

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

FINANCIAL STATEMENTS – 31 DECEMBER 2006

Domiciled in Malaysia.
Registered Office:
2, Leboh Ampang,
50100 Kuala Lumpur

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

CONTENTS

1	Board of Directors
2	Profile of Directors
5	Board Responsibility and Oversight <i>Board of Directors</i> <i>Board Committees</i>
19	Management Reports
20	Internal Audit and Internal Control Activities
21	Risk Management
26	Ratings Statement
27	Directors' Report
36	Directors' Statement
37	Statutory Declaration
38	Report of the Auditors
40	Balance Sheet
41	Income Statement
42	Statement of Changes in Equity
43	Cash Flow Statement
44	Notes to the Financial Statements

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

BOARD OF DIRECTORS

Michael Roger Pearson Smith, *non-executive Chairman*

Dato' Zarir Jal Cama, *Deputy Chairman and Chief Executive Officer*

Ian Douglas Francis Ogilvie, *executive Director and Deputy Chief Executive*

Douglas Jardine Flint, *non-independent non-executive Director*

Dato' Sulaiman bin Sujak, *non-independent non-executive Director*

Dato' Henry Sackville Barlow, *independent non-executive Director*

Datuk Ramli bin Ibrahim, *independent non-executive Director*

Datuk Dr Zainal Aznam bin Mohd Yusof, *independent non-executive Director*

Professor Emeritus Dr Mohamed Ariff bin Abdul Kareem, *independent non-executive Director*

Dato' Zuraidah binti Atan, *independent non-executive Director*

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

PROFILE OF DIRECTORS

Michael Roger Pearson Smith, non-executive Chairman

Age 50. Holds a BSc (Hons) from the London University. Joined HSBC in 1978 and, in 1991, following a number of appointments in the Asia-Pacific and the Middle East, moved to the Planning Department of Midland Bank (now HSBC Bank plc) in the UK. In 1993, appointed as Managing Director International at the bank.

From 1995-1997, he was executive Director and Deputy Chief Executive of Hongkong Bank Malaysia Berhad (now HSBC Bank Malaysia Berhad). In 1997, he was appointed Chief Executive Officer of HSBC Argentina Holdings SA assuming responsibility for the Group's operations in Argentina. He was appointed Chairman there in 2000 and, in the same year, was appointed a Group General Manager.

In March 2003, he returned to the UK as Group General Manager to review and restructure the Group Head Office.

Michael Smith was appointed President and Chief Executive Officer of The Hongkong and Shanghai Banking Corporation Limited and Chairman of HSBC Bank Malaysia Berhad on 1 January 2004. He has also been appointed as the Chairman of Hang Seng Bank Limited effective 22 April 2005.

Dato' Zarir Jal Cama, Deputy Chairman and Chief Executive Officer

Age 59. Dato' Cama went to school at St. Paul's School, Darjeeling and graduated from St. Stephen's College, Delhi University. Joined the HSBC Group in London in 1968. After two years training in the London office, he returned to India and worked in various operational, credit and branch capacities. In 1982, he was posted to the International Corporate Accounts Division in Hong Kong. He returned to India in 1984 to head the Bank's Merchant Banking operations where he was responsible for its business strategy and development. He moved to Saudi British Bank Ltd in 1988 to head the Corporate Bank and was subsequently appointed its Deputy Managing Director. In 1992, he was assigned to Head Office in Hong Kong as Senior Manager Group Corporate Planning and Senior Manager International and went on to become Senior Executive Global Banking Services, HSBC Holdings plc in October 1993 based in the Group's new headquarters in London.

In mid-March 1998, he was transferred back to India as Deputy Chief Executive Officer and was appointed Chief Executive Officer of The Hongkong and Shanghai Banking Corporation in India in October 1999. As Country Head, he was also Chairman of HSBC Securities and Capital Markets India Private Limited and of the Group's Processing Company, HSBC Electronic Data Processing India Private Ltd.

He became a Group General Manager of HSBC Holdings plc in August 2001. Dato' Cama was appointed Deputy Chairman and Chief Executive Officer for HSBC Bank Malaysia Berhad in November 2002 with responsibility for the Malaysian operations.

He is a Council Member of the Association of Banks in Malaysia and is on the General Committee of the Malaysian International Chamber of Commerce and Industry. Dato' Cama is also a member of Rotary Club of Kuala Lumpur DiRaja and an Honorary Member of Rotary Club Damansara. He is also a Trustee of WWF Malaysia and the Aged European Fund.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Profile of Directors (continued)

Ian Douglas Francis Ogilvie, executive Director and Deputy Chief Executive

Age 47. Mr Ogilvie obtained a MA Geography from Cambridge University. He joined the HSBC Group in 1981 as a Research and Planning Analyst and held the position of General Manager, Human Resources of HSBC Bank plc prior to his current appointment as executive Director and Deputy Chief Executive of HSBC Bank Malaysia Berhad.

During his career at HSBC he has held a wide variety of senior posts with the Group.

Douglas Jardine Flint, non-independent non-executive Director

Age 51. Douglas Flint is a Chartered Accountant from the Institute of Chartered Accountants of Scotland and participated in the Programme for Management Development (PMD) from Harvard Business School. Group Finance Director of HSBC Holdings plc. A non-executive Director since 1995. He is the Chairman of the Financial Reporting Council's review of the Turnbull Guidance on Internal Control; and served on The Accounting Standards Board in the UK and the Standards Advisory Council of the International Accounting Standards Board from 2001 to 2004. He was named 'Business Leader of the Year' by the Chartered Institute of Management Accountants in 2003 and best European Chief Financial Officer in the banking category of a survey carried out by Institutional Investor magazine in 2004. He was a former partner of KPMG, UK.

Dato' Sulaiman bin Sujak, non-independent non-executive Director

Age 72. Served as an executive Director and Adviser of HSBC Bank Malaysia Berhad for 15 years, before being appointed a non-executive Director in 2004. He graduated from the Royal Air Force College, Cranwell, England in 1958 and the Royal College of Defence Studies, London in 1973 and had served both with the Royal Air Force and the Royal Malaysian Air Force. He was the first Malaysian to be appointed as the Royal Malaysian Air Force Chief (1967-1976). He served as an Adviser of Bank Negara Malaysia (1977-1983), Commercial Director of Kumpulan Guthrie (1983-1989) and Deputy Chairman of Malaysia Airline System (1977-2001). Currently, he also sits on the board of FACB Industries Incorporated Berhad, Nationwide Express Courier Services Berhad and Cycle & Carriage Bintang Berhad.

Dato' Henry Sackville Barlow, independent non-executive Director

Age 62. He graduated from Eton College and obtained a MA from Cambridge University. He is a former Council Member of the Incorporated Society of Planters and Honorary Secretary of the Heritage Trust of Malaysia. He is a Director of Golden Hope Plantations Berhad and Guthrie Ropel Berhad. He was formerly Joint Managing Director of Highland and Lowlands Para Rubber Co. Ltd., being instrumental in the company's Malaysianisation process in the late 1970s and early 1980s. Dato' Barlow is a Fellow of The Institute of Chartered Accountants, England and Wales, and a keen environmentalist.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Profile of Directors (continued)

Datuk Ramli bin Ibrahim, independent non-executive Director

Age 66. Datuk Ramli is a Chartered Accountant from the Institute of Chartered Accountants of Australia. He is currently non-executive Director of several other public listed and unlisted companies, including MEASAT Global Berhad, Ranhill Berhad and BCT Technology Berhad. He was formerly Senior Partner of KPMG Peat Marwick Malaysia (now known as KPMG Malaysia) and executive Chairman of Kuala Lumpur Options and Financial Futures Exchange Berhad.

Datuk Dr Zainal Aznam bin Mohd Yusof, independent non-executive Director

Age 62. Datuk Dr Zainal holds a Bsc (Econ) from Queen's University, Belfast, Northern Ireland, MA (Development Economics) from University of Leicester, United Kingdom and Ph.D. (Economics) from Oxford University, United Kingdom. He was attached to the Economic Planning Unit of the Prime Minister's Department from 1969 to 1988. During the 1987-1988 academic year, he was a Visiting Scholar at the Harvard Institute for International Development (HIID), Harvard University (Fulbright Scholar). He has also served as a Deputy Executive Director of the Malaysian Institute of Economic Research (MIER) from 1988 to 1990. Prior to that, he was the South East Asia Regional Economist at Kleinwort Benson Research (Malaysia) Sdn Bhd.

From 1990-1994 he was the Adviser in Economics at Bank Negara Malaysia. In January 1998 he was appointed as a Member of the Working Committee of the National Economic Action Council (NEAC). He was a Commissioner of the Securities Commission from 1999 to 2004 and the Deputy Director-General of the Institute of Strategic and International Studies until 2002. Datuk Dr Zainal is a well-known economist in Malaysia.

Professor Emeritus Dr Mohamed Ariff bin Abdul Kareem, independent non-executive Director

Age 66. Prof. Emeritus Dr Mohamed Ariff obtained his B.A. First Class Honours and M.Ec. from the University of Malaya. He completed his Ph.D. program at the University of Lancaster, England in 1971, on a Commonwealth Scholarship.

Prof. Emeritus Dr Mohamed Ariff, a specialist in International Economics, is currently the executive Director of the Malaysian Institute of Economic Research (MIER). Previously he held the Chair of Analytical Economics at the University of Malaya where he had also served as the Dean of the Faculty of Economics and Administration. He was a Board Member of the Inland Revenue Board (IRB) and is a Board Member of National Productivity Centre (NPC) and Social Security Organisation (SOSCO). He had a brief stint in the private sector as the Chief Economist at the United Asian Bank in 1976.

Dato' Zuraidah binti Atan, independent non-executive Director

Age 47. Appointed on 18 October 2004. She is currently a Director and Chairman of the Finance Board of FAMA (Federal Agricultural Marketing Authority) and a Director of Universiti Utara Malaysia, NCB Holdings Berhad and Milux Corporation Berhad (formerly known as TH Hin Corporation Berhad). She was previously President and Chief Executive of Affin Merchant Bank Berhad for four years until September 2003. Prior to that, she served at OCBC Bank (Malaysia) Berhad in various capacities for ten years. A lawyer by training, she obtained her LLB from the University of Buckingham, Britain in 1984. She sits on various State Government Investment Committees, Boards and Advisory Panels such as Melaka State Government Investment Committee and Kedah State Government Insurance Brokers. She is also a member of the Association of Bumiputra Business and Professional Women, Malaysia. Currently she serves as an adviser to the National Cancer Society of Malaysia.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

BOARD RESPONSIBILITY AND OVERSIGHT

BOARD OF DIRECTORS

Composition of the Board

At the date of this report, the Board consists of ten (10) members; comprising two (2) non-independent executive Directors, three (3) non-independent non-executive Directors and five (5) independent non-executive Directors.

The concept of independence adopted by the Board is as defined in paragraph 2.26 of Bank Negara Malaysia's Guidelines on Corporate Governance for Licensed Institutions (Revised BNM/GP1). The key requirements for independent Directors are that they do not have a substantial shareholding interest in the Bank (5% equity interest, directly or indirectly), have not been employed or have an immediate family employed in an executive position in the Bank within the past two (2) years, have not engaged in any transaction worth more than RM1 million with the Bank within the past two (2) years and generally, are independent of management and free from any business or other relationship which could interfere with the exercise of independent judgement or the ability to act in the best interest of the Bank.

There is a clear division of responsibilities at the head of the Bank to ensure a balance of authority and power. The Board is led by Mr Michael Roger Pearson Smith as the non-executive Chairman and the executive management of the Bank is led by Dato' Zarir Jal Cama, the Chief Executive Officer.

Revised BNM/GP1 prescribes a maximum of one (1) executive Director on the Board, preferably the Chief Executive Officer. However, as there are two (2) executive Directors on the Board, that is, the Chief Executive Officer and the Deputy Chief Executive, the Bank has, on 8 December 2005, obtained Bank Negara Malaysia's approval to retain both executive Directors on the Board.

Roles and Responsibilities of the Board

The Board is responsible for the overall corporate governance of the Bank, including its strategic direction, establishing goals for management and monitoring the achievement of these goals. The role and function of the Board are clearly documented in a Shareholder's Mandate.

The Board has a formal schedule of matters reserved to itself for approval, which includes annual plans and performance targets, procedures for monitoring and control of operations, specified senior appointments, acquisitions and disposals above pre-determined thresholds and any substantial changes in the balance sheet management policy.

The Board carries out various functions and responsibilities laid down by Bank Negara Malaysia in guidelines and directives that are issued by Bank Negara Malaysia from time to time.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Board Responsibility and Oversight (continued)

BOARD OF DIRECTORS (continued)

Frequency and Conduct of Board Meetings

The Board ordinarily meets at least four (4) times a year, usually in the month following the closure of each financial quarter. During the financial year, the Board met on five (5) occasions.

However, as Revised BNM/GPI requires the Board to meet preferably on a monthly basis, but in any event, no less than once every two (2) months, the frequency of the Board meetings has been revised to once every two (2) months and the Board will meet six (6) times in 2007.

The Board receives reports on the progress of the Bank's business operations and minutes of meetings of Board Committees for review at each of its meetings. At these meetings, the members also consider a variety of matters including the Bank's financial results, major investment and strategic decisions and corporate governance matters. The Board also receives a number of annual presentations from each key business area, and on any other topic as they request.

The agenda for every Board meeting, together with comprehensive management reports, proposal papers and supporting documents are distributed to the Directors in advance of all Board meetings, to allow time for appropriate review and to enable full discussion at the meetings. All proceedings from the Board meetings are minuted. Minutes of every Board meeting are circulated to all Directors for their perusal prior to confirmation of the minutes at the following Board meeting.

Revised BNM/GPI requires non-executive Directors to have a minimum attendance of at least 75% of all Board meetings.

The attendance of Directors at the Board meetings held in the financial year ended 31 December 2006 was as follows:

Name of members	Independent/ Non-Independent	Attendance and number of meetings
Michael Roger Pearson Smith	Chairman, non-independent non-executive Director	5/5
Dato' Zarir Jal Cama	Deputy Chairman and Chief Executive Officer	5/5
Ian Douglas Francis Ogilvie	Executive Director and Deputy Chief Executive	5/5
Douglas Jardine Flint	Non-independent non-executive Director	5/5
Dato' Sulaiman bin Sujak	Non-independent non-executive Director	5/5
Dato' Henry Sackville Barlow	Independent non-executive Director	4/5
Datuk Ramli bin Ibrahim	Independent non-executive Director	5/5
Datuk Dr Zainal Aznam bin Mohd Yusof	Independent non-executive Director	3/5*
Professor Emeritus Dr Mohamed Ariff bin Abdul Kareem	Independent non-executive Director	4/5
Dato' Zuraidah binti Atan	Independent non-executive Director	5/5

* Datuk Zainal Aznam bin Mohd Yusof did not fulfill the minimum attendance requirement in 2006 due to a late change to the date of the Board meeting in July 2006.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Board Responsibility and Oversight (continued)

BOARD COMMITTEES

The Board has established Board Committees as well as various Management Committees to assist the Board in the running of the Bank. The functions and Terms of Reference of the Board Committees and Management Committees, as well as authority delegated by the Board to these Committees, have been clearly defined by the Board.

The Board Committee and Management Committees in the Bank are as follows:

Board Committees

- Audit Committee
- Risk Management Committee
- Nominating Committee

The Risk Management Committee and Nominating Committee were established in 2006 pursuant to Revised BNM/GP1. Revised BNM/GP1 also requires the Board to establish a Remuneration Committee. However, the Bank has, on 28 April 2006, obtained BNM's exemption from this requirement.

Management Committees

- Executive Committee
- Credit Committee
- Asset and Liability Management Committee
- Human Resource Steering Committee
- IT Steering Committee
- Operational Risk Management Committee
- Property Committee
- Senior Succession Planning Committee

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Board Responsibility and Oversight (continued)

AUDIT COMMITTEE

Membership

The present members of the Audit Committee ('the Committee') comprise:

Datuk Ramli bin Ibrahim (Chairman)
Dato' Sulaiman bin Sujak
Dato' Henry Sackville Barlow
Dato' Zuraidah binti Atan

Meetings

A total of four (4) Audit Committee meetings were held during the financial year. The attendance of the Directors at the Audit Committee meetings held in 2006 was as follows:

Name of members	Independent/ Non-Independent	Attendance and number of meetings
Datuk Ramli bin Ibrahim	Chairman, Independent non-executive Director	4 / 4
Dato' Henry Sackville Barlow	Independent non-executive Director	3 / 4
Dato' Sulaiman bin Sujak	Non-independent non-executive Director	4 / 4
Dato' Zuraidah binti Atan	Independent non-executive Director	2 / 2*

* Dato' Zuraidah binti Atan was appointed as a member of the Audit Committee in April 2006.

Terms of Reference

The Terms of Reference were approved at the meetings of the Audit Committee and Board held on 19 July 2005.

Membership

The Committee shall comprise not less than three independent non-executive Directors.

The appointment to the Committee of members and of the Chairman shall be subject to endorsement by the HSBC Group Audit Committee.

The Board may from time to time appoint additional members to the Committee from among the non-executive directors it has determined to be independent. In the absence of sufficient independent non-executive directors, the Board may appoint individuals from elsewhere in the HSBC Holdings plc Group ('HSBC Group') with no line or functional responsibility for the activities of the Bank or its subsidiaries.

The Chairman of the Committee shall be appointed by the Board following election by the members of the Committee.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Board Responsibility and Oversight (continued)

AUDIT COMMITTEE (continued)

The Committee may invite any director, executive, external auditor or other person to attend any meeting(s) of the Committee as it may from time to time consider desirable to assist the Committee in the attainment of its objective.

Meetings and Quorum

The Committee shall meet with such frequency and at such times as it may determine. It is expected that the Committee shall meet at least four (4) times each year.

The quorum for meetings shall be two (2) Directors.

Objective

The Committee shall be accountable to the Board and shall assist the Board in meeting its responsibilities in ensuring an effective system of internal control and compliance and for meeting its external financial reporting obligations, including its obligations under applicable laws and regulations and shall be directly responsible on behalf of the Board for the selection, oversight and remuneration of the external auditor.

Responsibilities of the Committee

Without limiting the generality of the Committee's objective, the Committee shall have the following responsibilities, powers, authorities and discretion.

1. To monitor the integrity of the financial statements of the Bank, and any formal announcements relating to the Bank's financial performance, reviewing significant financial reporting judgements contained in them. In reviewing the Bank's financial statements before submission to the Board, the Committee shall focus particularly on:
 - (i) any changes in accounting policies and practices;
 - (ii) major judgemental areas;
 - (iii) significant adjustments resulting from audit;
 - (iv) the going concern assumptions and any qualifications;
 - (v) compliance with accounting standards; and
 - (vi) compliance with applicable listing and other legal requirements in relation to financial reporting.

In regard to the above:

- (i) members of the Committee shall liaise with the Board, members of senior management and the principal financial officer and the Committee shall meet, at least once a year, with the external auditor and head of internal audit; and
- (ii) the Committee shall consider any significant or unusual items that are, or may need to be, reflected in the annual report and accounts and shall give due consideration to any matters raised by the principal financial officer, head of internal audit, head of compliance or external auditor.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Board Responsibility and Oversight (continued)

AUDIT COMMITTEE (continued)

- (iii) the Committee shall ensure that the accounts are prepared in a timely and accurate manner with frequent reviews of the adequacy of provisions against contingencies and bad and doubtful debts.

Responsibilities of the Committee (continued)

2. To review the Bank's financial and accounting policies and practices.
3. To review the Bank's internal financial controls and its internal control and risk management systems.
4. To monitor and review the internal audit plan, the effectiveness of the internal audit function and co-ordination between the internal and external auditors, consider the major findings of internal investigations and management's response, obtain assurances that the internal audit function is adequately resourced and has appropriate standing and is free from constraint by management or other restrictions. The Committee shall approve the appointment and removal of the head of internal audit.
5. To make recommendations to the Board, for it to put to the shareholders for their approval in general meeting, in relation to the appointment, re-appointment and removal of the external auditor and to approve the remuneration and terms of engagement of the external auditor.
6. To review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process, taking into consideration relevant professional and regulatory requirements and reports from the external auditors on their own policies and procedures regarding independence and quality control and to oversee the appropriate rotation of audit partners with the external auditor.
7. To implement the HSBC Group policy on the engagement of the external auditor to supply non-audit services, taking into account relevant ethical guidance regarding the provision of non-audit services by the external audit firm; where required under that policy to approve in advance any non-audit services provided by the external auditor that are not prohibited by the Sarbanes-Oxley Act of 2002 (in amounts to be pre-determined by the HSBC Group Audit Committee) and the fees for any such services; to report to the Board, identifying any matters in respect of which it considers that action or improvement is needed and make recommendations as to the steps to be taken. For this purpose "external auditor" shall include any entity that is under common control, ownership or management with the audit firm or any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as part of the audit firm nationally or internationally.
8. To review the external auditor's management letter and management's response, any material queries raised by the external auditor to management in respect of the accounting records, financial accounts or systems of control and management's response, the external auditors' annual report on the progress of the audit and management's annual internal control report.
9. To ensure a timely response is provided to the issues raised in the external auditor's management letter.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Board Responsibility and Oversight (continued)

AUDIT COMMITTEE (continued)

Responsibilities of the Committee (continued)

10. To discuss with the external auditor their general approach, nature and scope of their audit and reporting obligations before the audit commences including, in particular, the nature of any significant unresolved accounting and auditing problems and reservations arising from their interim reviews and final audits, major judgmental areas (including all critical accounting policies and practices used by the Bank and changes thereto), all alternative accounting treatments that have been discussed with management together with the potential ramifications of using those alternatives, the nature of any significant adjustments, the going concern assumption, compliance with accounting standards and legal requirements, reclassifications or additional disclosures proposed by the external auditor which are significant or which may in the future become material, the nature and impact of any material changes in accounting policies and practices, any written communications provided by the external auditor to management and any other matters the external auditor may wish to discuss (in the absence of management where necessary).
11. To review and discuss management's statement on internal control systems prior to endorsement by the Board, the effectiveness of the Bank's internal control systems and procedures for compliance with the HSBC Group compliance policy and the relevant regulatory and legal requirements in each of the markets where the Company is represented and whether management has discharged its duty to have an effective internal control system.
12. To consider any findings of major investigations of internal control matters as delegated by the Board or on the Committee's initiative and management's response.
13. To receive an annual report, and other reports from time to time as may be required by applicable laws and regulations, from the principal executive officer and principal financial officer to the effect that such persons have disclosed to the Committee and to the external auditor all significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which could adversely affect the Bank's ability to record and report financial data and any fraud, whether material or not, that involves management or other employees who have a significant role in the Bank's internal controls over financial reporting.
14. To review such information as the Disclosure Committee (if any) may request (including reports and minutes of the Disclosure Committee) from time to time.
15. To provide to the Board such assurances as it may reasonably require regarding compliance by the Bank, its subsidiaries and those of its associates for which it provides management services with all supervisory and other regulations to which they are subject.
16. To provide to the Board such additional assurance as it may reasonably require regarding the reliability of financial information submitted to it.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Board Responsibility and Oversight (continued)

AUDIT COMMITTEE (continued)

Responsibilities of the Committee (continued)

17. To receive from the Compliance function reports on the treatment of substantiated complaints regarding accounting, internal accounting controls or auditing matters received through the HSBC Group Disclosure Line (or such other system as the HSBC Group Audit Committee may approve) for the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters.
18. To review regular risk management reports setting out the risks involved in the Bank's business and how they are controlled and monitored by management and to review the effectiveness of the risk management framework.
19. To agree the Bank's policy for the employment of former employees of the external auditor, within the terms of the HSBC Group's policy.
20. Where applicable to review the composition, powers, duties and responsibilities of subsidiary companies' Audit Committees.
21. To undertake or consider on behalf of the Chairman or the Board such other related tasks or topics as the Chairman or the Board may from time to time entrust to it.
22. The Committee alone shall meet with the external auditor and with the head of internal audit at least once each year to ensure that there are no unresolved issues or concerns.
23. The Committee may appoint, employ or retain such professional advisors as the Committee may consider appropriate. Any such appointment shall be made through the secretary to the Committee, who shall be responsible for the contractual arrangements and payment of fees by the Company on behalf of the Committee.
24. The Committee shall review annually the Committee's terms of reference and its own effectiveness and recommend to the Board and HSBC Group Audit Committee any necessary changes.
25. To report to the Board on the matters set out in these terms of reference.
26. To provide half-yearly certificates to the HSBC Group Audit Committee, or to any audit committee of an intermediate holding company in the form required by the HSBC Group Audit Committee. Such certificates to include a statement that the members of the Committee are independent.
27. To review any related party transactions that may arise within the Bank and the HSBC Group.

Where the Committee's monitoring and review activities reveal cause for concern or scope for improvement, it shall make recommendations to the Board on action needed to address the issue or to make improvements and shall report any such concerns to the HSBC Group Audit Committee or to any audit committee of an intermediate holding company.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

RISK MANAGEMENT COMMITTEE

Membership

The present members of the Risk Management Committee ('the Committee') comprise:

Dato' Henry Sackville Barlow (Chairman)
Dato' Sulaiman bin Sujak
Datuk Ramli bin Ibrahim
Dato' Zuraidah binti Atan

Meetings

The first meeting of the Risk Management Committee was held on 17 July 2006 and a total of two (2) Risk Management Committee meetings were held during the financial year. The attendance of the Directors at the Risk Management Committee meetings held in 2006 was as follows:

Name of members	Independent/ Non-Independent	Attendance and number of meetings
Dato' Henry Sackville Barlow	Chairman, Independent non-executive Director	1 / 2
Dato' Sulaiman bin Sujak	Non-independent non-executive Director	2 / 2
Datuk Ramli bin Ibrahim	Independent non-executive Director	2 / 2
Dato' Zuraidah binti Atan	Independent non-executive Director	2 / 2

Terms of Reference

The Terms of Reference were approved at the meeting of the Board held on 9 February 2006.

Membership

The Committee shall comprise not less than three non-executive directors. All members shall be non-executive directors.

The Chairman of the Committee shall be an independent non-executive director appointed by the Board.

The Committee may invite any director, executive or other person to attend any meeting(s) of the Committee as it may from time to time consider desirable to assist the Committee in the attainment of its objective.

The Committee shall be supported by executives from the Bank's Executive Committee, Asset and Liability Committee and Audit Committee, or such other persons as the Committee shall consider appropriate. The Committee Secretary shall circulate such reports and minutes of the Risk Committees as are appropriate to all members of the Committee.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Board Responsibility and Oversight (continued)

RISK MANAGEMENT COMMITTEE (continued)

Meetings and Quorum

The Committee shall meet with such frequency and at such times as it may determine but in any event, not less than once every quarter.

The quorum for meetings shall be two non-executive directors, including one independent non-executive director.

At all meetings of the Committee, the Chairman of the Committee, if present, shall preside. If the Chairman is absent, the members present at the meeting shall elect a chairman of the meeting, who shall be an independent non-executive director.

Objective

The purpose of the Committee is to oversee senior management's activities in managing credit, market, liquidity, operational, legal and other risk and to ensure that the risk management process is in place and functioning.

Responsibilities of the Committee

1. Without limiting the generality of the Committee's objective, the Committee shall have the following responsibilities:
 - 1.1 To review and recommend risk management strategies, policies and risk tolerance for the Board's approval.
 - 1.2 To review and assess adequacy of risk management policies and framework in identifying, measuring, monitoring and controlling risk and the extent to which these are operating effectively.
 - 1.3 To ensure infrastructure, resources and systems are in place for risk management, i.e. ensuring that the staff responsible for implementing risk management systems perform those duties independent of the Bank's risk taking activities.
 - 1.4 To review management's periodic reports on risk exposure, risk portfolio composition and risk management activities.
2. In order to be consistent with HSBC Group's global risk management strategies, where strategies and policies related to the objective of this Committee are driven by the parent company, the Committee shall:
 - 2.1 Discuss, evaluate and provide input on strategies and policies to suit local environment; and
 - 2.2 Deliberate and make the necessary recommendations on such strategies and policies to assist the Board when approving major issues and strategies.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Board Responsibility and Oversight (continued)

RISK MANAGEMENT COMMITTEE (continued)

3. Where major decisions related to the objective of this Committee are made by the parent company, the Committee shall evaluate the issues before making recommendations to the Board for endorsement and adoption of the decision/strategy/policy. The policies adopted shall adhere to the laws of Malaysian jurisdiction and regulations.
4. The Committee shall not be delegated with decision making powers but shall report its recommendation to the Board for decision.

Written or Circulating Resolution

Any resolution in writing, signed or assented to by all the members of the Committee shall be as valid and effectual as if it had been passed at a meeting of the Committee duly called and constituted and may consist of several documents in the like form each signed by one or more of the members of the Committee.

Amendment

The Committee shall from time to time review the Committees' terms of reference and its own effectiveness and recommend to the Board any necessary changes.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

NOMINATING COMMITTEE

Membership

The present members of the Nominating Committee ('the Committee') comprise:

Datuk Dr Zainal Aznam bin Mohd Yusof (Chairman)
Dato' Zarir Jal Cama
Dato' Sulaiman bin Sujak
Professor Emeritus Dr Mohamed Ariff bin Abdul Kareem
Dato' Zuraidah binti Atan

Meetings

The first meeting of the Nominating Committee was held on 22 November 2006. One meeting was held during the financial year. The attendance of the Directors at the Nominating Committee meetings held in 2006 was as follows:

Name of members	Independent/ Non-Independent	Attendance and number of meetings
Datuk Dr Zainal Aznam bin Mohd Yusof	Chairman, Independent non-executive Director	1 / 1
Dato' Zarir Jal Cama	Deputy Chairman and Chief Executive Officer	1 / 1
Dato' Sulaiman bin Sujak	Non-independent non-executive Director	1 / 1
Professor Emeritus Dr Mohamed Ariff bin Abdul Kareem	Independent non-executive Director	1 / 1
Dato' Zuraidah binti Atan	Independent non-executive Director	1 / 1

Terms of Reference

The Terms of Reference were approved at the meeting of the Board held on 9 February 2006.

Membership

The Committee shall consist of a minimum of five members, of which at least four must be non-executive directors.

The Chairman of the Committee shall be an independent non-executive directors appointed by the Board. In order to avoid conflict of interest, a member of the Committee shall abstain from participating in discussions and decisions on matters involving him.

The Committee may invite any director, executive or other person to attend any meeting(s) of the Committee as it may from time to time consider desirable to assist the Committee in the attainment of its objective.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Board Responsibility and Oversight (continued)

NOMINATING COMMITTEE (continued)

Meetings and Quorum

The Committee shall meet with such frequency and at such times as it may determine but in any event, not less than once a year.

The quorum for meetings shall be two non-executive directors, including one independent non-executive director.

At all meetings of the Committee, the Chairman of the Committee, if present, shall preside. If the Chairman is absent, the members present at the meeting shall elect a chairman of the meeting, who shall be an independent non-executive director.

Objective

The Committee shall provide a formal and transparent procedure for the appointment of directors and Chief Executive Officer as well as assessment of effectiveness of individual directors, Board as a whole and the performance of the Chief Executive Officer and key senior management officers.

Responsibilities of the Committee

1. Without limiting the generality of the Committee's objective, the Committee shall have the following responsibilities:
 - 1.1 To establish minimum requirements for the Board, i.e. required mix of skills, experience, qualification and other core competencies required of a director. The Committee shall also be responsible for establishing minimum requirements for the Chief Executive Officer;
 - 1.2 To recommend and assess the nominees for directorship, Board committee members as well as nominees for the CEO. This includes assessing directors for reappointment, before an application for approval is submitted to Bank Negara Malaysia. The actual decision as to who shall be nominated should be the responsibility of the full Board;
 - 1.3 To oversee the overall composition of the Board, in terms of the appropriate size and skills, and the balance between executive directors, non-executive directors and independent directors through annual review;
 - 1.4 To recommend to the Board the removal of a director/CEO from the Board/management if the director/CEO is ineffective, errant and negligent in discharging his responsibilities;
 - 1.5 To establish a mechanism for the formal assessment on the effectiveness of the Board as a whole and the contribution of each director to the effectiveness of the Board, the contribution of the Board's various committees and the performance of the CEO and other key senior management officers. Annual assessment should be conducted based on an objective performance criterion. Such performance criteria should be approved by the full Board;

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Board Responsibility and Oversight (continued)

NOMINATING COMMITTEE (continued)

- 1.6 To ensure that all directors receive an appropriate continuous training program in order to keep abreast with the latest developments in the industry;
- 1.7 To oversee the appointment, management succession planning and performance evaluation of key senior management officers;
- 1.8 To recommend to the Board the removal of key senior management officers if they are ineffective, errant and negligent in discharging their responsibilities; and
- 1.9 To assess, on an annual basis, to ensure that the directors and key senior management officers are not disqualified under section 56 of the Banking and Financial Institutions Act 1989.
2. In order to be consistent with HSBC Group's global strategies, where strategies and policies related to the objective of this Committee are driven by the parent company, the Committee shall:
 - 2.1 Discuss, evaluate and provide input on strategies and policies to suit local environment; and
 - 2.2 Deliberate and make the necessary recommendations on such strategies and policies to assist the Board when approving major issues and strategies
3. Where major decisions related to the objective of this Committee are made by the parent company, the Committee shall evaluate the issues before making recommendations to the Board for endorsement and adoption of the decision/strategy/policy. The policies adopted shall adhere to the laws of Malaysian jurisdiction and regulations.
4. The Committee shall not be delegated with decision making powers but shall report its recommendation to the Board for decision.

Written or Circulating Resolution

Any resolution in writing, signed or assented to by all the members of the Committee shall be as valid and effectual as if it had been passed at a meeting of the Committee duly called and constituted and may consist of several documents in the like form each signed by one or more of the members of the Committee.

Amendment

The Committee shall from time to time review the Committees' terms of reference and its own effectiveness and recommend to the Board any necessary changes.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

MANAGEMENT REPORTS

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

- Quarterly business progress report
- Quarterly assets and liabilities summary
- Quarterly profit and loss statement
- Quarterly key financial ratios and statistics
- Quarterly significant Bank Negara Malaysia and HSBC Group's requirements
- Quarterly Bank Negara Malaysia's benchmarking statistics
- Quarterly derivatives outstanding
- Quarterly update on Basel II and Sarbanes-Oxley projects
- Quarterly risk management reports on sub-standard accounts and bad and doubtful debts
- Quarterly credit advances reports
- Minutes of the monthly Executive Committee meetings held
- Minutes of the monthly Asset and Liability Management Committee meetings held
- Minutes of the Audit Committee meetings held
- Minutes of the Risk Management Committee meetings held
- Human resource update
- Environmental issues update
- Comparative analysis of competitor banks

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

INTERNAL AUDIT AND INTERNAL CONTROL ACTIVITIES

The Board of Directors is responsible for internal control and for reviewing its effectiveness. Procedures have been designed for safeguarding assets against unauthorised use or disposition; for maintaining proper accounting records; and for the reliability of financial information used within the business or for publication. Such procedures are designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material errors, losses or fraud.

Systems and procedures are in place to identify, control and report on the major risks including credit, changes in the market prices of financial instruments, liquidity, operational error, breaches of law or regulations, unauthorised activities and fraud. Exposure to these risks is monitored by the Asset and Liability Management Committee (ALCO), Executive Committee (EXCO), Operational Risk Committee, Audit Committee, Risk Management Committee and Board of Directors.

Responsibilities for financial performance against plans and for capital expenditure, credit exposures and market risk exposures are delegated with limits to line management. Functional management in HSBC Group Head Office has been given responsibility to set policies, procedures and standards in the areas of finance; legal and regulatory compliance; internal audit; human resources; credit; market risk; operational risk; computer systems and operations; property management; and for certain global product lines. The Bank operates within these policies, procedures and standards set by the HSBC Group Head Office functions.

The Bank's internal audit function monitors compliance with policies and standards and the effectiveness of internal control structures across the whole Bank in conjunction with other HSBC Group Internal Audit units. The work of the internal audit function is focused on areas of greatest risk to the Bank as determined by a risk-based approach. The head of the internal audit function reports to the Audit Committee and the Head of HSBC Group Audit function for the Asia Pacific region.

The Audit Committee has kept under review the effectiveness of this system of internal control and has reported regularly to the Board of Directors. The key processes used by the Committee in carrying out its reviews include regular reports from the heads of key risk functions; the production annually of reviews of the internal control framework (RICF – a self certification process) against HSBC Group benchmarks, which cover all internal controls, both financial and non-financial; annual confirmations from the Chief Executive Officer that there have been no material losses, contingencies or uncertainties caused by weaknesses in internal controls; internal audit reports; external audit reports; prudential reviews; and regulatory reports.

The Audit Committee has also reviewed the annual internal audit plan to ensure adequate scope and comprehensive coverage on the audit activities, effectiveness of the audit process, adequate resource deployment for the year and satisfactory performance of the Bank's Internal Audit Unit. The Committee has reviewed the internal audit reports, audit recommendations made and management's response to these recommendations. Where appropriate, the Committee has directed action to be taken by the Bank's management team to rectify any deficiencies identified by internal audit and improve the system of internal controls based on the internal auditors' recommendations for improvements.

The Directors, through the Audit Committee and the Risk Management Committee, have conducted an annual review of the effectiveness of the Bank's system of internal control covering all controls, including financial, operational and compliance controls and risk management.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

RISK MANAGEMENT

All of the Bank's activities involve analysis, evaluation, acceptance and management of some degree of risk or combination of risks. The key business risks are credit risk, liquidity risk, market risk and operational risk. Market risk includes foreign exchange, interest rate and equity price risk.

The Bank's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls, and to monitor the risks and limits continually by means of reliable and up-to-date administrative and information systems. The Bank continually modifies and enhances its risk management policies and systems to reflect changes in markets, products and best practice risk management processes. Training, individual responsibility and accountability, together with a disciplined, conservative and constructive culture of control, lie at the heart of the Bank's management of risk.

The Executive Committee, Operational Risk Management Committee and Asset and Liability Management Committee, appointed by the Board of Directors, formulate risk management policy, monitors risk and regularly reviews the effectiveness of the Bank's risk management policies.

The Risk Management Committee has been entrusted with the responsibility to oversee senior management's activities in managing credit, market, liquidity, operational, legal and other risk and to ensure that the risk management process is in place and functioning.

Credit risk management

Credit risk is the risk that financial loss arises from the failure of a customer or counterparty to meet its obligations under a contract. It arises principally from lending, trade finance and treasury activities. The Bank has dedicated standards, policies and procedures to control and monitor all such risks.

A Credit and Risk Management structure under the Chief Credit Officer who reports to the Chief Executive Officer, is in place to ensure a more coordinated management of credit risk and a more independent evaluation of credit proposals. The Chief Credit Officer has a functional reporting line to the HSBC Group General Manager, Group Credit and Risk.

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

- risk concentrations and exposures to industry sectors;
- large customer group exposures; and
- large non-performing accounts and impairment allowances.

The Bank has systems in place to control and monitor its exposure at the customer and counterparty level. Regular audits of credit processes are undertaken by the Internal Audit function. Such audits include consideration of the completeness and adequacy of credit manuals and lending guidelines, together with an in-depth analysis of a representative sample of accounts, an overview of homogeneous portfolios of similar assets to assess the quality of the loan book and other exposures, and adherence to HSBC Group standards and policies in the extension of credit facilities.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Risk Management (continued)

Credit risk management (continued)

Individual accounts are reviewed to ensure that risk grades are appropriate, that credit and collection procedures have been properly followed and that, where an account evidences deterioration, impairment allowances are raised in accordance with the HSBC Group's established processes. Internal Audit will discuss with management risk ratings they consider to be inappropriate, and their subsequent recommendations for revised grades must then be assigned to the facilities concerned.

At balance sheet date, exposure to the purchase of residential property accounted for 36% (2005: 38%) of total loans, advances and financing. Other concentrations of credit risk by economic purposes are disclosed in Note 6(iv).

Liquidity and funding management

The Bank maintains a diversified and stable funding base of core retail and corporate customer deposits as well as portfolios of highly liquid assets. The objective of the Bank's liquidity and funding management is to ensure that all foreseeable funding commitments and deposit withdrawals can be met when due.

The management of liquidity and funding is primarily carried out in accordance with the Bank Negara Malaysia New Liquidity Framework; and practice and limits set by the HSBC Group Management Board. The HSBC Group Management Board ('GMB') operates as a general management committee under the direct authority of the HSBC Group Board of Directors. The HSBC GMB exercises the powers, authorities and discretions of the HSBC Group Board of Directors in so far as they concern the management and day to day running of the HSBC Group in accordance with such policies and directions as the HSBC Group Board of Directors may from time to time determine. These limits vary to take account of the depth and liquidity of the local market in which we operate. The Bank maintains a strong liquidity position and manages the liquidity profile of assets, liabilities and commitments so that cash flows are appropriately balanced and all funding obligations are met when due.

The Bank's liquidity and funding management process includes:

- projecting cash flows and considering the level of liquid assets necessary in relation thereto;
- monitoring balance sheet liquidity ratios against internal and regulatory requirements;
- maintaining a diverse range of funding sources with adequate back-up facilities;
- monitoring depositor concentration in order to avoid undue reliance on large individual depositors and ensure a satisfactory overall funding mix; and
- maintaining liquidity and funding contingency plans. These plans identify early indicators of stress conditions and describe actions to be taken in the event of difficulties arising from systemic or other crises while minimising adverse long-term implications for the business.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Risk Management (continued)

Market risk management

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

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

The Bank separates exposures to market risk into either trading or non-trading portfolios. Trading portfolios include those positions arising from market making and proprietary position taking. Non-trading portfolios primarily arise from the management of the commercial banking assets and liabilities.

The management of market risk is principally undertaken using risk limit mandates approved by the HSBC Group Traded Markets Development and Risk Unit ('TMR') (an independent unit which develops HSBC Group's market risk management policies and measurement techniques). Market risks which arise on each product is transferred to the Bank's Global Markets unit and ALCO portfolio for management as the Global Markets unit has the necessary skills and tools to professionally manage such risks. Limits are set for each portfolio, product currency and risk type, with market liquidity being the principal factor in determining the level of limits set. The Bank has an independent market risk control function that is responsible for measuring market risk exposures in accordance with the policies defined by TMR and monitoring and reporting these exposures against the prescribed limits on a daily basis. Positions are monitored daily and excesses are reported immediately to local senior management and HSBC Group Treasury.

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

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

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Risk Management (continued)

Market risk management (continued)

Value at risk ('VAR')

One of the principal tools used by the Bank to monitor and limit market risk exposure is VAR. VAR is a technique that estimates the potential losses that could occur on risk positions as a result of movements in market rates and prices over a specified time horizon and to a 99 per cent level of confidence. The Bank calculates VAR daily. The VAR model used by the Bank is predominantly based on historical simulation. The historical simulation model derives plausible future scenarios from historical market rates time series, taking account of inter-relationships between different markets and rates, for example between interest rates and foreign exchange rates. Potential movements in market prices are calculated with reference to market data from the last two years and these rate changes are applied to current positions to create a profit and loss distribution for the portfolio. The 99 per cent confidence interval for this distribution represents the Bank's one-day VAR.

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

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

The Bank recognises these limitations by augmenting its VAR limits with other position and sensitivity limit structures. Stress tests are produced on a monthly basis based on the HSBC Group's stress-testing parameters, and on a quarterly basis based on Bank Negara Malaysia's parameters to determine the impact of changes in interest rates, exchange rates and other main economic indicators on the Bank's profitability and capital adequacy. The stress-testing provides ALCO with an assessment of the financial impact of identified extreme events on the market risk exposures of the Bank.

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

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Risk Management (continued)

Operational risk management

Operational risk is the risk of loss arising from fraud, unauthorised activities, error, omission, inefficiency, systems failure or external events. It is inherent to every business organisation and covers a wide spectrum of issues.

The Bank manages this risk through a control-based environment in which processes are documented, authorisation is independent and transactions are reconciled and monitored. This is supported by an independent programme of periodic reviews undertaken by Internal Audit, and by monitoring external operational risk events, which ensure that the Bank stays in line with best practice and takes account of lessons learned from publicised operational failures within the financial services industry.

The Bank adheres to the HSBC Group standard on operational risk. This standard explains how HSBC manages operational risk by identifying, assessing, monitoring, controlling and mitigating the risk, rectifying operational risk events and implementing any additional procedures required for compliance with local statutory requirements. The standard covers the following:

- operational risk management responsibility is assigned at senior management level within the business operation;
- information systems are used to record the identification and assessment of operational risks and generate appropriate, regular management reporting;
- operational risks are identified by assessments covering operational risks facing each business and risk inherent in processes, activities and products. Risk assessment incorporates a regular review of identified risks to monitor significant changes;
- operational risk loss data is collected and reported to senior management. Aggregate operational risk losses are recorded and details of incidents above a materiality threshold are reported to the Audit Committee; and
- risk mitigation, including insurance, is considered where this is cost-effective.

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

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

RATINGS STATEMENT

Rating Agency Malaysia Berhad (RAM) has in May 2006 reaffirmed the Bank's long-term general bank rating at AAA and the short-term rating at P₁.

Bank Rating Symbols and Definitions

<i>Rating</i>	<i>Definition</i>
AAA	<i>Financial Institutions rated in this category are adjudged to offer the highest safety for timely payments of financial obligations. This level of rating indicates corporate entities with strong balance sheets, favourable credit profiles and consistent records of above-average profitability. Their capacities for timely payments of contractual financial obligations are unlikely to be impacted seriously by any foreseeable changes in economic conditions.</i>
P ₁	<i>Financial institutions in this category have superior capacities for timely payments of obligations.</i>

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

DIRECTORS' REPORT FOR THE YEAR ENDED 31 DECEMBER 2006

The directors have pleasure in submitting their report and the audited financial statements of the Bank and of the group for the year ended 31 December 2006.

Principal Activities

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

The principal activities of the subsidiary companies are as disclosed in Note 10 to the financial statements.

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

Results

	<i>Group and Bank</i>
	RM'000
Profit before taxation and zakat	949,062
Taxation and zakat	(261,656)
Profit after taxation and zakat	687,406

Dividends

Since the end of the previous financial year, the Bank paid a final dividend of 182.0% less tax totalling RM150 million as proposed in the previous year's directors' report. The Bank also paid an interim dividend of 182.0% less tax amounting to RM150 million in respect of financial year 2006.

The directors now recommend a final dividend of 303.3% less tax totalling RM250 million in respect of the current financial year on the fully issued and paid-up ordinary shares of the Bank.

Reserves and Provisions

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

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Directors' Report (continued)

Bad and Doubtful Debts and Financing

Before the financial statements of the Bank and of the group were made out, the directors took reasonable steps to ascertain that action had been taken in relation to the writing off of bad debts and the making of allowance for doubtful debts and financing, and satisfied themselves that all known bad debts had been written off and adequate allowance made for doubtful debts and financing.

At the date of this report, the directors are not aware of any circumstances which would render the amount written off for bad debts, or the amount of the allowance for doubtful debts, in the financial statements of the Bank and of the group inadequate to any substantial extent.

Current Assets

Before the financial statements of the Bank and of the group were made out, the directors took reasonable steps to ascertain that any current assets, other than debts and financing, which were unlikely to be realised in the ordinary course of business at their value as shown in the accounting records of the Bank and of the group have been written down to an amount which they might be expected to realise.

At the date of this report, the directors are not aware of any circumstances which would render the values attributed to the current assets in the financial statements of the Bank and of the group misleading.

Valuation Methods

At the date of this report, the directors are not aware of any circumstances which have arisen which would render adherence to the existing methods of valuation of assets or liabilities in the financial statements of the Bank and of the group misleading or inappropriate.

Contingent and Other Liabilities

At the date of this report there does not exist:

- a any charge on the assets of the Bank or of the group which has arisen since the end of the financial year which secures the liabilities of any other person, or
- b any contingent liability in respect of the Bank or of the group that has arisen since the end of the financial year other than in the ordinary course of business.

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

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Directors' Report (continued)

Change of Circumstances

At the date of this report, the directors are not aware of any circumstances, not otherwise dealt with in this report or the financial statements of the Bank and of the group, that would render any amount stated in the financial statements misleading.

Items of an Unusual Nature

Except as disclosed in the financial statements, the results of the operations of the Bank and of the group for the financial year were not, in the opinion of the directors, substantially affected by any item, transaction or event of a material and unusual nature.

There has not arisen in the interval between the end of the financial year and the date of this report, any item, transaction or event of a material and unusual nature likely to affect substantially the results of the operations of the Bank and of the group for the current financial year in which this report is made.

Business Strategy During the Year

In 2006, despite the US economy slowdown and price increases in domestic fuel supply or utilities which had an adverse impact on consumer demand, the Malaysia economy remained resilient. The banking sector was operating in an environment of softening consumer demand and increased competition mainly due to new players entering the banking sector arising from the liberalization policy progressively implemented by Bank Negara Malaysia.

The bank strategy was to continue investing in our brand, people and product development in order to differentiate us in terms of product quality and customer service. The bank continued to recruit talent in all areas and invest substantially on staff training aiming to offer premium quality services to our customers. Despite the increasing competitive commercial banking environment, HSBC is well positioned in all sectors of growth, namely retail and investment banking, Islamic Financing as well as Takaful.

In the recent regional brand tracking study, HSBC rebounded strongly in various brand measurements, reflecting the success of our marketing strategy. Rating Agency Malaysia has reaffirmed the bank's AAA/P1 ratings, reflecting our robust asset quality and strong financial standing. The bank continues to win recognition with various awards in 2006 including:

1. The Asset Triple A, Best Bank in Malaysia – *The Asset*
2. Best Foreign Bank in Malaysia – *Finance Asia*
3. Best Overall Foreign Cash Management Bank – *Asiamoney*
4. Best Islamic Wholesale Bank (HSBC Amanah) – *Euromoney*
5. Best for Islamic Private Banking Services (HSBC Amanah) – *Euromoney*
6. Top rated No. 1 Custodian in Malaysia – *Global Custody*
7. Best foreign Exchange bank in Malaysia – *Global Finance*
8. Best Sub-Custodian in Malaysia – *Global Finance*
9. Best Consumer Internet Bank in Malaysia – *Global Finance*
10. Award for Excellence in Banking and Finance–Foreign Bank for 2006
–*Technology Business Review*

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Directors' Report (continued)

Business Strategy During the Year (continued)

The bank continued to grow its mortgage, cards and personal term loans. In September 2006, our credit card business crossed the 1 million cards milestone, making HSBC the 3rd largest credit card issuer in Malaysia. The bank was also the leading independent unit trust agent amongst financial institutions in Malaysia and 13 additional unit trust funds were launched in 2006.

In 2006, under the liberalization policy in the finance sector, 3 new branches were opened and the fourth branch is scheduled to open in March 2007, expanding our geographical reach to a wider customer base.

On corporate banking, we continued to extend our competitive advantage with our global network as well as our expertise on cross border financing and international trade. The bank provided support to local companies expanding their operations into China, India and the Middle East.

In 2006, the Ringgit strengthened against USD and the Bank Negara Overnight Policy Rate was revised upwards twice. The volatility in rates resulted in greater hedging activity from corporate and institutional clients as well as higher trading opportunities. The bank continued to be the market leader in foreign exchange and interest rate derivatives in Malaysia. The bank also maintained its market leadership position in Debt Capital markets, being the top Foreign Bookrunner for Malaysian Bonds and also the top Syndicated Loan Manager in Malaysia for 2006, amid a market environment where corporate customers were seeking funds for local and foreign investment projects.

HSBC has proactively built its profile and visibility in the SME and commercial banking space through marketing activities, campaigns and sponsorships, as well as setting up our SME infrastructure. The bank introduced Business Internet Banking and Business Telephone Banking to provide our customers with greater access to our services and products.

In line with the government direction to promote Malaysia as the International Islamic Financial Hub, HSBC is committed to grow its Islamic banking business. Through HSBC Amanah Takaful, the bank aims to offer a full range of Islamic finance solutions to our customers.

HSBC has successfully reduced its gross NPL ratio from 3.12% last year to 2.15% as at 31 December 2006. The credit risk management of the bank utilised its risk identification database management system to enhance its surveillance capability in identifying potential high risk advances in order to contain credit losses.

In 2006, HSBC implemented credit card SMS interactive services and end-to-end straight-thru processing systems, to provide a higher quality of service to customers and improve operational efficiency. The shared ATM network (HOUSE) with three other locally-incorporated foreign banks was also implemented successfully, offering our customers access to an additional 221 ATMs nationwide.

As part of the continuous effort to improve customer experience, the bank has set-up the HSBC Service Centre (HSC) of Excellence. HSC will act as an one-stop service centre for all retail products as well as card operations. Major improvements in service quality were achieved in 2006 led by the bank's Quality Council and Service Transformation Team, namely a higher Net Promoter score, a lower average cashier waiting time and improved call centre abandoned rate, as well as reduced errors rates in processing operations.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Directors' Report (continued)

Business Strategy During the Year (continued)

HSBC custody unit was awarded the Best Sub-Custodian in Malaysia for the 4th consecutive year by Global Finance, recognizing the commitment of the bank in providing excellent custodian services to our customers.

HSBC continued to commit in corporate and social responsibility (CSR). The bank was proactively involved in various CSR programs, not only focusing on education of the environment but also contributing to charities, historical heritage conservation, Arts and Music. HSBC also sponsored NGOs on environmental research programmes. The Bank was invited to be part of the working committee which set up the Socially Responsible Investment (SRI) Index for Malaysia on 1st December 2006.

Outlook For 2007

With prime pumping activities under the 9th Malaysian Plan and other initiatives such as an expansionary budget for 2007, launching of Visit Malaysia Year and a number of major private sector projects, we are positive on the local economy in 2007. These stimuli are expected to cushion the projected decline in external demand, as the global economic outlook remains uncertain and challenging in 2007.

The government officially projects the 2007 GDP growth at 6% while Malaysia Institute of Economic Research projects the 2007 CPI to trend downwards to 3.0%. Growth segments expected in 2007 are the construction, agriculture and services sector while softening demand is expected in the electronic and electrical sector.

The local banking sector remains highly competitive under the liberalization policy in the finance industry. With a good number of Malaysian clients expanding overseas, HSBC is well positioned to service this customer segment. With the 9th Malaysian Plan being rolled out, we foresee more financing activities on a project basis. There will be a continued and focused push for funding through the debt capital markets, structured treasury products, trade financing, liability management and Amanah financing. Selectively with clients, there will be a push for convertible / exchangeable bonds and REITs.

The volatility in foreign exchange markets is expected to continue providing trading opportunities for the bank and hedging needs by corporate customers. The low interest rate environment has been attracting customers' interest in structured investment products. With the present conducive environment in Malaysia, Islamic financing and hedging solutions are likely to see a substantial growth in usage in the coming year.

In retail banking, the bank will continue to reinforce our market share in core products such as mortgages, personal installment loans, cards, wealth management products and deposit garnering. HSBC will leverage the one million card base by providing a complete financial solution to the card holders. The bank will continue to grow the mortgage book by providing innovative homeloan products that cater for different customer groups. HSBC will collaborate with HSBC Amanah Takaful Malaysia to drive penetration of bancassurance sales into our customer base.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Directors' Report (continued)

Outlook For 2007 (continued)

In 2007, the bank will invest in SME and MME sectors which will be the fastest growth sectors in coming years, amid intensive competition for customers, good quality credit, talent and increased asset attrition. For trade services, the bank will focus on growing Export Factoring, Supply Chain solutions, TradeAdvances and Structure Trade Finance business.

HSBC will continue to increase its operational efficiency and productivity through various operational process re-engineering and customer focused initiatives to reduce processing costs, free up time for sales and service to customers, and improve customer service delivery. Various initiatives to rationalise resources and simplify operational processes will be rolled out in 2007, with the ultimate goal to improve the customer experience.

HSBC is well positioned in all areas of growth and prepared for another challenging year in 2007.

Directors and Their Interests in Shares

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

Michael Roger Pearson Smith
Dato' Zarir Jal Cama
Ian Douglas Francis Ogilvie
Douglas Jardine Flint
Dato' Sulaiman bin Sujak
Dato' Henry Sackville Barlow
Datuk Ramli bin Ibrahim
Datuk Dr Zainal Aznam bin Mohd Yusof
Professor Emeritus Dr Mohamed Ariff bin Abdul Kareem
Dato' Zuraidah binti Atan

In accordance with the Articles of Association, Mr Michael Roger Pearson Smith, Mr Douglas Jardine Flint and Datuk Ramli bin Ibrahim retire from the Board at the Annual General Meeting and, being eligible, offer themselves for re-election.

In accordance with Section 129(2) of the Companies Act, 1965, Dato' Sulaiman bin Sujak being over seventy years (70) of age, retires at the Annual General Meeting, and being eligible, offers himself for reappointment in accordance with Section 129(6) of the Companies Act, 1965.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Directors' Report (continued)

Directors and Their Interests in Shares (continued)

According to the register of directors' shareholdings maintained by the Bank in accordance with Section 134 of the Companies Act, 1965, the directors holding office at year end who have beneficial interests in the shares of related corporations are as follows:

Name	Number of Shares			Balance at 31.12.2006
	Balance at 1.1.2006	Bought	(Sold)	
HSBC Holdings plc				
Ordinary shares of USD0.50				
Michael Roger Pearson Smith	86,873	66,927 (A)	(10,000)	143,800
Dato' Zarir Jal Cama	199,071	29,576 (B)	-	228,647
Ian Douglas Francis Ogilvie	3,511	11,157 (C)	(1,485)	13,183
Douglas Jardine Flint	81,726	23,208 (D)	-	104,934
Dato' Sulaiman bin Sujak	44,339	1,088 (E)	-	45,427
Dato' Henry Sackville Barlow	990,000 *	-	-	990,000 *

(A) Shares were acquired through scrip dividends and share plan awards vested.

(B) Shares were acquired through purchases, scrip dividends, share plan awards vested and exercise of rights over options.

(C) Shares were acquired through scrip dividends, share plan awards vested and exercise of rights over options.

(D) Shares were acquired through scrip dividends, share plan award vested, reinvestment of dividends and purchases.

(E) Shares were acquired through scrip dividends.

* Indirect interest held through Majedie Investments plc

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Directors' Report (continued)

Directors and Their Interests in Shares (continued)

Name	Number of Shares				
	Awards held at 1.1.2006	Awards made during year *	Awards forfeited during the year	(Awards vested during the year)	Awards held at 31.12.2006
HSBC Holdings plc					
Restricted Share Plan					
Michael Roger Pearson Smith	278,038	7,247	# (83,729)	(60,881)	140,675
Dato' Zarir Jal Cama	143,895	36,872	-	(12,548)	168,219
Ian Douglas Francis Ogilvie	58,184	15,604	-	(8,142)	65,646
Douglas Jardine Flint	584,304	15,790	# (177,883)	(65,761)	356,450
Dato' Sulaiman bin Sujak	6,118	-	-	-	6,118

* Includes scrip dividends

Shares belonging to the HSBC Share Plan but previously reported under the Restricted Share Plan

Name	Number of Shares				
	Awards held at 1.1.2006	Awards made during year [^]	Awards forfeited during the year	(Awards vested during the year)	Awards held at 31.12.2006
HSBC Holdings plc					
HSBC Share Plan					
Michael Roger Pearson Smith	-	165,102	-	-	165,102
Douglas Jardine Flint	-	353,041	-	-	353,041

[^] Included scrip dividends and shares previously reported under the Restricted Share Plan.

Name	Number of Shares				
	Balance at 1.1.2006	Granted	(Exercised)	(Lapsed)	Balance at 31.12.2006
Options over HSBC Holdings plc Shares					
Michael Roger Pearson Smith	70,500	-	(70,500)	-	-
Dato' Zarir Jal Cama	1,766	418	(1,794)	-	390
Ian Douglas Francis Ogilvie	41,972	-	(7,535)	-	34,437
Douglas Jardine Flint	2,617	-	-	-	2,617

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Directors' Report (continued)

Directors' Benefits

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

Neither at the end of the financial year, nor at any time during that year, did there subsist any arrangements to which the Bank is a party whereby Directors might acquire benefits by means of the acquisition of shares in, or debentures of, the Bank or any other body corporate, except for:

- i Directors who were granted the option to subscribe for shares in the ultimate holding company, HSBC Holdings plc, under Executive/Savings-Related Share Option Schemes at prices and terms as determined by the schemes, and
- ii Directors who were conditionally awarded shares of the ultimate holding company, HSBC Holdings plc, under its Restricted Share Plan/HSBC Share Plan.

Ultimate Holding Company

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

Auditors

The auditors, Messrs KPMG, have indicated their willingness to accept re-appointment.

Signed in accordance with a resolution of the directors:

.....Director
DATO' ZARIR JAL CAMA

.....Director
IAN DOUGLAS FRANCIS OGILVIE

Kuala Lumpur, Malaysia
29 January 2007

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

DIRECTORS' STATEMENT

In the opinion of the directors:

We, Dato' Zarir Jal Cama and Ian Douglas Francis Ogilvie, being two of the directors of HSBC Bank Malaysia Berhad, do hereby state on behalf of the directors that, in our opinion, the financial statements set out on pages 40 to 104 are drawn up in accordance with applicable approved accounting standards for entities other than private entities issued by the Malaysian Accounting Standards Board as modified by Bank Negara Malaysia's guidelines so as to give a true and fair view of the state of affairs of the Bank and of the group as at 31 December 2006 and of the results and cash flows of the Bank and of the group for the year ended on that date.

Signed at Kuala Lumpur, Malaysia this 29 January 2007.

In accordance with a resolution of the directors:

.....Director
DATO' ZARIR JAL CAMA

.....Director
IAN DOUGLAS FRANCIS OGILVIE

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

STATUTORY DECLARATION

I, Baldev Singh s/o Gurdial Singh, being the officer primarily responsible for the financial management of HSBC Bank Malaysia Berhad, do solemnly and sincerely declare that, to the best of my knowledge and belief, the financial statements set out on pages 40 to 104 are correct, and I make this solemn declaration conscientiously believing the same to be true, and by virtue of the provisions of the Statutory Declarations Act, 1960.

Subscribed and solemnly declared by the abovenamed

BALDEV SINGH s/o GURDIAL SINGH at KUALA LUMPUR

in WILAYAH PERSEKUTUAN, MALAYSIA this 29th day of January 2007.

.....

BEFORE ME:

.....

Signature of Commissioner for Oaths

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

**REPORT OF THE AUDITORS
TO THE MEMBERS OF HSBC BANK MALAYSIA BERHAD**

We have audited the financial statements set out on pages 40 to 104. The preparation of the financial statements is the responsibility of the HSBC Bank Malaysia Berhad's directors.

It is our responsibility to form an independent opinion, based on our audit, on the financial statements and to report our opinion to you, as a body, in accordance with Section 174 of the Companies Act, 1965 and for no other purpose. We do not assume responsibility to any other person for the content of this report.

We conducted our audit in accordance with approved Standards on Auditing in Malaysia. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Directors, as well as evaluating the overall financial statements presentation. We believe our audit provides a reasonable basis for our opinion.

In our opinion:

- (a) the financial statements are properly drawn up in accordance with the provisions of the Companies Act, 1965 and applicable approved accounting standards for entities other than private entities issued by the Malaysian Accounting Standards Board as modified by Bank Negara Malaysia's guidelines so as to give a true and fair view of:
 - i) the state of affairs of the Bank and of the group at 31 December 2006 and the results of their operations and cash flows for the year ended on that date; and
 - ii) the matters required by Section 169 of the Companies Act, 1965 to be dealt with in the financial statements of the Bank and the group;

and

- (b) the accounting and other records and the registers required by the Companies Act, 1965 to be kept by the Bank and its subsidiaries have been properly kept in accordance with the provisions of the said Act.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
AND ITS SUBSIDIARY COMPANIES
(Incorporated in Malaysia)

Report of the Auditors (continued)

We are satisfied that the financial statements of the subsidiary companies that have been consolidated with the Bank's financial statements are in form and content appropriate and proper for the purposes of the preparation of the consolidated financial statements and we have received satisfactory information and explanations required by us for those purposes.

Our audit reports on the financial statements of the subsidiary companies were not subject to any qualification and did not include any comment made under Sub-section (3) of Section 174 of the Act.

KPMG
Firm Number: AF 0758
Chartered Accountants

SIEW CHIN KIANG @ SEOW CHIN KIANG
Partner
Approval Number: 2012/11/08(J)

Kuala Lumpur, Malaysia
29 January 2007

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
(Incorporated in Malaysia)

BALANCE SHEET AS AT 31 DECEMBER 2006

	<i>Note</i>	<i>Group</i>		<i>Bank</i>	
		2006	2005	2006	2005
		RM'000	RM'000	RM'000	RM'000
Assets					
Cash and short term funds	2	6,114,345	7,710,602	6,114,345	7,710,602
Securities purchased under resale agreements		2,273,539	1,449,760	2,273,539	1,449,760
Deposits and placements with banks and other financial institutions	3	1,989,882	479,942	1,989,882	479,942
Securities held-for-trading	4	795,937	703,727	795,937	703,727
Securities available-for-sale	5	3,806,463	3,284,735	3,806,463	3,284,735
Loans, advances and financing	6	24,343,937	21,476,706	24,343,937	21,476,706
Other assets	8	578,089	371,825	578,089	371,825
Statutory deposits with Bank Negara Malaysia	9	698,648	698,948	698,648	698,948
Investments in subsidiary companies	10	-	-	21	21
Property, plant and equipment	11	303,387	304,916	303,387	304,916
Intangible assets	12	29,172	5,228	29,172	5,228
Deferred tax assets	13	69,330	56,809	69,330	56,809
Total Assets		<u>41,002,729</u>	<u>36,543,198</u>	<u>41,002,750</u>	<u>36,543,219</u>
Liabilities					
Deposits from customers	14	31,822,208	28,317,351	31,822,229	28,317,372
Deposits and placements of banks and other financial institutions	15	1,934,326	1,954,799	1,934,326	1,954,799
Obligations on securities sold under repurchase agreements		1,660,739	1,617,617	1,660,739	1,617,617
Bills and acceptances payable		490,055	475,940	490,055	475,940
Other liabilities	16	1,351,441	942,517	1,351,441	942,517
Recourse obligation on loans sold to Cagamas Berhad		899,751	787,931	899,751	787,931
Provision for taxation and zakat	17	31,278	29,716	31,278	29,716
Total liabilities		<u>38,189,798</u>	<u>34,125,871</u>	<u>38,189,819</u>	<u>34,125,892</u>
Shareholders' Fund					
Share capital	18	114,500	114,500	114,500	114,500
Reserves	19	2,448,431	2,152,827	2,448,431	2,152,827
Proposed dividend		250,000	150,000	250,000	150,000
Shareholders' funds		<u>2,812,931</u>	<u>2,417,327</u>	<u>2,812,931</u>	<u>2,417,327</u>
Total Liabilities and Shareholders' Funds		<u>41,002,729</u>	<u>36,543,198</u>	<u>41,002,750</u>	<u>36,543,219</u>
Commitments and Contingencies	30	<u>60,087,067</u>	<u>47,716,860</u>	<u>60,087,067</u>	<u>47,716,860</u>

The financial statements were approved and authorised for issue by the Board of Directors on 29 January 2007.

The accompanying Notes form an integral part of the Financial Statements.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
(Incorporated in Malaysia)

INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2006

	<i>Note</i>	<i>Group and Bank</i>	
		2006	2005
		RM'000	RM'000
Revenue		2,831,088	2,235,580
Interest income	20	1,763,687	1,443,345
Interest expense	21	(773,254)	(636,281)
Net interest income		990,433	807,064
Other operating income	22	761,855	623,263
Income from Islamic banking operations	39 (i)	178,801	107,888
Operating income		1,931,089	1,538,215
Other operating expenses	23	(875,215)	(791,255)
Profit before allowance		1,055,874	746,960
Allowance for losses on loans and financing	25	(106,812)	(10,282)
Profit before taxation and zakat		949,062	736,678
Taxation and zakat	26	(261,656)	(211,865)
Profit attributable to shareholders		687,406	524,813
Earnings per RM0.50 share			
- basic / diluted	27	300.2 sen	229.2 sen
Dividends per RM0.50 ordinary share (net)			
- interim dividend paid		65.5 sen	52.4 sen
- proposed		109.2 sen	65.5 sen
		174.7 sen	117.9 sen

The accompanying Notes form an integral part of the Financial Statements.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
(Incorporated in Malaysia)

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2006

		<i>Group and Bank</i>								
		← Non-distributable				→ Distributable				
<i>Note</i>	<i>Share capital</i>	<i>Share premium</i>	<i>Statutory reserve</i>	<i>Revaluation reserve</i>	<i>Capital redemption reserve</i>	<i>Available-for-sale reserve</i>	<i>Retained profits</i>	<i>Total reserves</i>	<i>Proposed dividend</i>	<i>Total</i>
	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
Balance as at 1 January 2005										
- as previously reported	114,500	741,375	114,500	118,966	190,000	56,671	728,155	1,949,667	100,000	2,164,167
- prior year adjustment	37	-	-	-	-	-	(10,381)	(10,381)	-	(10,381)
	114,500	741,375	114,500	118,966	190,000	56,671	717,774	1,939,286	100,000	2,153,786
Net profit for the year										
- as previously reported	-	-	-	-	-	-	533,685	533,685	-	533,685
- prior year adjustment	37	-	-	-	-	-	(8,872)	(8,872)	-	(8,872)
Net gains and losses not recognised in the income statement										
- Net unrealised losses on revaluation	-	-	-	-	-	(23,635)	-	(23,635)	-	(23,635)
Net gains reclassified to income statement	-	-	-	-	-	(17,637)	-	(17,637)	-	(17,637)
Dividend paid - 2004 final	-	-	-	-	-	-	-	-	(100,000)	(100,000)
Dividend paid - 2005 interim	-	-	-	-	-	-	(120,000)	(120,000)	-	(120,000)
Proposed dividend - 2005 final	-	-	-	-	-	-	(150,000)	(150,000)	150,000	-
Balance as at 31 December 2005	114,500	741,375	114,500	118,966	190,000	15,399	972,587	2,152,827	150,000	2,417,327
Balance as at 1 January 2006	114,500	741,375	114,500	118,966	190,000	15,399	972,587	2,152,827	150,000	2,417,327
Net profit for the year	-	-	-	-	-	-	687,406	687,406	-	687,406
Net gains and losses not recognised in the income statement										
- Net unrealised gains on revaluation	-	-	-	-	-	15,388	-	15,388	-	15,388
Net gains reclassified to income statement	-	-	-	-	-	(7,190)	-	(7,190)	-	(7,190)
Dividend paid - 2005 final	-	-	-	-	-	-	-	-	(150,000)	(150,000)
Dividend paid - 2006 interim	-	-	-	-	-	-	(150,000)	(150,000)	-	(150,000)
Proposed dividend - 2006 final	-	-	-	-	-	-	(250,000)	(250,000)	250,000	-
Balance as at 31 December 2006	114,500	741,375	114,500	118,966	190,000	23,597	1,259,993	2,448,431	250,000	2,812,931

The accompanying Notes form an integral part of the Financial Statements.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
(Incorporated in Malaysia)

CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2006

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Cash Flows from Operating Activities		
Profit before taxation and zakat	949,062	736,678
Adjustments for :		
Property, plant and equipment written off	2,298	440
Intangible assets written off	79	5
Depreciation of property, plant and equipment	28,255	28,139
Amortisation of intangible assets	5,762	2,783
Net gain on disposal of property, plant and equipment	(379)	(696)
Dividend income	(2,253)	(2,991)
Operating profit before changes in operating assets	982,824	764,358
(Increase)/ Decrease in operating assets		
Securities purchased under resale agreements	(823,779)	211,921
Deposits and placements with banks and other financial institutions	(1,509,940)	(373,763)
Securities held-for-trading	(92,210)	167,474
Loans, advances and financing	(2,867,231)	(2,512,915)
Other assets	(206,264)	(72,968)
Statutory deposits with Bank Negara Malaysia	300	64,000
Increase/ (Decrease) in operating liabilities		
Deposits from customers	3,504,857	1,760,666
Deposits and placements of banks and other financial institutions	(20,473)	522,463
Obligations on securities sold under repurchase agreements	43,122	(194,488)
Bills and acceptances payable	14,115	143,038
Other liabilities	408,924	315,227
Recourse obligation on loans sold to Cagamas Berhad	111,820	157,743
Net cash (used in)/ generated from operating activities before income tax	(453,935)	952,756
Taxes and zakat paid	(275,803)	(226,513)
Net cash (used in)/ generated from operating activities	(729,738)	726,243
Cash Flows from Investing Activities		
Purchase of property, plant and equipment	(31,319)	(40,195)
Purchase of intangible assets	(29,785)	(2,860)
Proceeds from disposal of property, plant and equipment	2,674	1,961
Securities available-for-sale	(510,342)	1,475,044
Dividend received	2,253	2,991
Net cash (used in)/ generated from investing activities	(566,519)	1,436,941
Cash Flows from Financing Activities		
Dividends paid	(300,000)	(220,000)
Net cash used in financing activities	(300,000)	(220,000)
Net (decrease)/ increase in Cash and Cash Equivalents	(1,596,257)	1,943,184
Cash and Cash Equivalents at beginning of year	7,710,602	5,767,418
Cash and Cash Equivalents at end of year	6,114,345	7,710,602
Analysis of Cash and Cash Equivalents		
Cash and short-term funds	6,114,345	7,710,602

The accompanying Notes form an integral part of the Financial Statements.

HSBC BANK MALAYSIA BERHAD
(Company No. 127776-V)
(Incorporated in Malaysia)

Notes to the Financial Statements as at 31 December 2006

1 Summary of Significant Accounting Policies

The accounting policies adopted by the Group and the Bank are consistent with those adopted in the previous years except for the adoption of the new and revised Financial Reporting Standards (FRS) issued by the Malaysian Accounting Standards Boards (MASB) that are effective for accounting periods beginning on or after 1 January 2006 or available for early adoption.

In this set of financial statements, the Group and the Bank have chosen not to early adopt the following FRSs:

FRS 117	Leases, which is effective for financial periods beginning on or after 1 October 2006.
FRS 124	Related Party Disclosure, which is effective for financial periods beginning on or after 1 October 2006.
FRS 139	Financial Instruments: Recognition and Measurement, for which the MASB has yet to announce the effective date of the standard.

The impact of applying FRS 117 Leases, FRS 124 Related Party Disclosure and FRS 139 Financial Instruments: Recognition and Measurement on this financial statements upon first adoption of the standards as required by paragraph 30 (b) of FRS 108 Accounting Policies, Changes in Accounting Estimates and Errors are not required to be disclosed by virtue of exemptions provided under paragraph 67B of FRS 117, paragraph 22A under FRS 124 and paragraph 103AB of FRS 139 respectively.

The adoption of these new and revised FRS do not have any significant financial impact on the Group and the Bank except for FRS 2 Share Based Payment. The principal effect of the changes in accounting policies resulting from the adoption of FRS 2 is disclosed in Note 37.

1 Summary of Significant Accounting Policies

(a) Basis of Preparation of the Financial Statements

The financial statements of the Bank have been prepared under the historical cost basis unless otherwise indicated; and in accordance with the provisions of the Companies Act, 1965 and applicable approved accounting standards for entities other than private entities issued by the Malaysian Accounting Standards Board as modified by Bank Negara Malaysia's guidelines.

The financial statements incorporate those activities relating to Islamic Banking which have been undertaken by the Bank. Islamic Banking refers generally to the acceptance of deposits and granting of financing under the Shariah principles.

In the preparation of the financial statements, management has been required to make judgements, estimates and assumptions that affect the application of accounting policies and in the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the financial statements in the period in which the estimate is revised and in any future periods affected.

Significant areas of estimation uncertainty and critical judgements used in applying accounting policies that have significant effect on the amount recognized in the financial statements include the following :-

- i. Estimation of recoverable amount based on the discounted cashflow methodology for impaired loan (Notes 1 (j), 7(ii) and 25).
- ii. Fair value estimation of financial assets and liabilities (Note 33)

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

(b) Basis of Consolidation

The group financial statements include the financial statements of the Bank and its subsidiary companies.

The results of subsidiary companies acquired or incorporated during the financial year are included in the group income statement from the dates of acquisition or incorporation.

All significant intercompany transactions and balances have been eliminated on consolidation.

(c) Revenue

Revenue comprises gross interest income, fee income, dealing income, investment income and other income derived from banking operations.

1 Summary of Significant Accounting Policies (continued)

(d) Recognition of Interest and Expense / Islamic Financing Income and Expense

Interest income and expense for all interest-bearing financial instruments except those classified as held-for-trading are recognised in 'interest income' and 'interest expense' in the income statement using the effective interest rates of the financial assets or financial liabilities to which they relate.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability, or where appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument but not future credit losses. The calculation includes all amounts paid or received by the Bank that are an integral part of the effective interest rate, including transaction costs and all other premiums or discounts.

Where an amount is classified as non-performing, interest accrued and recognised as income prior to the date the loan is classified as non-performing shall be reversed out of income by debiting the interest income in the income statement and crediting the accrued interest receivable account in the balance sheet. Subsequently, interest earned on non-performing loans shall be recognised as income on a cash basis. Customers' accounts are classified as non-performing where repayments are in arrears for more than three months for all loans, advances and financing.

Income from Islamic banking operations and attributable profits on deposits and borrowings on activities relating to Islamic banking operations are recognised on an accrual basis in accordance with the principles of Shariah.

(e) Recognition of Fees and Other Income

The Bank earns fee income from a diverse range of services it provides to its customers. Fee income is accounted for as follows:

- if the income is earned on the execution of a significant act, it is recognised as revenue when the significant act has been completed (for example, fees arising from negotiating, or participating in the negotiation of, a transaction for a third party, such as the arrangement for the acquisition of shares or other securities);
- if the income is earned as services are provided, it is recognised as revenue as the services are provided (for example, portfolio and other management advisory and service fee); and
- if the income is an integral part of the effective interest rate of a financial instrument, it is recognised as an adjustment to the effective interest rate (for example, loan commitment fees) and recorded in 'interest income' (see Note 1 (d)).

Dividend income from equity securities is recognised when the right to receive payment is established.

1 Summary of Significant Accounting Policies (continued)

(f) Cash and Cash Equivalents

For the purpose of the cash flow statement, cash and cash equivalents comprise cash and bank balances, and short term deposits and placements maturing within one month that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value.

(g) Resale and Repurchase Agreements

Securities purchased under resale agreements are securities which the Bank had purchased with a commitment to resell at future date. The commitment to resell the securities is reflected as an asset on the balance sheet.

Conversely, obligation on securities sold under repurchase agreements are securities which the Bank had sold from its portfolio, with a commitment to repurchase at future dates. Such financing transactions and the obligation to repurchase the securities are reflected as a liability on the balance sheet.

(h) Securities

The holdings of securities portfolio of the Bank are classified based on the following categories and valuation methods:

i Held for trading

Securities are classified as held for trading if acquired principally for the purpose of selling or repurchasing it in the near term or are part of a portfolio of identified securities that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Securities classified as held for trading are stated at fair value and any gains or losses from a change in the fair value, together with related interest income, are recognised within 'Other operating income' in the income statement.

ii Held-to-maturity

Held-to-maturity investments are securities with fixed or determinable payments and fixed maturities that the Bank has the positive intention and ability to hold until maturity. These investments are initially recorded at fair value plus any directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest rate method, less any impairment losses.

1 Summary of Significant Accounting Policies (continued)

(h) Securities (continued)

iii Available-for-sale

Available-for-sale securities are securities that are not classified as held for trading or held-to-maturity investments; and measured at fair value. Investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are stated at cost. Changes in the fair value are recognised directly in equity, net of applicable taxes, until the securities are either sold or impaired. On the sale of available-for-sale securities, cumulative gains or losses previously recognised in equity are recognised through income statement. Interest income is recognised on such securities using the effective interest method, calculated over the asset's expected life. Where dated available-for-sale securities have been purchased at a premium or discount, these premiums and discounts are included in the calculation of the effective interest rate. Dividends on available-for-sale equity instruments are recognised in the income statement when the right to receive payment is established.

An assessment is made at each balance sheet date as to whether there is any objective evidence of impairment, being circumstances where an adverse impact on estimated future cash flows of the securities or group of securities can be reliably measured.

If an available-for-sale security is determined to be impaired, the cumulative loss that had been recognised directly in equity shall be removed from equity and recognised in the income statement. The amount of cumulative loss is measured as the difference between the acquisition cost (net of any principal repayment and amortisation) and the current fair value, less any impairment loss on that security previously recognised in the income statement. If, in subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, that portion of impairment loss is reversed through the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement.

For loans converted into debt or equity instruments classified as available-for-sale, these instruments are measured at fair value. The difference between the net book value of the restructured loans (outstanding amount of loans net of specific allowance) and the fair value of the debt or equity instruments will be gain or loss from the conversion scheme.

- Where the net book value of the restructured loans is higher than the fair value of the debt or equity instruments, the loss shall be recognised in income statement in the current reporting period.
- Where the fair value of the debt or equity instruments is higher than the net book value of the restructured loans, the gain from the conversion exercise is transferred to the "impairment loss" account, which would be netted off from the "Securities" account in the balance sheet.

(i) Loans, Advances and Financing

Loans, advances and financing include loans and advances originated from the Bank, which are not intended to be sold in the short term and have not been classified as held for trading. Loans, advances and financing are recognised when cash is advanced to borrowers. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method, less impairment losses.

1 Summary of Significant Accounting Policies (continued)

(j) Allowance for Losses on Loans and Financing/ Loan Impairment

The Bank's allowance for non-performing loans and financing is in conformity with the requirements of Bank Negara Malaysia's "Guidelines on the Suspension of Interest on Non-Performing Loans and Provision for Bad and Doubtful Debts, BNM/GP3". Accounts are classified as non-performing when interest or principal is in arrears for more than ninety (90) days.

Specific allowances are made for doubtful debts and financing which have been individually reviewed and specifically identified as bad or doubtful.

A general allowance based on a percentage of the loan and financing portfolio is also made to cover possible losses which are not specifically identified.

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

Impaired loans are measured at their estimated recoverable amount based on the discounted cash flow methodology. Specific allowances are provided if the recoverable amount (present value of estimated future cash flows discounted at original effective interest rate) is lower than the net book value of the loans (outstanding amount of loans, advances and financing, net of specific allowance). The expected cash flows are based on projections of liquidation proceeds, realisation of assets or estimates of future operating cash flows.

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

In addition, the Bank makes additional specific allowance as follows:

- i fifty per cent (50%) of the secured portion of non-performing loans which are in arrears for more than five (5) years but less than seven (7) years; and
- ii hundred per cent (100%) of the secured portion of non-performing loans which are in arrears for more than seven (7) years.

(k) Investment in Subsidiary Companies

A subsidiary company is a company in which the Bank controls the composition of its board of directors or holds more than half of its voting power, or holds more than half of its issued ordinary share capital.

Investment in subsidiary companies are stated at cost, less impairment losses if any.

1 Summary of Significant Accounting Policies (continued)

(l) Property, Plant and Equipment

Property plant and equipment are stated at cost/valuation less accumulated depreciation and accumulated impairment losses except for freehold land which is stated at cost and directors' valuation.

i Revaluation

Land and buildings are revalued once every five years and at shorter intervals whenever the fair value of the revalued assets is expected to differ materially from their carrying value.

Surpluses arising from revaluation are dealt with in the property revaluation reserve account. Any deficit arising is offset against the revaluation reserve to the extent of a previous increase for the same property. In all other cases, a decrease in carrying amount is charged to the income statement.

ii Depreciation

Freehold land is not depreciated. Depreciation of other property, plant and equipment is calculated to write off the cost of the property, plant and equipment on a straight line basis over the expected useful lives of the assets concerned. The principal annual rates are:

Buildings on freehold land	50 years
Leasehold land with more than fifty (50) years to expiry and buildings thereon	50 years
Leasehold land with less than fifty (50) years to expiry and buildings thereon	Over the unexpired period of the lease
Office equipment, fixtures and fittings	5 to 10 years
Computer equipment	3 to 5 years
Motor vehicles	5 years

With the exception of properties, additions to property, plant and equipment costing RM1,000 and under are fully depreciated in the year of purchase; for those assets costing more than RM1,000, depreciation is provided at the above rates.

During the year, the Bank revised the annual depreciation rates of computer equipment to be 3 to 5 years (2005: 5 years) and fully depreciated additions to property, plant and equipment costing RM1,000 (2005: RM500) in the year of purchase so as to better reflect their estimated useful lives. The revision was accounted for as a change in accounting estimates, which is applied prospectively. The change in accounting estimates has no material impact on the financial statements.

(m) Intangible Assets

Intangible assets represent computer software and are stated at cost less amortisation and accumulated impairment losses. Amortisation of intangible assets is calculated to write off the cost of the intangible assets on a straight line basis over the expected useful lives of 3 to 5 years.

(n) Bills and Acceptances Payable

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

1 Summary of Significant Accounting Policies (continued)

(o) *Recourse Obligation on Loans Sold to Cagamas Berhad*

In the normal course of banking operations, the Bank sells loans to Cagamas Berhad. The Bank is liable in respect of the loans sold directly to Cagamas Berhad under the condition that the Bank undertakes to administer the loans on behalf of Cagamas Berhad and to buy back any loans which are regarded as defective based on prudence. Such financing transactions and the obligation to buy back the loans is reflected as a liability on the balance sheet.

(p) *Taxation and Deferred Taxation*

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

Current tax expense is the expected tax payable on the taxable income for the year, calculated using tax rates enacted or substantially enacted by the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the balance sheet. Temporary differences are not recognised for the initial recognition of assets or liabilities that at the time of the transaction affects neither accounting nor taxable profit. The amount of deferred tax provided is based on the expected manner or realisation of settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted by the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

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

(q) *Derivatives and Hedge Accounting*

Derivatives are recognised initially, and are subsequently remeasured, at fair value. Fair values are obtained from quoted market prices in active markets, or by using valuation techniques, including recent market data, where an active market does not exist. Valuation techniques include discounted cash flow models and option pricing models as appropriate. All derivatives are classified as assets when their fair value is positive, or as liabilities when their fair value is negative. All gains and losses from changes in the fair value of derivatives held for trading are recognised in the income statement.

The accounting for changes (i.e. gains and losses) in the fair value of a derivative which qualifies for hedge accounting depends on the intended use of the derivative and the resulting designation as described below:

1 Summary of Significant Accounting Policies (continued)

(q) Derivatives and Hedge Accounting - continued

i Fair value hedge

For a derivative designated as hedging the exposures in the fair value of a recognised asset or liability or a firm commitment, the gain or loss is recognised in the income statement, together with the associated loss or gain on the hedged item attributable to the hedged risk.

ii Cash flow hedge

For a derivative designated as hedging the exposure to variable cash flows of a recognised asset or liability, or of a highly probable forecast transaction, the gain or loss on the derivative associated with the effective portion of the hedged is recognised in equity. Any gain or loss relating to an in-effective portion is recognised immediately in the income statement.

(r) Currency Translations

Individual foreign currency assets and liabilities are stated in the balance sheet at spot rates of exchange which closely approximate those ruling at the balance sheet date. Income statement items are translated at rates prevailing on transaction dates. Exchange gains and losses are recognised in the income statement in the year they arise.

(s) Provisions

A provision is recognised when it is probable that an outflow of resources embodying economic benefits will be required to settle a present legal or constructive obligation as a result of a past event and a reliable estimate can be made of the amount of the obligation.

(t) Profit Equalisation Reserves ('PER')

PER refers to the amount appropriated out of the total Islamic Banking gross income in order to maintain an acceptable level of return to depositors as stipulated by Bank Negara Malaysia's "The Framework of Rate of Return". PER is a provision shared by both the depositors and the Bank, and is deducted from the total gross income. Maximum monthly provision of PER is up to 15% of the gross income and can be accumulated up to a maximum of 30% of Islamic Banking Capital Funds.

(u) Employee Benefits

i Short term employee benefits

Wages, salaries, bonuses, paid annual and sick leave, social security contributions and non-monetary benefits are accrued in the period in which the associated services are rendered by the employees of the Bank.

ii Post-employment benefits

As required by law, the Bank makes contributions to the Employees Provident Fund ('EPF'), the national defined contribution plan and recognises such contributions as an expense in the income statement as incurred. Once the contributions have been paid, the Bank has no further payment obligations in future.

2 Cash and Short Term Funds

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Cash and balances with banks and other financial institutions	720,397	414,406
Money at call and deposit placements maturing within one month	5,393,948	7,296,196
	6,114,345	7,710,602

3 Deposits and Placements with Banks and Other Financial Institutions

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Licensed finance companies	35,275	-
Licensed merchant banks	17,507	22,147
Bank Negara Malaysia	1,937,100	420,000
Other financial institutions	-	37,795
	1,989,882	479,942

4 Securities Held-for-Trading

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Money market instruments:		
Malaysian Government treasury bills	116,400	39,256
Bank Negara Malaysia bills	202,738	231,566
Bank Negara Malaysia Islamic bills	14,887	7,875
Malaysian Government securities	213,998	222,765
Malaysian Government Islamic bonds	23,361	-
Khazanah bonds	11,404	2,021
Cagamas bonds and notes	4,745	31,513
	587,533	534,996
Unquoted securities:		
Private debt securities (including commercial paper)	208,404	168,731
	795,937	703,727

5 Securities Available-for-Sale

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Money market instruments:		
Malaysian Government treasury bills	30,794	-
Malaysian Government Islamic treasury bills	39,408	-
Bank Negara Malaysia bills	-	49,309
Bank Negara Malaysia Islamic bills	-	308,442
Malaysian Government securities	574,899	467,581
Malaysian Government Islamic bonds	579,980	21,811
Khazanah bonds	262,200	243,958
Cagamas bonds and notes	841,168	691,864
Negotiable instruments of deposit	477,020	554,847
Bankers' acceptance and Islamic accepted bills	531,279	143,326
	3,336,748	2,481,138
Quoted securities:		
Shares	20,340	36,764
Warrants	-	148
Loan stock	12,492	15,173
	32,832	52,085
Unquoted securities:		
Shares	28,572	17,392
Private and Islamic debt securities	420,895	754,322
	449,467	771,714
Impairment loss:		
Quoted securities in Malaysia:		
Shares	(5,701)	(11,291)
Warrants	-	(7)
Loan stock	(6,883)	(8,904)
	(12,584)	(20,202)
	3,806,463	3,284,735

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

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Maturing within one year	1,721,614	1,452,480
One year to three years	1,572,311	952,869
Three years to five years	42,823	75,709
Over five years	-	80
	3,336,748	2,481,138

6 Loans, Advances and Financing

(i) By type

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Overdrafts	1,489,375	1,618,309
Term loans/ financing		
Housing loans/ financing	8,569,510	7,885,225
Syndicated term loans/ financing	41,277	19,695
Hire purchase receivables	191,050	111,690
Lease receivables	30,854	49,740
Other term loans/ financing	6,395,016	5,515,035
Bills receivable	1,093,859	772,852
Trust receipts	412,583	180,166
Claims on customers under acceptance credits	2,717,235	3,109,050
Staff loans/ financing	312,700	307,157
Loans to executive directors	232	-
Credit/ charge cards	2,017,522	1,616,357
Revolving credit	1,848,250	1,072,172
Other loans/ financing	12,285	10,722
Less: Unearned interest and income	(142,816)	(141,321)
	24,988,932	22,126,849
Less: Allowance for bad and doubtful debts and financing:		
- General	(372,600)	(327,200)
- Specific	(272,395)	(322,943)
Total net loans, advances and financing	24,343,937	21,476,706

(ii) By type of customer

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Domestic non-bank financial institutions		
- Stockbroking companies	150,087	5,238
- Others	162,927	141,425
Domestic business enterprises		
- Small medium enterprises	4,338,440	2,655,201
- Others	7,093,461	7,584,366
Government and statutory bodies	46	64
Individuals	12,798,944	11,144,011
Other domestic entities	3,508	2,754
Foreign entities	441,519	593,790
	24,988,932	22,126,849

(iii) By interest/ profit rate sensitivity

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Fixed rate		
Housing loans/ financing	307,762	328,417
Hire purchase receivables	169,720	102,190
Other fixed rate loans/ financing	5,399,982	3,711,654
Variable rate		
BLR plus	15,245,696	13,978,020
Cost-plus	1,848,250	1,073,903
Other variable rates	2,017,522	2,932,665
	24,988,932	22,126,849

6 Loans, Advances and Financing (continued)

(iv) By sector

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Agricultural, hunting, forestry and fishing	999,703	893,313
Mining and quarrying	191,676	99,672
Manufacturing	4,569,025	3,739,427
Electricity, gas and water	134,452	81,383
Construction	452,645	428,685
Real estate	635,859	545,809
Purchase of landed property:		
- Residential	8,953,961	8,384,960
- Non-residential	1,019,027	970,920
Wholesale & retail trade and restaurants & hotels	2,296,170	2,164,107
Transport, storage and communication	174,796	190,842
Finance, insurance and business services	1,332,493	1,347,020
Purchase of securities	115,595	173,523
Purchase of transport vehicles	34,284	17,560
Consumption credit	3,765,751	2,894,133
Others	313,495	195,495
	24,988,932	22,126,849

(v) By maturity structure

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Maturing within one year	12,772,516	9,843,898
One year to three years	1,711,717	1,596,418
Three years to five years	2,197,706	1,732,472
Over five years	8,306,993	8,954,061
	24,988,932	22,126,849

7 Non-Performing Loans/ Financing (NPL/ NPF)

(i) Movements in non-performing loans, advances and financing

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
At beginning of year	688,626	1,055,888
Classified as non-performing during the year	325,223	314,067
Reclassified as performing	(111,016)	(199,467)
Amount recovered	(176,815)	(275,478)
Amount written off	(188,153)	(207,031)
Other movements	536	647
At end of year	538,401	688,626
Specific allowance	(272,395)	(322,943)
Net non-performing loans, advances and financing	266,006	365,683
Ratio of net non-performing loans, advances and financing to net loans, advances and financing	1.1%	1.7%

7 Non-Performing Loans/ Financing (NPL/ NPF) (continued)

(ii) Movements in allowance for bad and doubtful debts

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
General allowance		
At beginning of year	327,200	289,300
Allowance made during the year	45,400	37,900
At end of year	372,600	327,200
As % of gross loans, advances and financing less specific allowance	1.5%	1.5%
Specific allowance		
At beginning of year	322,943	477,334
Allowance made during the year	224,961	192,822
Amount recovered	(98,275)	(144,029)
Amount written off	(177,770)	(203,831)
Other movements	536	647
At end of year	272,395	322,943

(iii) By sector

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Agricultural, hunting, forestry and fishing	2,190	2,202
Mining and quarrying	541	631
Manufacturing	100,486	185,029
Construction	24,585	31,718
Real estate	16,863	17,589
Purchase of landed property:		
- Residential	226,133	255,725
- Non-residential	20,057	23,088
Wholesale & retail trade and restaurants & hotels	38,191	53,291
Transport, storage and communication	3,224	4,628
Finance, insurance and business services	20,711	28,300
Purchase of securities	362	17,806
Purchase of transport vehicles	170	177
Consumption credit	82,041	65,210
Others	2,847	3,232
	538,401	688,626

8 Other Assets

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Assets, including gains, resulting from off-balance-sheet interest rate, exchange rate and equities contracts which are marked to market	313,578	203,871
Interest/ income receivable	55,658	34,082
Other receivables, deposits and prepayments	208,853	133,872
	578,089	371,825

9 Statutory Deposits with Bank Negara Malaysia

The non-interest bearing statutory deposits are maintained with Bank Negara Malaysia in compliance with Section 37(1)(c) of the Central Bank of Malaysia Act, 1958 (revised 1994), the amounts of which are determined at set percentages of total eligible liabilities.

10 Investments in Subsidiary Companies

	<i>Bank</i>	
	2006	2005
	RM'000	RM'000
Unquoted shares, at cost - in Malaysia	21	21

The subsidiary companies of the Bank are as follows:

<i>Name</i>	<i>Principal activities</i>	<i>Country of incorporation</i>	<i>Percentage of equity held</i>	
			2006	2005
HSBC (Kuala Lumpur) Nominees Sdn Bhd	Nominee company	Malaysia	100%	100%
HSBC Nominees (Tempatan) Sdn Bhd	Nominee company	Malaysia	100%	100%
HSBC Nominees (Asing) Sdn Bhd	Nominee company	Malaysia	100%	100%

All income and expenditure arising from the nominee activities of the subsidiary companies have been recognised in the Bank's results.

11 Property, Plant and Equipment

2006	Group and Bank									Total
	Freehold land	Short term leasehold land	Long term leasehold land	Building on freehold land	Building on short term leasehold land	Building on long term leasehold land	Office equipment, fixtures and fittings	Computer equipment	Motor vehicles	
	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
Cost or valuation										
Balance as at 1 January 2006	76,500	8,261	14,204	127,693	6,139	9,810	135,927	141,465	8,034	528,033
Additions	-	-	-	3,421	-	-	9,363	18,181	354	31,319
Disposals	-	-	-	-	-	-	(872)	(7,732)	(1,775)	(10,379)
Written off	-	-	-	(541)	(92)	(447)	(7,931)	(47,212)	-	(56,223)
Reclassification	-	-	-	-	-	-	(3,093)	3,093	-	-
	76,500	8,261	14,204	130,573	6,047	9,363	133,394	107,795	6,613	492,750
Representing items at:										
Cost	-	-	-	4,203	-	-	133,394	107,795	6,613	252,005
Valuation - 2004	76,500	8,261	14,204	126,370	6,047	9,363	-	-	-	240,745
	76,500	8,261	14,204	130,573	6,047	9,363	133,394	107,795	6,613	492,750
Accumulated depreciation										
Balance as at 1 January 2006	-	199	287	2,595	201	200	111,460	105,615	2,560	223,117
Charge for the year	-	199	286	2,979	201	197	9,921	13,007	1,465	28,255
Disposals	-	-	-	-	-	-	(853)	(6,327)	(904)	(8,084)
Written off	-	-	-	(300)	(60)	(249)	(7,745)	(45,571)	-	(53,925)
Reclassification	-	-	-	-	-	-	(1,536)	1,536	-	-
Balance as at 31 December 2006	-	398	573	5,274	342	148	111,247	68,260	3,121	189,363
Net book value at 31 December 2006	76,500	7,863	13,631	125,299	5,705	9,215	22,147	39,535	3,492	303,387

Had the land and building been carried at historical cost less accumulated depreciation, the carrying amount of the revalued assets that would have been included in the financial statements at the end of the year would be as follows:

2006	18,003	308	2,539	75,181	4,689	7,215	-	-	-	107,935
2005	18,003	318	2,597	74,417	4,912	7,633	-	-	-	107,880

The land and buildings of the Bank were revalued by directors on the open market value basis as of 31 December 2004 based on professional valuations.

11 Property, Plant and Equipment (continued)

2005	<i>Group and Bank</i>									
	<i>Freehold land</i>	<i>Short term leasehold land</i>	<i>Long term leasehold land</i>	<i>Building on freehold land</i>	<i>Building on short term leasehold land</i>	<i>Building on long term leasehold land</i>	<i>Office equipment, fixtures and fittings</i>	<i>Computer equipment</i>	<i>Motor vehicles</i>	<i>Total</i>
	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
Cost or valuation										
Balance as at 1 January 2005	76,500	8,261	14,204	126,911	6,139	9,810	130,015	127,238	8,058	507,136
Additions	-	-	-	782	-	-	15,277	21,820	2,316	40,195
Disposals	-	-	-	-	-	-	(1,510)	(1,011)	(2,281)	(4,802)
Written off	-	-	-	-	-	-	(7,855)	(6,582)	(59)	(14,496)
Balance as at 31 December 2005	76,500	8,261	14,204	127,693	6,139	9,810	135,927	141,465	8,034	528,033
Representing items at:										
Cost	-	-	-	782	-	-	135,927	141,465	8,034	286,208
Valuation - 2004	76,500	8,261	14,204	126,911	6,139	9,810	-	-	-	241,825
	76,500	8,261	14,204	127,693	6,139	9,810	135,927	141,465	8,034	528,033
Accumulated depreciation										
Balance as at 1 January 2005	-	-	-	-	-	-	110,149	99,564	2,904	212,617
Charge for the year	-	199	287	2,595	201	200	9,700	13,303	1,654	28,139
Disposals	-	-	-	-	-	-	(663)	(935)	(1,939)	(3,537)
Written off	-	-	-	-	-	-	(7,726)	(6,317)	(59)	(14,102)
Balance as at 31 December 2005	-	199	287	2,595	201	200	111,460	105,615	2,560	223,117
Net book value at 31 December 2005	76,500	8,062	13,917	125,098	5,938	9,610	24,467	35,850	5,474	304,916

12 Intangible Assets

	<i>Group and Bank</i>
2006	<i>Computer software</i>
	RM'000
Cost	
Balance as at 1 January 2006	23,538
Additions	29,785
Written off	(1,214)
Balance as at 31 December 2006	<u>52,109</u>
Accumulated depreciation	
Balance as at 1 January 2006	18,310
Charge for the year	5,762
Written off	(1,135)
Balance as at 31 December 2006	<u>22,937</u>
Net book value at 31 December 2006	<u>29,172</u>
2005	RM'000
Cost	
Balance as at 1 January 2005	20,900
Additions	2,860
Written off	(222)
Balance as at 31 December 2005	<u>23,538</u>
Accumulated depreciation	
Balance as at 1 January 2005	15,698
Charge for the year	2,783
Written off	(171)
Balance as at 31 December 2005	<u>18,310</u>
Net book value at 31 December 2005	<u>5,228</u>

13 Deferred Tax

The amounts, determined after appropriate offsetting, are as follows:

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Deferred tax liabilities	(43,525)	(40,351)
Deferred tax assets	112,855	97,160
	69,330	56,809

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

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

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Property, plant and equipment		
- capital allowances	(9,893)	(9,443)
- revaluation	(24,455)	(24,919)
Available-for-sale reserve	(9,177)	(5,989)
Allowances		
- general allowance	104,328	91,616
- others	2,210	1,074
Share based payment	5,345	3,262
Lease receivables	972	1,208
	69,330	56,809

13 Deferred tax (continued)

Movement in temporary differences during the year

Group and Bank

	<i>As at 01-Jan-05</i>	<i>Recognised in income statement</i>	<i>Recognised in equity</i>	<i>Restated at 31-Dec-05</i>	<i>Recognised in income statement</i>	<i>Recognised in equity</i>	<i>As at 31-Dec-06</i>
	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
Property, plant and equipment							
- capital allowance	(9,085)	(358)	-	(9,443)	(450)	-	(9,893)
- revaluation	(25,207)	288	-	(24,919)	464	-	(24,455)
Available for sale reserves	(22,039)	-	16,050	(5,989)	-	(3,188)	(9,177)
Allowances							
- general allowances	81,004	10,612	-	91,616	12,712	-	104,328
- others	1,183	(109)	-	1,074	1,136	-	2,210
Share based payments	1,656	1,606	-	3,262	2,083	-	5,345
Lease receivables	1,675	(467)	-	1,208	(236)	-	972
Interest in suspense	26,514	(26,514)	-	-	-	-	-
	55,701	(14,942)	16,050	56,809	15,709	(3,188)	69,330

14 Deposits from Customers

(i) By type of deposit

	<i>Group</i>		<i>Bank</i>	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Demand deposits	6,273,226	5,689,273	6,273,247	5,689,294
Savings deposits	4,734,188	4,243,692	4,734,188	4,243,692
Fixed / Investment deposits	19,147,567	16,400,684	19,147,567	16,400,684
Negotiable instruments of deposit	1,073,968	1,702,320	1,073,968	1,702,320
Others	593,259	281,382	593,259	281,382
	31,822,208	28,317,351	31,822,229	28,317,372

The maturity structure of fixed / investment deposits and negotiable instruments of deposit is as follows:

	<i>Group and Bank</i>	
	2006 RM'000	2005 RM'000
Due within six months	16,060,096	14,544,092
Six months to one year	3,687,742	3,135,727
One year to three years	240,060	248,841
Three years to five years	85,003	26,957
Over five years	148,634	147,387
	20,221,535	18,103,004

(ii) By type of customer

	<i>Group</i>		<i>Bank</i>	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Government and statutory bodies	97,772	15,780	97,772	15,780
Business enterprises	12,195,118	9,532,602	12,195,139	9,532,623
Individuals	15,964,350	14,185,641	15,964,350	14,185,641
Others	3,564,968	4,583,328	3,564,968	4,583,328
	31,822,208	28,317,351	31,822,229	28,317,372

15 Deposits and Placements of Banks and Other Financial Institutions

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Licensed banks	81,000	120,000
Bank Negara Malaysia	18,774	38,247
Other financial institutions	1,834,552	1,796,552
	1,934,326	1,954,799

16 Other Liabilities

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Liabilities, including losses, resulting from off-balance-sheet interest rate, exchange rate and equities contracts which are marked to market	309,747	183,219
Interest/ profit payable	175,082	144,243
Allowance for commitments and contingencies	2,369	3,030
Profit equalisation reserve	4,700	1,700
Other creditors and accruals	859,543	610,325
	1,351,441	942,517

Movement in allowance for commitments and contingencies is as follows:

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
At beginning of year	3,030	2,793
Allowance made during the year	419	1,075
Amount released	(1,077)	(615)
	(658)	460
Other movements	(3)	(223)
At end of year	2,369	3,030

17 Provision for Taxation and Zakat

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Taxation	31,278	29,667
Zakat	-	49
	31,278	29,716

18 Share Capital

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Authorised		
Ordinary shares of RM0.50 each	500,000	500,000
Preference shares of RM0.50 each	500,000	500,000
	1,000,000	1,000,000
Issued and Fully Paid		
Ordinary shares of RM0.50 each	114,500	114,500

19 Reserves

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Share premium	741,375	741,375
Statutory reserve	114,500	114,500
Revaluation reserve	118,966	118,966
Capital redemption reserve	190,000	190,000
Available-for-sale reserve	23,597	15,399
Retained profits	1,259,993	972,587
	2,448,431	2,152,827

The statutory reserve is maintained in compliance with Section 36 of the Banking and Financial Institutions Act, 1989 and is not distributable as cash dividends.

The capital redemption reserve is maintained in compliance with Section 61 of the Companies Act, 1965 arising from the full redemption of RM190 million cumulative redeemable preference shares.

The Bank has sufficient tax credit under Section 108 of the Income Tax Act, 1967 to frank the payment of dividend out of all its retained profits.

20 Interest Income

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Loans and advances		
- Interest income other than recoveries from NPLs	1,337,368	1,062,576
- Recoveries from NPLs	51,077	66,219
Money at call and deposit placement with financial institutions	306,601	208,391
Securities available-for-sale	78,225	119,577
	1,773,271	1,456,763
Amortisation of premium less accretion of discounts	10,007	(1,829)
Interest suspended	(19,591)	(11,589)
Total interest income	1,763,687	1,443,345

21 Interest Expense

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Deposits and placements of banks and other financial institutions	71,188	36,925
Deposits from customers	592,439	517,936
Loans sold to Cagamas	42,379	29,730
Others	67,248	51,690
	773,254	636,281

22 Other Operating Income

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Fees and commissions	372,021	349,573
Net gains arising from sale of securities		
- Securities held-for-trading	29,064	15,733
- Securities available-for-sale	17,369	29,309
Net interest trading income	22,075	16,328
Net gains arising from dealing in foreign currency	266,934	181,692
Net gains arising from trading in derivatives	15,243	5,249
Dividend income from securities available-for-sale		
- Quoted in Malaysia	1,098	1,497
- Unquoted in Malaysia	1,155	1,494
Net unrealised (losses)/gains on revaluation of trading securities (including derivatives)	(3,761)	7,409
Net unrealised (losses)/ gains from foreign exchange translations	(14,565)	5,585
Rental income	6,539	6,147
Net gains on disposal of property, plant and equipment	379	696
Gain from sale of a business operation	35,156	-
Other operating income	13,148	2,551
	761,855	623,263

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

Cards	170,642	173,381
Service charges and fees	103,200	95,809
Agency fees	41,940	35,649
Credit facilities	25,627	18,567

23 Other Operating Expenses

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Personnel expenses	448,935	356,397
Promotion and marketing related expenses	70,862	81,741
Establishment related expenses	92,296	84,509
General administrative expenses	263,122	268,608
	875,215	791,255

The above expenditure includes the following major items / statutory disclosures:

Personnel expenses		
Salaries, allowances and bonuses	334,195	273,972
Employees Provident Fund contributions	53,143	40,617
Directors' remuneration (Note 24)	7,121	7,629
Promotion and marketing related expenses		
Advertising and promotion	43,608	46,700
Commercial sponsorships	6,439	6,748
Establishment related expenses		
Depreciation of property, plant and equipment	28,255	28,139
Amortisation of intangible assets	5,762	2,783
Information technology costs	18,001	19,388
Hire of equipment	8,466	8,679
Rental of premises	10,539	8,072
Property, plant and equipment written off	2,298	440
Intangible assets written off	79	5
General administrative expenses		
Intercompany expenses	149,802	115,229
Fees and commissions paid	35,866	52,630
Auditors' remuneration	325	325

The number of employees of the Bank as at 31 December 2006 was 4,996 (31 December 2005: 4,715).

24 CEO and Directors' Remuneration

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Executive Directors and CEO		
Salary and other remuneration	4,234	4,464
Bonuses	954	1,266
Benefits-in-kind	1,588	1,573
	6,776	7,303
Non-Executive Directors		
Fees	332	315
Other remuneration	13	11
	345	326

24 CEO and Directors' Remuneration (continued)

The number of directors of the Bank whose remuneration including benefits-in-kind for the financial year falls into the following bands:

	<i>Number of Directors</i>	
	2006	2005
Executive Directors		
RM4,300,001 - RM4,350,000	1	-
RM4,200,001 - RM4,250,000	-	1
RM2,450,001 - RM2,500,000	1	-
RM2,050,001 - RM2,100,000	-	1
RM1,000,001 - RM1,050,000	-	1
	2	3
Non-Executive Directors		
RM50,001 - RM100,000	6	6
	6	6

25 Allowance for Losses on Loans and Financing

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Allowance for bad and doubtful debts on loans and financing		
(a) Specific allowance		
- Made in the financial year	224,961	192,822
- Written back	(98,275)	(144,029)
(b) General allowance		
- Made in the financial year	45,400	37,900
Bad debts on loans and financing		
- Recovered	(76,302)	(82,924)
- Written off	11,686	6,053
Allowance for losses on commitments and contingencies		
- Made in the financial year	419	1,075
- Written back	(1,077)	(615)
	106,812	10,282

26 Taxation and Zakat

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Malaysian income tax	283,310	227,000
Deferred tax		
Origination and reversal of temporary differences	(15,709)	(11,572)
Over provision in respect of prior years	(6,000)	(30,126)
Reversal of deductible temporary differences in respect of prior years	-	26,514
	261,601	211,816
Zakat	55	49
	261,656	211,865

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

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Profit before taxation	949,062	736,678
Income tax using Malaysian tax rates (28%)	265,737	206,270
Non-deductible expenses	12,276	9,277
Tax exempt income	(10,412)	(119)
Over provision in respect of prior years	(6,000)	(30,126)
Reversal of deductible temporary differences in respect of prior years	-	26,514
Tax expense	261,601	211,816

27 Earnings per Share

The earnings per ordinary share have been calculated based on the net profit and 229,000,000 (2005:229,000,000) ordinary shares of RM0.50 each in issue during the year.

28 Significant Related Party Transactions and Balances

	2006		2005	
	<i>Parent companies</i> RM'000	<i>Other related companies</i> RM'000	<i>Parent companies</i> RM'000	<i>Other related companies</i> RM'000
Income				
Interest on intercompany placements	-	22,130	-	24,982
Interest on current accounts	-	12,918	-	7,185
Fees and commission	-	10,585	-	8,218
Other income	-	8,551	-	2,267
	<u>-</u>	<u>54,184</u>	<u>-</u>	<u>42,652</u>
Expenditure				
Interest on intercompany deposits	-	33,528	-	13,658
Interest on current accounts	-	29	-	20
Fees and commission	-	3,053	-	1,975
Operating expenses	41,379	108,423	6,513	108,716
	<u>41,379</u>	<u>145,033</u>	<u>6,513</u>	<u>124,369</u>
Amount due from				
Intercompany placements	-	184,408	-	742,698
Current account balances	-	460,673	-	165,697
Other assets	-	12,724	-	5,200
	<u>-</u>	<u>657,805</u>	<u>-</u>	<u>913,595</u>
Amount due to				
Intercompany deposits	-	382,504	-	518,738
Current account balances	-	132,919	-	121,721
Other liabilities	80,408	122,147	25,409	57,895
	<u>80,408</u>	<u>637,570</u>	<u>25,409</u>	<u>698,354</u>

29 Capital Adequacy

	<i>Bank</i>	
	2006 RM'000	2005 RM'000
Tier 1 capital		
Paid-up ordinary share capital	114,500	114,500
Share premium	741,375	741,375
Capital redemption reserve	190,000	190,000
Retained profit	1,509,993	1,122,587
Other reserves	114,500	114,500
	2,670,368	2,282,962
Less: Deferred tax adjustments	(104,554)	(88,845)
Total Tier 1 capital	2,565,814	2,194,117
Tier 2 capital		
Revaluation reserves	72,507	72,507
General allowance for bad and doubtful debts and financing	372,600	327,200
Total Tier 2 capital	445,107	399,707
Total capital	3,010,921	2,593,824
Less: Investment in subsidiaries	(21)	(21)
Capital base	3,010,900	2,593,803
Core capital ratio	10.1%	9.8%
Risk-weighted capital ratio	11.9%	11.6%
Core capital ratio (net of proposed dividend)	9.1%	9.1%
Risk-weighted capital ratio (net of proposed dividend)	10.9%	10.9%

Breakdown of gross risk-weighted assets in the various categories of risk-weights:

	<i>Bank</i>			
	2006		2005	
	Principal RM'000	Risk-weighted RM'000	Principal RM'000	Risk-weighted RM'000
0%	12,062,562	-	10,475,706	-
10%	327,586	32,759	399,528	39,953
20%	3,369,913	673,983	3,158,802	631,760
50%	8,562,107	4,281,053	7,715,056	3,857,528
100%	19,728,370	19,728,370	17,342,260	17,342,260
Total risk-weighted assets equivalent for market risk	-	678,808	-	553,272
	44,050,538	25,394,973	39,091,352	22,424,773

30 Commitments and Contingencies

In the normal course of business, the Bank makes various commitments and incurs certain contingent liabilities with legal recourse to its customers. No material losses are anticipated as a result of these transactions.

The table below shows the contract or underlying principal amounts, credit equivalents amounts and risk weighted amounts of unmatured off-balance sheet transactions as at balance sheet date. The contract or underlying principle amounts indicate the volume of business outstanding and do not represent amount at risk.

	<i>Group and Bank</i>					
	2006			2005		
	Principal amount RM'000	Credit equivalent amount * RM'000	Risk weighted amount RM'000	Principal amount RM'000	Credit equivalent amount * RM'000	Risk weighted amount RM'000
Direct credit substitutes	713,289	713,289	672,985	610,872	610,872	571,773
Transaction-related contingent items	2,413,779	1,206,889	1,155,394	1,883,990	941,995	916,181
Short-term self-liquidating trade-related contingencies	436,088	87,218	71,399	259,019	51,804	46,555
Irrevocable commitments to extend credit:						
- Maturity not exceeding one year	17,263,576	-	-	15,131,142	-	-
- Maturity exceeding one year	915,711	457,856	457,856	1,298,798	649,399	649,399
Foreign exchange related contracts:						
- Less than one year	14,144,291	210,429	78,462	11,751,863	228,029	88,034
- One year to less than 5 years	668,208	52,944	24,917	1,818,966	137,126	54,254
Interest rate related contracts:						
- Less than one year	9,527,856	23,883	7,269	2,768,837	7,667	2,341
- One year to less than 5 years	12,788,488	338,967	134,989	11,166,070	289,349	124,080
- 5 years and above	498,225	30,440	13,673	976,309	60,427	28,417
Others	717,556	186,884	153,087	50,994	12,166	8,835
	60,087,067	3,308,799	2,770,031	47,716,860	2,988,834	2,489,869

* The credit equivalent amount is arrived at using the credit conversion factors as per Bank Negara Malaysia guidelines.

30 Commitments and Contingencies (continued)

	<i>Group and Bank</i>			
	2006		2005	
	Contracted amount RM'000	Fair value RM'000	Contracted amount RM'000	Fair value RM'000
Foreign exchange related contracts				
- forward and future contracts	12,840,173	(1,155)	11,526,475	13,158
- options purchased	411,132	1,968	431,202	17,834
- options written	241,943	(2,237)	428,368	(17,827)
- swaps	1,319,251	1,560	1,184,784	6,704
Interest rate related contracts				
- forward and future contracts	4,706,358	1,504	2,037,078	(895)
- options	2,033,282	(2,495)	2,334,158	(3,122)
- swaps	16,074,929	4,687	10,539,980	4,799

Credit risk

Credit risk arises from the possibility that a counterparty may be unable to meet the terms of a contract in which the Bank has a gain position. As at 31 December 2006, the amount of credit risk, measured in terms of the cost to replace the profitable contracts, was RM280million (As at 31 December 2005: RM203million). This amount will increase or decrease over the life of the contracts, mainly as a function of maturity dates and market rates or prices.

31 Interest/ Profit Rate Risk

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

Bank 2006	← Non-trading book →					Non-interest sensitive RM'000	Trading book RM'000	Effective interest rate %	
	Up to 1 month RM'000	>1 - 3 months RM'000	>3 - 12 months RM'000	1 - 5 years RM'000	Over 5 years RM'000				Total RM'000
ASSETS									
Cash and short term funds	5,803,102	-	-	-	-	311,243	-	6,114,345	3.67
Securities purchased under resale agreements	674,820	806,490	792,229	-	-	-	-	2,273,539	3.60
Deposits and placements with banks and other financial institutions	-	1,972,375	-	17,507	-	-	-	1,989,882	3.68
Securities held for trading	-	-	-	-	-	-	795,937	795,937	3.87
Securities available-for-sale	612,610	527,659	720,049	1,888,479	14,454	43,212	-	3,806,463	3.72
Loans, advances and financing									
- performing	19,461,601	1,902,625	503,647	1,131,363	419,732	658,963	-	24,077,931	6.88
- non-performing *	-	-	-	-	-	266,006	-	266,006	-
Others	-	-	-	-	-	1,349,370	329,277	1,678,647	-
TOTAL ASSETS	26,552,133	5,209,149	2,015,925	3,037,349	434,186	2,628,794	1,125,214	41,002,750	
LIABILITIES AND SHAREHOLDERS' FUNDS									
Deposits from customers	16,226,218	3,497,782	6,033,105	669,024	169,181	5,226,919	-	31,822,229	2.91
Deposits and placements of banks and other financial institutions	1,202,396	297,444	26,614	4,950	2,763	400,159	-	1,934,326	3.33
Obligation on securities sold under repurchase agreements	1,660,739	-	-	-	-	-	-	1,660,739	2.93
Bills and acceptances payable	77,146	60,278	2,984	-	-	349,647	-	490,055	3.27
Recourse obligation on loans sold to Cagamas Berhad	-	-	81,689	818,062	-	-	-	899,751	4.57
Others	-	-	-	-	-	1,052,983	329,736	1,382,719	-
Total Liabilities	19,166,499	3,855,504	6,144,392	1,492,036	171,944	7,029,708	329,736	38,189,819	
Shareholders' funds	-	-	-	-	-	2,812,931	-	2,812,931	
Total Liabilities and Shareholders' funds	19,166,499	3,855,504	6,144,392	1,492,036	171,944	9,842,639	329,736	41,002,750	
On-balance sheet interest sensitivity gap	7,385,634	1,353,645	(4,128,467)	1,545,313	262,242	(7,213,845)	795,478	-	
Off-balance sheet interest sensitivity gap									
Interest rate contracts									
- futures	-	(250,833)	344,833	(94,000)	-	-	-	-	
- options	720,897	196,255	(130,601)	(786,551)	-	-	-	-	
- swaps	(605,675)	344,814	(264,514)	542,390	(19,800)	-	-	(2,785)	
Total interest sensitivity gap	7,500,856	1,643,881	(4,178,749)	1,207,152	242,442	(7,213,845)	795,478	(2,785)	

* This is arrived after deducting specific allowance from non-performing loans.

31 Interest/ Profit Rate Risk (continued)

Bank 2005	←		Non-trading book				→		Effective interest rate %
	Up to 1 month RM'000	>1 - 3 months RM'000	>3 - 12 months RM'000	1 - 5 years RM'000	Over 5 years RM'000	Non-interest sensitive RM'000	Trading book RM'000	Total RM'000	
ASSETS									
Cash and short term funds	7,364,991	-	-	-	-	345,611	-	7,710,602	3.20
Securities purchased under resale agreements	1,123,087	160,613	166,060	-	-	-	-	1,449,760	3.00
Deposits and placements with banks and other financial institutions	-	479,942	-	-	-	-	-	479,942	3.22
Securities held for trading	-	-	-	-	-	-	703,727	703,727	3.57
Securities available-for-sale	331,223	816,071	642,419	1,431,880	20,135	43,007	-	3,284,735	3.53
Loans, advances and financing									
- performing	16,368,497	1,642,167	514,933	1,177,644	760,572	647,210	-	21,111,023	6.02
- non-performing *	-	-	-	-	-	365,683	-	365,683	-
Others	-	-	-	-	-	1,206,314	231,433	1,437,747	-
TOTAL ASSETS	25,187,798	3,098,793	1,323,412	2,609,524	780,707	2,607,825	935,160	36,543,219	
LIABILITIES AND SHAREHOLDERS' FUNDS									
Deposits from customers	12,929,993	4,521,310	5,691,566	325,798	167,934	4,680,771	-	28,317,372	2.63
Deposits and placements of banks and other financial institutions	1,013,316	179,499	358,641	6,562	2,422	394,359	-	1,954,799	2.80
Obligation on securities sold under repurchase agreements	1,617,617	-	-	-	-	-	-	1,617,617	2.50
Bills and acceptances payable	40,079	88,972	7,269	-	-	339,620	-	475,940	2.71
Recourse obligation on loans sold to Cagamas Berhad	-	-	-	439,904	348,027	-	-	787,931	4.57
Others	-	-	-	-	-	662,159	310,074	972,233	-
Total Liabilities	15,601,005	4,789,781	6,057,476	772,264	518,383	6,076,909	310,074	34,125,892	
Shareholders' funds	-	-	-	-	-	2,417,327	-	2,417,327	-
Total Liabilities and Shareholders' funds	15,601,005	4,789,781	6,057,476	772,264	518,383	8,494,236	310,074	36,543,219	
On-balance sheet interest sensitivity gap	9,586,793	(1,690,988)	(4,734,064)	1,837,260	262,324	(5,886,411)	625,086	-	
Off-balance sheet interest sensitivity gap									
Interest rate contracts									
- futures	-	150,267	(228,267)	78,000	-	-	-	-	
- options	(243,130)	8,100	-	454,330	(219,300)	-	-	-	
- swaps	(715,538)	288,501	5,967	432,121	(9,800)	-	-	1,251	
Total interest sensitivity gap	8,628,125	(1,244,120)	(4,956,364)	2,801,711	33,224	(5,886,411)	625,086	1,251	

* This is arrived at after deducting specific allowance from non-performing loans.

32 Collateral

In the normal course of business, the Bank pledges assets to raise liabilities and accepts assets as collateral that are permitted for resale or repledge. Collateral pledged and received are mainly via repurchase agreements and reverse repurchase agreements.

	<i>Bank</i>	
	2006	2005
	RM'000	RM'000
Carrying amount of assets pledged as collateral		
- Collateral pledged for repurchase agreements	1,708,280	1,617,617
Fair value of assets accepted as collateral and collateral sold/ repledged		
- Collateral accepted for reverse repurchase agreement	2,303,513	1,517,383
- Collateral sold	11,969	123,955

33 Fair Values of Financial Assets and Liabilities

The following table summarises the fair value of the financial assets and liabilities carried on the balance sheet as at 31 December.

	2006	2006	2005	2005
	Carrying	Fair	Carrying	Fair
	amount	Value	amount	Value
	RM'000	RM'000	RM'000	RM'000
Financial Assets				
Cash and short term funds	6,114,345	6,114,345	7,710,602	7,710,602
Securities purchased under resale agreements	2,273,539	2,273,539	1,449,760	1,449,760
Deposits and placements with banks and other financial institutions	1,989,882	1,989,882	479,942	479,942
Securities held-for-trading	795,937	795,937	703,727	703,727
Securities available-for-sale	3,806,463	3,810,062	3,284,735	3,297,692
Loans, advances and financing	24,343,937	24,269,662	21,476,706	21,443,719
Financial Liabilities				
Deposits from customers	31,822,229	31,835,556	28,317,372	28,311,164
Deposits and placements of banks and other financial institutions	1,934,326	1,934,317	1,954,799	1,954,786
Obligations on securities sold under repurchase agreements	1,660,739	1,660,739	1,617,617	1,617,617
Bills and acceptances payable	490,055	490,055	475,940	475,940
Recourse obligation on loans sold to Cagamas Berhad	899,751	909,689	787,931	801,336

33 Fair Values of Financial Assets and Liabilities (continued)

The methods and assumptions used in estimating the fair values of financial instruments are as follows:

Cash and short term funds

Securities purchased under resale agreements

Deposits and placements with banks and other financial institutions

Obligations on securities sold under repurchase agreements

Bills and acceptances payable

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

Securities

Listed equity shares are valued at the quoted market price whilst unlisted equity shares whose fair value cannot be reliably measured are stated at cost. Fair value of the unlisted equity shares is reliably measurable if (a) the variability in the range of reasonable fair value estimates is not significant for that instrument or (b) the probabilities of the various estimates within the range can be reasonably assessed and used in estimating fair value. Unlisted equity shares, whose fair value can be reliably measured, are valued using an appropriate valuation model.

Fair values for other securities are estimated using market prices for these financial instruments. Where market prices are not available, fair values have been estimated using prices for financial instruments with similar characteristics, or a suitable valuation technique where practicable to do so.

Loans, advances and financing

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

Deposits from customers

Deposits and placements of banks and other financial institutions

Recourse obligation on loans sold to Cagamas Berhad

Deposits, placements and obligations which mature or reprice after six months are grouped by residual maturity. Fair value is estimated using discounted cash flows, applying either market rates, where applicable, or current rates offered for deposits of similar remaining maturities.

Unrecognised financial instruments

The valuation of financial instruments not recognised in the balance sheet reflects their current market rates at the balance sheet date. The contracted amount and fair value of financial instruments not recognised in the balance sheet as at 31 December are disclosed in Note 30.

34 Lease Commitments

The Bank and the group have lease commitments in respect of rented premises and hired equipment, all of which are classified as operating leases. A summary of the non-cancellable long term commitments net of sub-leases are as follows:

Year	<i>Group and Bank</i>	
	RM'000	
Less than one year		12,634
Between one and five years		19,302
More than five years		1,120

35 Capital Commitments

	<i>Group and Bank</i>	
	2006	2005
	RM'000	RM'000
Capital expenditure:		
- Authorised and contracted for	8,776	9,037
- Authorised but not contracted for	1,963	4,002
	10,739	13,039

36 Equity-based Compensation

The Bank participated in the following cash settled share compensation plans operated by the HSBC Group for the acquisition of HSBC Holdings plc shares.

a. Executive Share Option Scheme/Group Share Option Plan

The HSBC Holdings Group Share Option Plan, and previously the HSBC Holdings Executive Share Option Scheme, are discretionary share incentive plans under which HSBC employees, based on performance criteria and potential, are granted options to acquire HSBC Holdings ordinary shares. The exercise price of options granted under the Group Share Option Plan, is the higher of the average market value of the ordinary shares on the five business days prior to the grant of the option or the market value of the ordinary shares on the date of grant of the option. The exercise price of options granted under the Executive Share Option Scheme was the market value of the ordinary shares on the business day prior to the grant of the option. They are normally exercisable between the third and tenth anniversary of the date of grant. The cost of the awards is amortised over the vesting period.

Movements in the number of share options held by employees are as follows:

Year	2006	Weighted average exercise price	2005	Weighted average exercise price
	Number	£	Number	£
	('000)		('000)	
Outstanding at 1 January	2,195	7.85	2,471	7.85
Exercised in the year	(318)	7.72	(221)	7.87
Lapsed in the year	(24)	8.06	(55)	7.89
Outstanding at 31 December	1,853	7.87	2,195	7.85
Options vested at 31 December	1,232		1,047	
	2006		2005	
	RM'000		RM'000	
Compensation cost recognised during the year	10,618		4,741	

The Group Share Option Plan ceased in 2005 and is replaced by the Achievement Shares Award. The existing share options held by employees granted under Group Share Option Plan prior to 2005 will continue until they are exercised or lapsed.

36 Equity-based Compensation (continued)

b. Savings-Related Share Option Schemes

The Savings-Related Share Option Schemes are all-employee share plans under which eligible HSBC employees are granted options to acquire HSBC Holdings ordinary shares. Employees may make monthly contributions up to £250 over a period of three or five years which may be used, on the third or fifth anniversary of the commencement of the relevant savings contract, to exercise the options; alternatively the employee may elect to have the savings (plus interest) repaid in cash. The options are exercisable within six months following the third or fifth anniversary of the commencement of the relevant savings contract. The exercise price is set at a discount of up to 20 per cent to the market value of the ordinary shares at the date of grant. The cost of the awards is amortised over the vesting period.

Movements in the number of share options held by employees are as follows:

Year	2006 Number (‘000)	Weighted average exercise price £	2005 Number (‘000)	Weighted average exercise price £
Outstanding at 1 January	1,786	6.19	2,544	6.00
Granted in the year	547	7.67	553	6.68
Exercised in the year	(528)	5.44	(17)	5.93
Lapsed in the year	(83)	6.78	(1,284)	6.06
Transfers	(10)	6.50	(10)	6.08
Outstanding at 31 December	<u>1,712</u>	<u>6.60</u>	<u>1,786</u>	<u>6.19</u>
Options vested at 31 December	<u>515</u>		<u>12</u>	
	2006 RM’000		2005 RM’000	
Compensation cost recognised during the year	<u>7,438</u>		<u>5,737</u>	

36 Equity-based Compensation (continued)

c. Restricted Share Plan

The HSBC Holdings Restricted Share Plan is intended to align the interests of executives with those of shareholders by linking executive awards to the creation of superior shareholder value. This is achieved by focusing on predetermined targets. The cost of the conditional awards is recognised through an annual charge based on the likely level of vesting of shares, apportioned over the period of service to which the award relates.

Year	2006 Number (‘000)	2005 Number (‘000)
Outstanding at 1 January	217	184
Additions during the year	54	60
Released in the year	(22)	(27)
Outstanding at 31 December	<u>249</u>	<u>217</u>
	2006 RM’000	2005 RM’000
Compensation cost recognised during the year	<u>2,400</u>	<u>1,771</u>

The weighted average purchase price for all shares purchased by HSBC for awards under the Restricted Share Plan is £8.66 (2005: £8.26). The closing price of the HSBC share at 31 December 2006 was £9.31 (2005: £9.33). The weighted average remaining vesting period as at 31 December 2006 was 1.31 years (2005: 1.96 years).

d. Achievement Share Award

Achievement Share Award was introduced in 2005 to replace the Group Share Option Plan. HSBC Holdings ordinary shares are awarded to senior executives, without corporate performance conditions and will be released to the individual after three years, provided participants remain continuously employed within the HSBC Group. Additional awards are made during the three-year life of the award. These represent the equivalent value of dividends reinvested in shares. At the end of three years, the original Award together with the Additional Share Awards (added to the original award) will be released. The cost of the awards is recognised through an annual charge based on the cost of the shares purchased, apportioned over a period of three years to which the award relates.

Year	2006 Number (‘000)	2005 Number (‘000)
Outstanding at 1 January	88	-
Additions during the year	94	88
Outstanding at 31 December	<u>182</u>	<u>88</u>
	2006 RM’000	2005 RM’000
Compensation cost recognised during the year	<u>3,396</u>	<u>1,336</u>

The weighted average purchase price for all shares purchased by HSBC for awards under the Achievement Shares Award is £8.99 (2005: £8.43). The closing price of the HSBC share at 31 December 2006 was £9.31 (2005: £9.33). The weighted average remaining vesting period as at 31 December 2006 was 2.52 years (2005: 2.17 years).

37 Change in Accounting Policy**Change in Accounting Policy**

In the current financial year, the Bank adopted a new accounting standard, FRS 2 on Share-based Payment. FRS 2 requires companies to adopt a fair-value-based method of accounting for share-based compensation plans which takes into account vesting conditions related to market performance, for example total shareholder return. Under this method, compensation cost is measured at the date of grant based on the assessed value of the award and is recognised over the service period, which is usually the vesting period. The fair value of share options granted is to be recognised in the income statement.

The change in accounting policy has been accounted for by restating comparatives and adjusting the opening balance of retained profit as at 1 January 2005 as disclosed in Note 38(a) and the Statement of Changes in Equity respectively.

Prior Year Adjustments

The change in accounting policy as described above was applied retrospectively and has the following cumulative impact on the opening retained profit of the Bank:

	31 Dec 2005
	RM'000
At 31 December 2005, as previously stated	991,840
Effect of adopting FRS 2	<u>(19,253)</u>
As at 31 December 2005, as restated	<u>972,587</u>

38 Comparative Figures

The presentation and classification of items in the current financial statements have been consistent with the previous financial year except for the following:

- (a) Changes in accounting policy explained in Note 37.

	<i>Group and Bank</i>	
	As restated	As previously stated
	RM'000	RM'000
<i>Balance Sheet</i>		
<i>as at 31 December 2005</i>		
Securities available-for-sale	3,284,735	3,277,490
Other assets	371,825	376,829
Deferred tax asset	56,809	53,547
Other liabilities	942,517	917,761
Reserves	<u>2,152,827</u>	<u>2,172,080</u>

38 Comparative Figures (continued)

(a) Changes in accounting policy explained in Note 37.

	<i>Group and Bank</i>	
	As restated RM'000	As previously stated RM'000
<i>Income Statement for the financial year ended 31 December 2005</i>		
Other operating expenses	791,255	780,777
Profit before allowance	746,960	757,438
Profit before taxation and zakat	736,678	747,156
Profit attributable to shareholders	524,813	533,685
Earnings per RM0.50 share	<u>229.2 sen</u>	<u>233.1 sen</u>

(b) Reclassification to conform to current years' presentation

	<i>Group and Bank</i>	
	As restated RM'000	As previously stated RM'000
<i>Balance Sheet as at 31 December 2005</i>		
Property, plant and equipment	304,916	310,144
Intangible assets	<u>5,228</u>	<u>-</u>

39 Operations of Islamic Banking

Balance Sheet as at 31 December 2006 (10 Zulhijjah 1427)

		2006	2005
Assets	<i>Note</i>	RM'000	RM'000
Cash and short term funds	<i>(a)</i>	975,534	1,157,855
Deposits and placements with banks and other financial institutions	<i>(b)</i>	160,000	90,000
Securities available-for-sale	<i>(c)</i>	1,040,407	1,026,595
Financing, advances and other loans	<i>(d)</i>	3,080,253	2,853,518
Other assets	<i>(f)</i>	11,096	13,666
Statutory deposits with Bank Negara Malaysia		89,600	98,500
Equipment		268	342
Intangible assets		552	1,089
Deferred tax asset	<i>(g)</i>	15,603	13,737
Total Assets		<u>5,373,313</u>	<u>5,255,302</u>
Liabilities			
Deposits from customers	<i>(h)</i>	3,654,806	3,512,422
Deposits and placements of banks and other financial institutions	<i>(i)</i>	186,806	270,124
Other liabilities	<i>(j)</i>	958,576	946,987
Provision for taxation and zakat	<i>(k)</i>	20,683	20,680
Total liabilities		<u>4,820,871</u>	<u>4,750,213</u>
Islamic Banking Capital Funds			
Funds allocated from Head Office		430,000	430,000
Reserves	<i>(l)</i>	122,442	75,089
Islamic Banking Capital Funds		<u>552,442</u>	<u>505,089</u>
Total Liabilities and Islamic Banking Capital Funds		<u>5,373,313</u>	<u>5,255,302</u>
Commitments and Contingencies	<i>(v)</i>	<u>311,526</u>	<u>241,408</u>

The accompanying sub-notes form an integral part of the Financial Statements.

39 Operations of Islamic Banking (continued)

Income Statement for the Year Ended 31 December 2006 (10 Zulhijjah 1427)

	<i>Note</i>	2006 RM'000	2005 RM'000
Income derived from investment of depositors' funds and others	<i>(m)</i>	258,252	138,540
Allowance for losses on financing	<i>(n)</i>	(23,713)	(19,193)
Profit equalisation reserve	<i>(j)</i>	(3,000)	(460)
Total distributable income		231,539	118,887
Income attributable to depositors	<i>(o)</i>	(156,397)	(86,415)
Income attributable to the Bank		75,142	32,472
Income derived from investment of Islamic banking capital funds	<i>(p)</i>	47,294	30,432
Total net income		122,436	62,904
Other operating expenses	<i>(q)</i>	(57,957)	(5,173)
Profit before taxation and zakat		64,479	57,731
Taxation and zakat	<i>(s)</i>	(18,383)	(16,555)
Profit after taxation and zakat		46,096	41,176

The accompanying sub-notes form an integral part of the Financial Statements.

39 Operations of Islamic Banking (continued)

Statement of Changes in Equity for the Year Ended 31 December 2006 (10 Zulhijjah 1427)

	← Non-distributable →		Distributable		
	<i>Funds allocated from Head Office</i>	<i>Available- for-sale reserve</i>	<i>Retained profits</i>	<i>Total reserves</i>	<i>Total</i>
	RM'000	RM'000	RM'000	RM'000	RM'000
Balance as at 1 January 2005	200,000	4,198	33,021	37,219	237,219
Funds allocated	230,000	-	-	-	230,000
Net profit for the year	-	-	41,176	41,176	41,176
Net gains and losses not recognised in the income statement					
- Net unrealised losses on revaluation	-	(3,306)	-	(3,306)	(3,306)
Balance as at 31 December 2005	430,000	892	74,197	75,089	505,089
Balance as at 1 January 2006	430,000	892	74,197	75,089	505,089
Net profit for the year	-	-	46,096	46,096	46,096
Net gains and losses not recognised in the income statement					
- Net unrealised gains on revaluation	-	1,302	-	1,302	1,302
Net gains reclassified to income statement	-	(45)	-	(45)	(45)
Balance as at 31 December 2006	430,000	2,149	120,293	122,442	552,442

The accompanying sub-notes form an integral part of the Financial Statements.

39 Operations of Islamic Banking (continued)

Cash Flow Statement for the Year Ended 31 December 2006 (10 Zulhijjah 1427)

	2006 RM'000	2005 RM'000
Cash Flows from Operating Activities		
Profit before taxation and zakat	64,479	57,731
Adjustments for :		
Equipment written off	36	2
Intangible assets written off	4	-
Depreciation of equipment	85	83
Amortisation of intangible assets	538	524
Operating profit before changes in operating assets	<u>65,142</u>	<u>58,340</u>
(Increase)/ Decrease in operating assets		
Deposits and placements with banks and other financial institutions	(70,000)	(90,000)
Financing, advances and other loans	(226,735)	(1,075,431)
Other assets	(18,165)	28,366
Statutory deposits with Bank Negara Malaysia	8,900	(98,500)
Increase/ (Decrease) in operating liabilities		
Deposits from customers	142,384	1,498,064
Deposits and placements of banks and other financial institutions	(83,318)	270,080
Other liabilities	11,589	(9,966)
Net cash (used in)/ generated from operating activities	<u>(170,203)</u>	<u>580,953</u>
Cash Flows from Investing Activities		
Purchase of equipment	(47)	(221)
Purchase of intangible assets	(5)	(154)
Securities available-for-sale	(12,066)	(88,832)
Net cash used in from investing activities	<u>(12,118)</u>	<u>(89,207)</u>
Cash Flows from Financing Activities		
Funds allocated from Head Office	-	230,000
Net cash generated from financing activities	<u>-</u>	<u>230,000</u>
Net (decrease)/ increase in Cash and Cash Equivalents	(182,321)	721,746
Cash and Cash Equivalents at beginning of year	1,157,855	436,109
Cash and Cash Equivalents at end of year	975,534	1,157,855
Analysis of Cash and Cash Equivalents		
Cash and short-term funds	<u>975,534</u>	<u>1,157,855</u>

The accompanying sub-notes form an integral part of the Financial Statements.

39 Operations of Islamic Banking (continued)

(a) Cash and Short Term Funds

	2006	2005
	RM'000	RM'000
Cash and balances with banks and other financial institutions	534	855
Money at call and deposit placements maturing within one month	975,000	1,157,000
	975,534	1,157,855

(b) Deposits and Placements with Banks and Other Financial Institutions

	2006	2005
	RM'000	RM'000
Bank Negara Malaysia	160,000	90,000

(c) Securities Available-for-Sale

	2006	2005
	RM'000	RM'000
Money market instruments:		
Malaysian Government Islamic Treasury bills	39,408	-
Bank Negara Malaysia Islamic bills	-	308,442
Malaysian Government Islamic bonds	373,915	-
Negotiable Islamic instruments of deposit	9,990	4,988
Islamic accepted bills	-	55,830
Islamic Khazanah bonds	262,200	-
Islamic Cagamas bonds	3,994	-
	689,507	369,260
Unquoted securities:		
Islamic debt securities	350,900	657,335
	1,040,407	1,026,595

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

	2006	2005
	RM'000	RM'000
Maturing within one year	78,034	369,260
One year to three years	611,473	-
	689,507	369,260

39 Operations of Islamic Banking (continued)

(d) Financing, Advances and Other Loans

(i) By type	2006	2005
	RM'000	RM'000
Term financing		
House financing	104,471	113,141
Hire purchase receivables	190,341	110,885
Lease receivables	30,339	49,224
Other term financing	1,367,673	843,590
Claims on customers under acceptance credits	1,596,149	1,927,977
Credit /charge cards	1,538	1,409
Less: Unearned income	(142,815)	(141,321)
	3,147,696	2,904,905
Less: Allowance for bad and doubtful financing :		
- General	(48,740)	(43,770)
- Specific	(18,703)	(7,617)
Total net financing, advances and other loans	3,080,253	2,853,518

(ii) By contract

	2006	2005
	RM'000	RM'000
Bai' Bithaman Ajil (<i>deferred payment sale</i>)	534,376	521,209
Ijarah (<i>operating lease</i>)	28,749	45,875
Ijarah Thumma Al-Bai (<i>hire purchase / finance lease</i>)	169,010	101,385
Murabahah (<i>cost-plus</i>)	1,222,689	1,346,043
Others	1,192,872	890,393
	3,147,696	2,904,905

(iii) By type of customer

	2006	2005
	RM'000	RM'000
Domestic business enterprises		
- Small medium enterprises	968	1,535
- Others	2,258,307	2,527,761
Individuals	878,439	369,256
Foreign entities	9,982	6,353
	3,147,696	2,904,905

39 Operations of Islamic Banking (continued)

(d) Financing, Advances and Other Loans (continued)

(iv) By profit rate sensitivity

	2006	2005
	RM'000	RM'000
Fixed rate		
House financing	83,945	89,747
Hire purchase receivables	169,011	101,386
Other financing	2,893,202	2,712,363
Variable rate		
Other financing	1,538	1,409
	<u>3,147,696</u>	<u>2,904,905</u>

(v) By sector

	2006	2005
	RM'000	RM'000
Agriculture, hunting, forestry and fishing	258,335	288,150
Mining and quarrying	2,198	4,786
Manufacturing	1,430,224	1,382,641
Electricity, gas and water	5,921	6,031
Construction	38,016	80,901
Real estate	12,563	15,498
Purchase of landed property:		
- Residential	83,945	89,747
- Non-residential	7,751	7,788
Wholesale & retail trade and restaurants & hotels	367,010	545,386
Transport, storage and communication	48,697	41,779
Finance, insurance and business services	10,344	80,230
Consumption credit	802,561	283,966
Others	80,131	78,002
	<u>3,147,696</u>	<u>2,904,905</u>

(vi) By maturity structure

	2006	2005
	RM'000	RM'000
Maturing within one year	1,623,977	1,965,726
One year to three years	375,700	196,852
Three years to five years	824,741	419,758
Over five years	323,278	322,569
	<u>3,147,696</u>	<u>2,904,905</u>

39 Operations of Islamic Banking (continued)

(e) Non-Performing Financing (NPF)

(i) Movements in non-performing financing, advances and other loans (including income receivables)

	2006 RM'000	2005 RM'000
At beginning of year	12,805	16,921
Classified as non-performing during the year	21,692	5,409
Reclassified as performing	(399)	(346)
Amount recovered	(4,073)	(2,520)
Amount written off	(7,842)	(6,659)
At end of year	<u>22,183</u>	<u>12,805</u>
Specific allowance	<u>(18,703)</u>	<u>(7,617)</u>
Net non-performing financing, advances and other loans	<u>3,480</u>	<u>5,188</u>
Ratio of net non-performing financing, advances and other loans to net financing, advances and other loans	<u>0.1%</u>	<u>0.2%</u>

(ii) Movements in allowance for bad and doubtful financing

	2006 RM'000	2005 RM'000
General allowance		
At beginning of year	43,770	27,509
Allowance made during the year	<u>4,970</u>	<u>16,261</u>
At end of year	<u>48,740</u>	<u>43,770</u>
As % of total financing less specific allowance	<u>1.5%</u>	<u>1.5%</u>

	2006 RM'000	2005 RM'000
Specific allowance		
At beginning of year	7,617	10,305
Allowance made during the year	23,716	4,870
Amount recovered	(4,926)	(936)
Amount written off	(7,704)	(6,622)
At end of year	<u>18,703</u>	<u>7,617</u>

(iii) Non-performing financing by sector

	2006 RM'000	2005 RM'000
Manufacturing	5,462	4,939
Purchase of landed property:		
- Residential	2,081	1,645
Wholesale & retail trade and restaurants & hotels	1,195	1,785
Transport, storage and communication	885	2,290
Consumption credit	11,016	601
Others	<u>1,544</u>	<u>1,545</u>
	<u>22,183</u>	<u>12,805</u>

39 Operations of Islamic Banking (continued)

(f) Other Assets

	2006	2005
	RM'000	RM'000
Settlement due from Head Office	1,589	4,655
Income receivable	9,436	8,677
Other receivables, deposits and prepayments	71	334
	11,096	13,666

(g) Deferred Tax Asset

	2006	2005
	RM'000	RM'000
Deferred tax assets	15,603	13,737

The recognised deferred tax assets are as follows:

	2006	2005
	RM'000	RM'000
Lease receivables		
- capital allowance	1,117	1,353
Available-for-sale reserve	(837)	(347)
Allowances		
- general allowance	13,647	12,256
- others	1,676	475
	15,603	13,737

(h) Deposits from Customers

(i) By type of deposit

	2006	2005
	RM'000	RM'000
Non-Mudharabah Fund		
Demand deposits	60,949	38,948
Savings deposits	271,085	157,048
	332,034	195,996
Mudharabah Fund		
General investment deposits	3,322,772	3,316,426
	3,654,806	3,512,422

The maturity structure of general investment deposits is as follows:

	2006	2005
	RM'000	RM'000
Due within six months	3,015,895	3,142,528
Six months to one year	304,234	173,898
One year to three years	2,353	-
Three years to five years	290	-
	3,322,772	3,316,426

(ii) By type of customer

	2006	2005
	RM'000	RM'000
Government and statutory bodies	92,209	10,335
Business enterprises	2,216,611	2,481,328
Individuals	1,231,061	893,263
Others	114,925	127,496
	3,654,806	3,512,422

39 Operations of Islamic Banking (continued)

(i) Deposits and Placements of Banks and Other Financial Institutions

	2006	2005
	RM'000	RM'000
Mudharabah Fund		
Licensed Islamic banks	67,500	70,000
Licensed banks	25,000	50,000
Bank Negara Malaysia	1,330	124
Other financial institutions	92,976	150,000
	186,806	270,124

(j) Other Liabilities

	2006	2005
	RM'000	RM'000
Special placement deposits by Head Office	920,792	921,294
Profit equalisation reserve	4,700	1,700
Profit payable	19,738	9,675
Other creditors and accruals	13,346	14,318
	958,576	946,987

Movement in profit equalisation reserve is as follows:

	2006	2005
	RM'000	RM'000
At beginning of year	1,700	1,240
Provided in the financial year	3,000	460
At end of year	4,700	1,700

(k) Provision for Taxation and Zakat

	2006	2005
	RM'000	RM'000
Taxation	20,683	20,631
Zakat	-	49
	20,683	20,680

(l) Reserves

	2006	2005
	RM'000	RM'000
Retained profits	120,293	74,197
Available-for-sale reserve	2,149	892
	122,442	75,089

39 Operations of Islamic Banking (continued)

(m) Income Derived from Investment of Depositors' Funds and Others

	2006	2005
	RM'000	RM'000
Income derived from investment of:		
(i) general investment deposits	186,920	90,262
(ii) specific investment deposits	42,249	35,913
(iii) other deposits	29,083	12,365
	258,252	138,540

(i) Income derived from investment of general investment deposits

	2006	2005
	RM'000	RM'000
<u>Finance income and hibah:</u>		
Financing, advances and other loans	148,777	80,324
Money at call and deposit with financial institutions	36,718	9,583
Total finance income and hibah	185,495	89,907
<u>Other operating income</u>		
Net gain from dealing in foreign currency	1,425	355
	186,920	90,262

(ii) Income derived from investment of specific investment deposits

	2006	2005
	RM'000	RM'000
<u>Finance income and hibah:</u>		
Available-for-sale securities	31,603	36,964
Accretion of discount less amortisation of premium	10,646	(1,051)
Total finance income and hibah	42,249	35,913

39 Operations of Islamic Banking (continued)

(m) Income Derived from Investment of Depositors' Funds and Others (continued)

(iii) Income derived from investment of other deposits

	2006	2005
	RM'000	RM'000
<u>Finance income and hibah:</u>		
Financing, advances and other loans	23,148	11,004
Money at call and deposit with financial institutions	5,713	1,313
Total finance income and hibah	28,861	12,317
<u>Other operating income</u>		
Net gain from dealing in foreign currency	222	48
	29,083	12,365

(n) Allowance for Losses on Financing

	2006	2005
	RM'000	RM'000
Allowance for bad and doubtful debts on financing:		
(a) Specific allowance		
- Made in the financial year	23,716	4,870
- Written back	(4,926)	(936)
(b) General allowance		
- Made in the financial year	4,970	16,261
Bad debts on loans and financing		
- Recovered	(170)	(1,287)
- Written off	123	285
	23,713	19,193

(o) Income Attributable to Depositors

	2006	2005
	RM'000	RM'000
Deposits from customers		
- Mudharabah Fund	117,765	59,267
- Non-Mudharabah Fund	3,867	369
Deposits and placements of banks and other financial institutions		
- Mudarabah Fund	2,113	988
Special placement deposits by Head Office	32,652	25,791
	156,397	86,415

39 Operations of Islamic Banking (continued)

(p) Income Derived from the Investment of Islamic Banking Capital Funds

	2006	2005
	RM'000	RM'000
<u>Financing income and hibah:</u>		
Financing, advances and other loans	21,867	10,695
Money at call and deposit with financial institutions	5,397	1,276
Total finance income and hibah	27,264	11,971
<u>Other operating income</u>		
Fees and commission	19,821	18,414
Net gain from dealing in foreign currency	209	47
	47,294	30,432

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

Service charges and fees	15,743	13,573
Agency fees	2,814	2,787
Cards	861	1,563

(q) Other operating expenses

	2006	2005
	RM'000	RM'000
Personnel expenses	18,468	3,362
Promotion and marketing related expenses	1,286	401
Establishment related expenses	3,396	838
General administrative expenses	34,807	572
	57,957	5,173

(r) Shariah Committee's Remuneration

	2006	2005
	RM'000	RM'000
Shariah Committee	94	62

39 Operations of Islamic Banking (continued)

(s) Taxation and Zakat

	2006 RM'000	2005 RM'000
Malaysian income tax	20,683	20,631
Deferred tax		
Origination and reversal of temporary differences	<u>(2,355)</u>	<u>(4,125)</u>
	18,328	16,506
Zakat	<u>55</u>	<u>49</u>
	18,383	16,555

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

	2006 RM'000	2005 RM'000
Profit before taxation	<u>64,479</u>	<u>57,731</u>
Income tax using Malaysian tax rates (28%)	18,054	16,165
Non-deductible expenses	<u>274</u>	<u>341</u>
	18,328	16,506

(t) Income from Islamic Banking Operations

For consolidation with the conventional operations, income from Islamic banking operations comprises the following items:

	2006 RM'000	2005 RM'000
Income derived from investment of depositors' funds and others	258,252	138,540
Profit equalisation reserves	(3,000)	(460)
Income attributable to the depositors	(156,397)	(86,415)
Income attributable to special placement deposits by Head Office	<u>32,652</u>	<u>25,791</u>
	131,507	77,456
Income derived from the investment of Islamic banking capital funds	47,294	30,432
Income from Islamic banking operations	<u>178,801</u>	<u>107,888</u>

39 Operations of Islamic Banking (continued)

(u) Capital Adequacy

The capital adequacy ratios of the Islamic Banking Operation are as follows:

	2006	2005
	RM'000	RM'000
<u>Tier 1 capital</u>		
Funds allocated from Head Office	430,000	430,000
Retained profits	120,293	74,197
	550,293	504,197
Less: Deferred tax adjustments	(16,440)	(14,085)
Total Tier 1 capital	533,853	490,112
<u>Tier 2 capital</u>		
General allowance for bad and doubtful debts and financing	48,740	43,770
Total Tier 2 capital	48,740	43,770
Capital base	582,593	533,882
Core capital ratio	14.6%	13.4%
Risk-weighted capital ratio	15.9%	14.6%

Breakdown of gross risk-weighted assets in the various categories of risk-weights:

	2006		2005	
	Principal	Risk-weighted	Principal	Risk-weighted
	RM'000	RM'000	RM'000	RM'000
0%	1,900,515	-	1,534,433	-
10%	-	-	-	-
20%	20,124	4,025	188,240	37,648
50%	71,765	35,882	76,568	38,284
100%	3,620,676	3,620,676	3,580,919	3,580,919
	5,613,080	3,660,583	5,380,160	3,656,851

39 Operations of Islamic Banking (continued)

(v) Commitments and Contingencies

In the normal course of business, the Bank makes various commitments and incurs certain contingent liabilities with legal recourse to its customers. No material losses are anticipated as a result of these transactions.

The table below shows the contract or underlying principal amounts, credit equivalents amounts and risk weighted amounts of unmatured off-balance sheet transactions as at balance sheet date. The contract or underlying principal amounts indicate the volume of business outstanding and do not represent amount at risk.

	2006			2005		
	Principal amount RM'000	Credit equivalent amount * RM'000	Risk weighted amount RM'000	Principal amount RM'000	Credit equivalent amount * RM'000	Risk weighted amount RM'000
Irrevocable commitments to extend credit:						
- Maturity not exceeding one year	18,291	-	-	63,262	-	-
- Maturity exceeding one year	173,210	86,605	86,605	171,446	85,723	85,723
Others	120,025	120,025	120,025	6,700	6,700	6,700
	311,526	206,630	206,630	241,408	92,423	92,423

* The credit equivalent amount is arrived at using the credit conversion factors as per Bank Negara Malaysia guidelines.

39 Operations of Islamic Banking (continued)

(w) Profit Rate Risk

The Bank is exposed to various risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows of the Islamic banking operations. The following table indicates the effective profit rates at the balance sheet date and the periods of repricing or maturity, whichever is earlier.

2006	Non-trading book						Trading book RM'000	Total RM'000	Effective profit rate %
	Up to 1 month RM'000	>1 - 3 months RM'000	>3 - 12 months RM'000	1 - 5 years RM'000	Over 5 years RM'000	Non-profit sensitive RM'000			
ASSETS									
Cash and short term funds	975,392	-	-	-	-	142	-	975,534	3.59
Deposits and placements with banks and other financial institutions	-	160,000	-	-	-	-	-	160,000	3.69
Securities available-for-sale	-	19,966	157,709	862,732	-	-	-	1,040,407	3.97
Financing, advances and other loans									
- performing	1,573,208	34,647	26,908	1,123,773	318,237	-	-	3,076,773	7.66
- non-performing *	-	-	-	-	-	3,480	-	3,480	-
Others	-	-	-	-	-	117,119	-	117,119	-
TOTAL ASSETS	2,548,600	214,613	184,617	1,986,505	318,237	120,741	-	5,373,313	
LIABILITIES AND ISLAMIC BANKING CAPITAL FUNDS									
Deposits from customers	2,168,356	805,645	617,213	2,643	-	60,949	-	3,654,806	3.20
Deposits and placements of banks and other financial institutions	186,806	-	-	-	-	-	-	186,806	3.21
Others	940,075	-	-	-	-	39,184	-	979,259	3.59
Total Liabilities	3,295,237	805,645	617,213	2,643	-	100,133	-	4,820,871	
Islamic Banking Capital Funds	-	-	-	-	-	552,442	-	552,442	
Total Liabilities and Islamic Banking Capital Funds	3,295,237	805,645	617,213	2,643	-	652,575	-	5,373,313	
On-balance sheet profit sensitivity gap	(746,637)	(591,032)	(432,596)	1,983,862	318,237	(531,834)	-	-	
Total profit sensitivity gap	(746,637)	(591,032)	(432,596)	1,983,862	318,237	(531,834)	-	-	

* This is arrived at after deducting the specific allowance from non-performing loans.

39 Operations of Islamic Banking (continued)

(w) Profit Rate Risk (continued)

2005	Non-trading book						Trading book RM'000	Total RM'000	Effective profit rate %
	Up to 1 month RM'000	>1 - 3 months RM'000	>3 - 12 months RM'000	1 - 5 years RM'000	Over 5 years RM'000	Non-profit sensitive RM'000			
ASSETS									
Cash and short term funds	1,157,491	-	-	-	-	364	-	1,157,855	2.95
Deposits and placements with banks and other financial institutions	-	90,000	-	-	-	-	-	90,000	3.00
Securities available-for-sale	-	509,934	180,324	336,337	-	-	-	1,026,595	3.79
Financing, advances and other loans									
- performing	1,894,987	1,756	36,205	600,012	315,370	-	-	2,848,330	4.47
- non-performing *	-	-	-	-	-	5,188	-	5,188	-
Others	-	-	-	-	-	127,334	-	127,334	-
TOTAL ASSETS	3,052,478	601,690	216,529	936,349	315,370	132,886	-	5,255,302	
LIABILITIES AND ISLAMIC BANKING CAPITAL FUNDS									
Deposits from customers	1,503,233	968,594	1,001,647	-	-	38,948	-	3,512,422	2.74
Deposits and placements of banks and other financial institutions	270,124	-	-	-	-	-	-	270,124	2.96
Others	920,792	-	-	-	-	46,875	-	967,667	3.12
Total Liabilities	2,694,149	968,594	1,001,647	-	-	85,823	-	4,750,213	
Islamic Banking Capital Funds	-	-	-	-	-	505,089	-	505,089	
Total Liabilities and Islamic Banking Capital Funds	2,694,149	968,594	1,001,647	-	-	590,912	-	5,255,302	
On-balance sheet profit sensitivity gap	358,329	(366,904)	(785,118)	936,349	315,370	(458,026)	-	-	
Total profit sensitivity gap	358,329	(366,904)	(785,118)	936,349	315,370	(458,026)	-	-	

* This is arrived at after deducting the specific allowance from non-performing loans.

39 Operations of Islamic Banking (continued)

(x) Fair Values of Financial Assets and Liabilities

The following table summarises the fair value of the financial assets and liabilities carried on the balance sheet as at 31 December.

	2006	2006	2005	2005
	Carrying	Fair	Carrying	Fair
	amount	Value	amount	Value
	RM'000	RM'000	RM'000	RM'000
Financial Assets				
Cash and short term funds	975,534	975,534	1,157,855	1,157,855
Deposits and placements with banks and other financial institutions	160,000	160,000	90,000	90,000
Securities available-for-sale	1,040,407	1,040,407	1,026,595	1,026,595
Financing, advances and other loans	3,080,253	3,021,062	2,853,518	2,824,925
Financial Liabilities				
Deposits from customers	3,654,806	3,655,543	3,512,422	3,512,023
Deposits and placements of banks and other financial institutions	186,806	186,806	270,124	270,124

The methods and assumptions used to estimate the fair values of the financial assets and financial liabilities of the operations of Islamic banking are as stated in Note 33.

39 Operations of Islamic Banking (continued)

(y) Shariah Committee

In line with Bank Negara Malaysia's "Guidelines on the Governance of Shariah Committee for The Islamic Financial Institutions" known as BNM/GPS 1, the following Shariah scholars were appointed:

- 1) Dr. Mohamad Akram Laldin, Head of Fiqh and Usul Al-fiqh Department at International Islamic University of Malaysia. He is a graduate of University of Jordan, Shariah Department and a Ph.D holder in Islamic Law from the University of Edinburgh, Scotland.
- 2) Dr. Rusni Hassan, Assistant Professor of Law at International Islamic University of Malaysia. She holds a double degree, LLB and LLB (Shariah) as well as Ph.D in Law from the same university.
- 3) Khairul Anuar Ahmad, lecturer with Selangor Islamic College University. He holds a Bachelor and Master of Shariah from University of Malaya.

Monthly meetings are held to discuss Shariah issues complemented by ad-hoc meetings to resolve urgent Shariah matters. The Committee peruse all the documents from inception of a product, to documentation and marketing to ensure that the process flow complies with Shariah at all times. No major Shariah issues were raised and none remain unresolved.

A Shariah Compliance executive was employed during the year to support the Shariah function and the Committee. This role will expand to include Shariah review of operations and other relevant Shariah work.