalents	956,584	946,068
Lease liabilities	(2,830)	(5,308)
Net debt	<u>953,754</u>	<u>940,760</u>
Cash and cash equivalents	956,584	946,068
Gross debt – fixed interest rate	(2,830)	(5,308)
Net debt	<u>953,754</u>	<u>940,760</u>

	Lease	Cash and cash equivalents	Total
Net debt as at 1 January 2022	(1,964)	1,769,416	1,767,452
Cash flows	2,144	(811,708)	(809,564)
Acquisition – leases	(5,470)	-	(5,470)
Interest expense (note 5(b))	(18)	-	(18)
Foreign exchange adjustments	-	(11,640)	(11,640)
Net debt as at 31 December 2022 and 1 January 2023	<u>(5,308)</u>	<u>946,068</u>	<u>940,760</u>
Cash flows	3,254	9,969	13,223
Acquisition – leases	(689)	-	(689)
Interest expense (note 5(b))	(87)	-	(87)
Foreign exchange adjustments	-	547	547
Net debt as at 31 December 2023	<u>(2,830)</u>	<u>956,584</u>	<u>953,754</u>

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25. Related party transactions

Save as disclosed elsewhere in the financial statements, the Bank had the following transactions with its related parties during the year.

(i) Key management personnel compensation

Transactions with key management personnel have been disclosed below.

	Year ended 31 December 2023	Year ended 31 December 2022
Short-term employee benefits	30,215	32,069
Share-based payments	12,467	9,670
Deferred bonus	428	749
	<u>43,110</u>	<u>42,488</u>

(ii) Transactions with related parties

ZA Online

	Year ended 31 December 2023	Year ended 31 December 2022
Interest income	<u>732</u>	<u>731</u>

The Bank has recharge arrangement with ZATI under which the Bank used and occupied certain resources of ZATI, such as designated employees and office premises, to support its business and operation. In connection with this recharge arrangement, ZATI recharged the Bank for the operating expenses attributable to the Bank monthly on a cost basis.

During the year ended 31 December 2023, ZATI has allocated and recharged operating expenses including staff and rental expenses of HK\$327,354,574 (2022:HK\$261,660,298) to the Bank.

	Year ended 31 December 2023	Year ended 31 December 2022
Operating expenses	(327,355)	(261,660)
Interest expense	(1)	(2)
	<u>(327,356)</u>	<u>(261,662)</u>

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25. Related party transactions (Continued)

(ii) Transactions with related parties (Continued)

Fellow subsidiaries	Year ended 31 December 2023	Year ended 31 December 2022
Operating expenses	(41,750)	(95,572)
Fee and commission income	1,903	3,265
	<u>(39,847)</u>	<u>(92,307)</u>
Other related parties	Year ended 31 December 2023	Year ended 31 December 2022
Interest expense	(3,554)	(158)
Operating expenses	(500)	(500)
	<u>(4,054)</u>	<u>(658)</u>

During the year ended 31 December 2023 and 2022, the Bank has the following transactions with the key management personnel.

	Year ended 31 December 2023	Year ended 31 December 2022
Interest income	28	46
Interest expense	(3,418)	(1,083)
Operating expenses	(48)	(1)
Fee and commission income	28	10
	<u>(3,410)</u>	<u>(1,028)</u>

(iii) Balances with related parties

As at 31 December 2023 and 2022, the Bank has the following balances with related parties.

ZA Online	2023	2022
Debt securities measured at FVOCI	<u>22,007</u>	<u>20,212</u>
ZATI	2023	2022
Deposits from customers	(3,494)	(5,826)
Other accounts and accruals	(48,114)	(70,890)
	<u>(51,608)</u>	<u>(76,716)</u>

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25. Related party transactions (Continued)

(iii) Balances with related parties (Continued)

Fellow subsidiaries	2023	2022
Deposits from customers	(3,644)	(8,001)
Other accounts and accruals	(13,209)	(12,087)
Other assets	1,903	248
	<u>(14,950)</u>	<u>(19,840)</u>
	<u><u>(14,950)</u></u>	<u><u>(19,840)</u></u>
Other related parties	2023	2022
Deposits from customers	(122,620)	(73,738)
Interest payable	(222)	(141)
Other accounts and accruals	(11,154)	(5,351)
	<u>(133,996)</u>	<u>(79,230)</u>
	<u><u>(133,996)</u></u>	<u><u>(79,230)</u></u>
Key management personnel	2023	2022
Deposits from customers	(143,301)	(131,017)
Interest payable	(890)	(440)
Bonus payable	(6,489)	(7,072)
Loans and advances to customers	1,622	3,008
Interest receivable	1	3
	<u>(149,057)</u>	<u>(135,518)</u>
	<u><u>(149,057)</u></u>	<u><u>(135,518)</u></u>

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26. Benefits and interest of the Directors of the Bank

During the year, except as disclosed below, no other emoluments, retirement benefits, payments or benefits in respect of termination of directors' services were paid or made, directly or indirectly, to the directors of the Bank. No consideration was provided to or receivable by third parties for making available directors' services during the year. There are no loans, quasi-loans or other dealings in favour of the directors, their controlled bodies corporate and connected entities during the year.

No director of the Bank had a material interest, directly or indirectly, in any significant transactions, arrangements and contracts in relation to the Bank's business to which the Bank was or is a party that subsisted at the end of the year or at any time during the year.

Directors' emoluments

The aggregate emoluments paid to or receivable by directors in respect of their services as directors, pursuant to section 383 of the Hong Kong Companies Ordinance (Cap.622) and the Companies (Disclosure of Information about Benefits of Directors) Regulation (Cap.622G) were set out below:

	Year ended 31 December 2023	Year ended 31 December 2022
Directors' fees	2,000	1,658
Salaries and bonus	6,278	6,744
Contribution to retirement benefits schemes	36	30
Other benefits	6,754	1,122
Total	<u>15,068</u>	<u>9,554</u>

27. Dividends

No dividend was paid or proposed for the year ended 31 December 2023 and 31 December 2022.

28. Comparative figures

Certain comparative figures in the financial statements have been reclassified to conform with current year's presentation.

29. Approval of financial statements

The financial statements were approved by the board of directors on 26 March 2024.