Company No.
127776-V

HSBC BANK MALAYSIA BERHAD
(Company No.127776-V)
(Incorporated in Malaysia)
Risk Weighted Capital Adequacy Framework (Basel II) Pillar 3 Disclosures
as at 31 December 2010

CHIEF EXECUTIVE OFFICER'S ATTESTATION

I, Mukhtar Malik Hussain, being the Chief Executive Officer of HSBC Bank Malaysia Berhad, do hereby state that, in my opinion, the Pillar 3 Disclosures set out on pages 1-16 have been prepared according to the Risk Weighted Capital Adequacy Framework (Basel II), and are accurate and complete.

....
MUKHTAR MALIK HUSSAIN
CHIEF EXECUTIVE OFFICER
Date: 10 February 2011

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(a) Introduction

HSBC Bank Malaysia Berhad ("the Bank") is principally engaged in the provision of banking and other related financial services. The subsidiaries of the Bank are principally engaged in the businesses of Islamic Banking and nominee services. Islamic Banking operations refer generally to the acceptance of deposits and granting of financing under the principles of Shariah. The Bank and its subsidiaries are herein referred to as "the Group" in this document.

(b) Basel II

The Group's lead regulator, Bank Negara Malaysia ("BNM") sets and monitors capital requirements for the Group as a whole. With effect from 2008, the Group is required to comply with the provisions of the Basel II framework in respect of regulatory capital. The Group adopts the Standardised approach for Credit, Operational and Market Risk in its trading portfolios.

Basel II is structured around three 'pillars': minimum capital requirements, supervisory review process and market discipline. Pillar 3 aims to encourage market discipline by developing a set of disclosure requirements which allow market participants to assess certain specific information on the capital management processes, and risk assessment processes, and hence the capital adequacy of the Group. Disclosures consist of both quantitative and qualitative information and are provided at the consolidated level. Banks are required to disclose all their material risks as part of the Pillar 3 framework. All material and non-proprietary information required by Pillar 3 is included in the Risk Weighted Capital Adequacy Framework (Basel II) Pillar 3 Disclosures as at 31 December 2010. BNM permits certain Pillar 3 requirements to be satisfied by inclusion within the financial statements. Where this is the case, references are provided to relevant sections in the Financial Statements as at 31 December 2010.

(c) Consolidation basis

The basis of consolidation for financial accounting purposes is described in Note 3(a) to the financial statements and is similar to that used for regulatory purposes. The subsidiary companies of HSBC Bank Malaysia Berhad are listed in Note 14 to the financial statements, and are fully consolidated for both financial accounting and regulatory purposes.

(d) Transferability of capital and funds within the Group

HSBC Bank Malaysia Berhad is the primary provider of equity capital to its subsidiaries. Each subsidiary manages its own capital to support its planned business growth. During 2010, none of the Group's subsidiaries were subject to any significant restriction on paying dividends or repaying inter-company loans and advances.

(e) Internal assessment of capital adequacy

The Group assesses the adequacy of its capital by considering the resources necessary to cover unexpected losses arising from discretionary risks, being those which it accepts such as credit risk and market risk, or non-discretionary risks, being those which arise by virtue of its operations, such as operational and reputational risk.

The methods to undertake this assessment is contained in the Group's Internal Capital Adequacy Assessment Process (ICAAP). This process ensures that the Group's level of capital:
• Remains sufficient to support the Group's risk profile and outstanding commitments
• Exceeds the Group's formal minimum regulatory requirements
• Is capable of withstanding a severe economic downturn stress scenario

The ICAAP is a comprehensive document designed to evaluate the risk profile, processes for identifying, measuring and controlling risks, capital requirements, capital resources and compliance with standards laid down by BNM. It plays an increasingly crucial role in developing risk-based capital management capabilities, by incorporating different aspects of risk management framework including stress testing and risk appetite.

(e) Internal assessment of capital adequacy (Cont'd)

The ICAAP demonstrates the extent to which capital management is embedded in the Group. In particular, the ICAAP demonstrates the extent to which the implications of its capital buffers has been considered on a forward-looking basis by providing the analysis that the Group remains above the minimum Regulatory Capital (RC) requirement on a consolidated basis and established monitoring triggers against the Capital Adequacy Ratio.

Refer to Note 37 to the financial statements for the total risk weighted capital ratio and Tier 1 capital ratio, and risk weighted assets and capital requirements for credit risk, market risk and operational risk.

Stress Testing

Stress testing and scenario analysis form an important part of ICAAP to demonstrate that the Group can maintain risk capital sufficient enough to sustain opeartions during an economic downturn. Essentially, stress testing is to make risks more transparent by estimating the potential losses on the exposures under the abnormal market or economic conditions. It will also assess specifically the extent by which risk-weighted assets and capital requirements will increase, and how profit and loss will change. The results of the analyses will facilitate informed capital management and will help the business lines to manage their business through various measures such as establishing triggers and devising mitigation actions which can be readily implemented should the adverse scenarios materialise.

In line with BNM's Guideline on Stress Testing and the Group's Policy Paper for Stress Testing, a Stress Test Steering Committee (STSC) is established. STSC conducts stress testing on a quarterly basis based on the guidelines and methodology endorsed by the Board. The analysis makes reference to the Group's latest actual financials and Rolling Operating Plan (ROP) (the base case) to estimate the impact on profits and risk weighted assets (the gross impact). It also incorporates the impact of management actions to determine whether or not the Group is able to withstand such an event (the net impact).

Risk Appetite

Risk appetite is a central component of the Group's integrated approach to risk, capital and value management and an important mechanism to realise its strategic vision and corporate strategy. The Group's risk appetite framework describes the quantum and types of risk that the Group is prepared to take in executing its strategy. The formulation of Risk Appetite considers risk capacity, financial position, strength of the Group's core earnings and resilience of reputation and brand. It is expressed both qualitatively, describing which risks are taken and why, and quantitatively.

By developing and attaching hard, quantitative metrics within the Risk Appetite framework, the Group is seeking to further strengthen its management and governance processes in order that:

- Underlying business activity may be guided and controlled so that it continues to be aligned to the risk appetite framework;
- Key assumptions underpinning the risk appetite can be monitored and, as necessary, adjusted through subsequent business plan iterations; and
- Anticipated mitigating business decisions are flagged and acted upon promptly.

(f) Capital structure

For regulatory purposes, the Group's regulatory capital is divided into two categories, or tiers. These are Tier 1 and Tier 2. The main features of capital securities issued by the Group are disclosed below:

- Tier 1 capital includes ordinary share capital*, share premium, capital redemption reserves, retained earnings, statutory reserves and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes. (Refer to Note 37 the financial statements for the amount of Tier 1 capital and a breakdown of its components).

**Refer to Note 24 to the financial statements for further details on ordinary share capital. All ordinary shares in issue confer identical rights in respect of capital, dividends and voting.*

- Tier 2 capital includes qualifying subordinated bonds**, collective impairment allowances (excluding individual impairment allowances attributable to loans classified as impaired) and the element of the fair value reserve relating to revaluation of property. (Refer to Note 37 to the financial statements for the amount of Tier 2 capital and a breakdown of its components).

*** Refer to Note 23 to the financial statement for terms and conditions of the subordinated bonds.*

Risk Weighted Capital Adequacy Framework (Basel II) Pillar 3 Disclosures (Cont'd)

(g) Risk management policies

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

-credit risk
-liquidity risk
-market risk (includes foreign exchange, interest/profit rate and equity/commodity price risk)
-operational risk

Refer to Note 4 to the financial statements for the Group's risk managements policies on the above mentioned risks.

1) Credit Risk

Refer to Note 4 b) to the financial statements for definitions of past due and impaired loans. The approaches for the determination of individual and collective impairment provisions are detailed in Note 3 m) to the financial statements.

Table 1: Geographical distribution of loans/financing broken down by type

	2010				
Group (RM'000)	Northern	Southern	Central	Eastern	Total
Overdrafts	136,555	216,012	509,590	334,594	1,196,751
Term loans/financing					
Housing loans/financing	2,272,680	2,081,362	6,078,350	962,209	11,394,601
Syndicated term loan/financing	-	-	83,345	-	83,345
Factoring receivables	13,567	7,192	44,055	4,089	68,903
Hire purchase receivables	22,657	48,278	67,281	39,246	177,462
Lease receivables	482	83	1,620	622	2,807
Other term loans/financing	1,344,366	1,394,434	5,079,850	1,597,506	9,416,156
Bills receivable	209,084	196,739	2,134,901	150,382	2,691,106
Trust receipts	154,610	243,192	532,591	54,090	984,483
Claims on customers under acceptance credits	862,968	508,732	1,157,137	596,494	3,125,331
Staff loans/financing	33,345	34,823	301,663	28,863	398,694
Credit/charge cards	525,928	423,047	1,578,338	310,910	2,838,223
Revolving credit	58,062	93,033	2,452,879	50,645	2,654,619
Other loans/financing	1,545	2,680	1,992	2,486	8,703
Less : Unearned income	(8,383)	(11,131)	(40,410)	(6,803)	(66,727)
	5,627,466	5,238,476	19,983,182	4,125,333	34,974,457

Table 2: Geographical distribution of impaired loans/financing broken down by type

	2010				
Group (RM'000)	Northern	Southern	Central	Eastern	Total
Overdrafts	4,114	10,088	11,079	7,582	32,863
Term loans/financing					
Housing loans/financing	44,841	78,960	80,292	10,976	215,069
Hire purchase receivables	-	1,777	1,677	78	3,532
Lease receivables	-	-	11	-	11
Other term loans/financing	43,668	53,984	127,929	60,998	286,579
Bills receivable	308	6,444	1,347	2,087	10,186
Trust receipts	287	6,641	2,478	91	9,497
Claims on customers under acceptance credits	10,299	28,662	12,870	5,201	57,032
Staff loans/financing	733	105	5,327	19	6,184
Credit/charge cards	11,718	9,425	35,165	6,927	63,235
Revolving credit	-	-	1,115	-	1,115
Other loans/financing	1,544	2,677	1,888	1,069	7,178
	117,512	198,763	281,178	95,028	692,481

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

Risk Weighted Capital Adequacy Framework (Basel II) Pillar 3 Disclosures (Cont'd)

(g) Risk management policies (Cont'd)

1) Credit Risk (Cont'd)

Table 3: Residual contractual maturity of loans/financing broken down by type

	2010				
Group (RM'000)	Maturing within one year	One year to three years	Three years to five years	Over five years	Total
Overdrafts	1,196,751	-	-	-	1,196,751
Term loans/financing					
Housing loans/financing	2,016,893	72,378	192,961	9,112,369	11,394,601
Syndicated term loan/financing	-	7,887	75,458	-	83,345
Factoring receivables	68,903	-	-	-	68,903
Hire purchase receivables	8,549	95,006	73,907	-	177,462
Lease receivables	1,982	825	-	-	2,807
Other term loans/financing	2,103,879	1,660,469	1,630,305	4,021,503	9,416,156
Bills receivable	2,691,106	-	-	-	2,691,106
Trust receipts	984,483	-	-	-	984,483
Claims on customers under acceptance credits	3,125,331	-	-	-	3,125,331
Staff loans/financing	6,135	17,249	11,941	363,369	398,694
Credit/charge cards	2,838,223	-	-	-	2,838,223
Revolving credit	2,654,619	-	-	-	2,654,619
Other loans/financing	8,703	-	-	-	8,703
Less: Unearned income	(22,840)	(16,432)	(19,543)	(7,912)	(66,727)
	17,682,717	1,837,382	1,965,029	13,489,329	34,974,457

(g) Risk management policies (Cont'd)

1) Credit risk (Cont'd)

Table 4: Distribution of loans/financing by sector, broken down by type

	2010 Group (RM'000)															
	Overdraft	Housing loans/ financing	Syndicated term loans/financing	Factoring receivables	Hire purchase receivables	Lease receivables	Other term loans/financing	Bills receivable	Trust receipts	Claims on customers under acceptances credits	Staff loans/ financing	Credit/ charge card	Revolving credit	Other loans/ financing	Unearned income	Total
Agricultural, hunting, forestry and fishing	79,640	-	-	-	1,777	-	557,289	244,265	26,209	127,675	-	-	55,057	1,416	(1,593)	1,091,735
Mining and quarrying	4,820	-	-	635	6,849	-	224,494	31,274	198	3,936	-	-	105,140	-	(2,615)	374,731
Manufacturing	271,027	-	-	34,270	93,115	2,194	1,728,333	1,512,987	585,969	2,157,463	-	-	744,791	6,084	(14,618)	7,121,615
Electricity, gas and water	1,920	-	-	-	891	-	26,810	-	636	12,654	-	-	150,833	2	(74)	193,672
Construction	52,281	-	-	-	5,390	-	532,577	39,820	5,705	53,580	-	-	164,422	25	(1,195)	852,605
Real estate	24,258	-	-	-	-	-	805,959	-	-	-	-	-	432,033	205	(5,030)	1,257,425
Wholesale & retail trade and restaurants & hotels	206,424	-	-	26,282	10,924	-	338,966	275,436	311,090	686,001	-	-	196,390	936	(2,216)	2,050,233
Transport, storage and communication	37,091	-	7,887	-	9,311	-	336,265	5,006	10,013	5,938	-	-	39,276	10	(4,175)	446,622
Finance, insurance and business services	144,604	-	75,458	5,904	26,478	613	419,626	23,550	44,463	41,135	-	-	677,331	19	(5,074)	1,454,107
Household-retail	21,812	11,392,765	-	-	20,172	-	3,581,011	-	-	2,807	398,694	2,838,223	-	-	(25,219)	18,230,265
Others	352,874	1,836	-	1,812	2,555	-	864,826	558,768	200	34,142	-	-	89,346	6	(4,918)	1,901,447
	1,196,751	11,394,601	83,345	68,903	177,462	2,807	9,416,156	2,691,106	984,483	3,125,331	398,694	2,838,223	2,654,619	8,703	(66,727)	34,974,457

Table 5: Distribution of impaired loans/financing by sector, broken down by type (Group)

	2010 Group (RM'000)														
	Overdraft	Housing loans/ financing	Syndicated term loans/financing	Factoring receivables	Hire purchase receivables	Lease receivables	Other term loans/financing	Bills receivable	Trust receipts	Claims on customers under acceptances credits	Staff loans/ financing	Credit/ charge card	Revolving credit	Other loans/ financing	Total
Agricultural, hunting, forestry and fishing	-	-	-	-	-	-	955	59	170	-	-	-	-	1	1,185
Manufacturing	2,518	-	-	-	2,787	11	85,249	1,411	5,649	24,869	-	-	-	266	122,760
Construction	1,221	-	-	-	-	-	2,947	-	510	-	-	-	-	25	4,703
Real estate	2,497	-	-	-	-	-	5,888	-	-	-	-	-	-	205	8,590
Wholesale & retail trade and restaurants & hotels	7,628	-	-	-	-	-	13,810	8,716	3,168	32,164	-	-	1,115	936	67,537
Transport, storage and communication	4,327	-	-	-	80	-	6,523	-	-	-	-	-	-	10	10,940
Finance, insurance and business services	2,136	-	-	-	664	-	816	-	-	-	-	-	-	19	3,635
Household-retail	12,536	215,000	-	-	-	-	170,243	-	-	-	6,184	63,235	-	5,710	472,908
Others	-	69	-	-	-	-	148	-	-	-	-	-	-	6	223
	32,863	215,069	-	-	3,531	11	286,579	10,186	9,497	57,033	6,184	63,235	1,115	7,178	692,481

Risk Weighted Capital Adequacy Framework (Basel II) Pillar 3 Disclosures (Cont'd)

(g) Risk management policies (Cont'd)

1) Credit Risk (Cont'd)

Table 6: Past due loans/financing broken down by sector *

	2010
	Group (RM'000)
Agricultural, hunting, forestry and fishing	4,539
Manufacturing	470,175
Construction	18,013
Real estate	32,900
Wholesale & retail trade and restaurants & hotels	258,669
Transport, storage and communication	41,901
Finance, insurance and business services	13,922
Household-retail	1,811,256
Others	854
	2,652,229

Table 7: Past due loans/financing broken down by geographical location*

	2010
	Group (RM'000)
Northern region	450,076
Southern region	761,270
Central region	1,076,922
Eastern region	363,961
	2,652,229

* The amount of impaired loans broken down by sector and geographical location is disclosed in Note 11 (iii) and 11 (v) of the financial statements respectively.

Table 8: Individual and collective impairment provision broken down by sector

	2010	
	Group (RM'000)	
	Individual impairment provision	Collective impairment provison
Agricultural, hunting, forestry and fishing	1,775	16,350
Mining and quarrying	-	5,621
Manufacturing	73,644	105,720
Electricity, gas and water	-	2,905
Construction	5,048	12,714
Real estate	20,869	18,549
Wholesale & retail trade and restaurants & hotels	51,200	29,985
Transport, storage and communication	16,973	6,445
Finance, insurance and business services	936	21,797
Household-retail	208,128	270,459
Others	785	28,510
	379,358	519,055

Table 9: Individual and collective impairment provision broken down by geographical location

	2010	
	Group (RM'000)	
	Individual impairment provision	Collective impairment provison
Northern region	25,617	84,028
Southern region	64,776	77,606
Central region	251,260	296,106
Eastern region	37,705	61,315
	379,358	519,055

Risk Weighted Capital Adequacy Framework (Basel II) Pillar 3 Disclosures (Cont'd)

(g) Risk management policies (Cont'd)

1) Credit Risk (Cont'd)

Table 10: Charges and write-offs for individual impairment provisions ("IIP") during the period broken down down by sector

	2010	
	Group (RM'000)	
	IIP charges	Write-off of IIP
Agricultural, hunting, forestry and fishing	17	-
Mining and quarrying	1,374	-
Manufacturing	10,486	13,464
Electricity, gas and water	3,430	-
Construction	1,518	81
Real estate	13,221	-
Wholesale & retail trade and restaurants & hotels	3,520	4,886
Transport, storage and communication	5,688	2,537
Finance, insurance and business services	664	63
Household-retail	233,981	207,127
Others	273	803
	274,172	228,961

The reconciliation of changes in loan impairment provisions is disclosed in Note 11(ii) of the financial statements.

(g) Risk management policies (Cont'd)

1) Credit Risk (Cont'd)

i) External Credit Assessment Institutions

The standardised approach requires banks to use risk assessments prepared by External Credit Assessment Institutions ("ECAIs") to determine the risk weightings applied to rated counterparties.

ECAIs are used by the Group as part of the determination of risk weightings for the following classes of exposure:
• Sovereigns and Central Banks
• Multilateral development banks (MDBs)
• Public sector entities (PSEs)
• Corporates
• Banks
• Securities firms

For the purpose of Pillar 1 reporting to the regulator, the Group uses the external credit ratings from the following ECAIs:
• Standard & Poor's Rating Services (S&P)
• Moody's Investors Services (Moody's)
• Fitch Ratings (Fitch)
• RAM Rating Services Berhad (RAM)
• Malaysian Rating Corporation Berhad (MARC)

Data files of external ratings from the nominated ECAIs are matched with the customer records in the Group's centralised credit database. When calculating the risk-weighted value of any exposure under the standardised approach, the customer in question is identified and matched to a rating, according to BNM's selection rules. The relevant risk weight is then derived using the BNM's prescribed risk weights and rating categories mapping as appended below. All other exposure classes are assigned risk weightings as prescribed in the BNM's framework.

Sovereigns and Central Banks

Rating Category	S&P	Moody's	Fitch	Risk weight
1	AAA to AA-	Aaa to Aa3	AAA to AA-	0%
2	A+ to A-	A1 to A3	A+ to A-	20%
3	BBB+ to BBB-	Baa1 to Baa3	BBB+ to BBB-	50%
4	BB+ to B-	Ba1 to B3	BB+ to B-	100%
5	CCC+ to D	Caa1 to C	CCC+ to D	150%
Unrated	-	-	-	100%

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Risk Weighted Capital Adequacy Framework (Basel II) Pillar 3 Disclosures (Cont'd)

(g) Risk management policies (Con'td)

1) Credit Risk (Cont'd)

i) External Credit Assessment Institutions (Cont'd)

Banking Institutions

Rating Category	S&P	Moody's	Fitch	RAM	MARC	Risk weight	Risk weight (original maturity of 6 months or less)	Risk weight (original maturity of 3 months or less)
1	AAA to AA-	Aaa to Aa3	AAA to AA-	AAA to AA3	AAA to AA-	20%	20%	20%
2	A+ to A-	A1 to A3	A+ to A-	A1 to A3	A+ to A-	50%	20%	20%
3	BBB+ to BBB-	Baa1 to Baa3	BBB+ to BBB-	BBB1 to BBB3	BBB+ to BBB-	50%	20%	20%
4	BB+ to B-	Ba1 to B3	BB+ to B-	BB1 to B3	BB+ to B-	100%	50%	20%
5	CCC+ to D	Caa1 to C	CCC+ to D	C1 to D	C+ to D	150%	150%	20%
Unrated	-	-	-	-	-	50%	20%	20%

Corporate

Rating Category	S&P	Moody's	Fitch	RAM	MARC	Risk weight
1	AAA to AA-	Aaa to Aa3	AAA to AA-	AAA to AA3	AAA to AA-	20%
2	A+ to A-	A1 to A3	A+ to A-	A1 to A3	A+ to A-	50%
3	BBB+ to BB-	Baa1 to Ba3	BBB+ to BB-	BBB1 to BB3	BBB+ to BB-	100%
4	B+ to D	B1 to C	B+ to D	B1 to D	B+ to D	150%
Unrated	-	-	-	-	-	100%

Banking Institutions and Corporate (Short term ratings)

Rating Category	S&P	Moody's	Fitch	RAM	MARC	Risk weight
1	A-1	P-1	F1+, F1	P-1	MARC-1	20%
2	A-2	P-2	F2	P-2	MARC-2	50%
3	A-3	P-3	F3	P-3	MARC-3	100%
4	Others	Others	B to D	NP	MARC-4	150%

Risk Weighted Capital Adequacy Framework (Basel II) Pillar 3 Disclosures (Cont'd)

(g) Risk management policies (Cont'd)

1) Credit Risk (Cont'd)

i) External Credit Assessment Institutions (Cont'd)

Risk weights under the standardised approach as at the reporting date are reflected under Note 37 to the financial statements. Rated and unrated exposures according to ratings by ECAIs as at reporting date are as follows:-

2010
Group (RM '000)

		Ratings of Corporate by Approved ECAIs				
	S&P	AAA to AA-	A+ to A-	BBB+ to BB-	B+ to D	Unrated
	Moodys	Aaa to Aa3	A1 to A3	Baa1 to Ba3	B+ to C	Unrated
	Fitch	AAA to AA-	A+ to A-	BBB+ to BB-	B+ to D	Unrated
	RAM	AAA to AA3	A to A3	BBB to BB	B to D	Unrated
Exposure Class	MARC	AAA to AA-	A+ to A-	BBB+ to BB-	B+ to D	Unrated
On and Off Balance-Sheet Exposures						
Corporates		719,103	820,857	215,506	-	15,290,150
Total		719,103	820,857	215,506	-	15,290,150

2010
Group (RM '000)

		Ratings of Sovereigns and Central Banks by Approved ECAIs					
	S&P	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to D	Unrated
	Moodys	Aaa to Aa3	A1 to A3	Baa1 to Baa3	Ba1 to B3	Caa1 to C	Unrated
Exposure Class	Fitch	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to D	Unrated
On and Off Balance-Sheet Exposures							
Sovereigns & Central Banks		-	17,816,769	-	-	-	-
Total		-	17,816,769	-	-	-	-

2010
Group (RM '000)

		Ratings of Banking Institutions by Approved ECAIs					
	S&P	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to D	Unrated
	Moodys	Aaa to Aa3	A1 to A3	Baa1 to Baa3	Ba1 to B3	Caa1 to C	Unrated
	Fitch	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to D	Unrated
	RAM	AAA to AA3	A to A3	BBB1 to BBB3	BB1 to B3	C1+ to D	Unrated
Exposure Class	MARC	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	C+ to D	Unrated
On and Off Balance-Sheet Exposures							
Banks, MDBs and FDIs		3,186,202	1,606,692	1,230,436	19,669	-	2,665,458
Total		3,186,202	1,606,692	1,230,436	19,669		2,665,458

(g) Risk management policies (Cont'd)

1) Credit Risk (Cont'd)

ii) Credit risk mitigation ("CRM")

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

The Group’s policy when granting credit facilities is on the basis of the customer’s capacity to repay, rather than placing primary reliance on credit risk mitigation. Depending on the customer’s standing and the type of product, facilities may be provided unsecured. Mitigation of credit risk is nevertheless a key aspect of effective risk management and in the Group, takes many forms. There is no material concentration of credit risk mitigation held.

The Group’s general policy is to promote the use of credit risk mitigation, justified by commercial prudence and good practice as well as capital efficiency. Specific, detailed policies cover acceptability, structuring and terms of various types of business with regard to the availability of credit risk mitigation, for example in the form of collateral security, and these policies, together with the determination of suitable valuation parameters, are subject to regular review to ensure that they are supported by empirical evidence and continue to fulfill their intended purpose.

The most common method of mitigating credit risk is to take collateral. The principal collateral types employed by the Group are as follows:

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

Settlement risk arises in any situation where a payment in cash, securities or equities is made in the expectation of a corresponding receipt of cash, securities or equities. Daily settlement limits are established for counterparties to cover the aggregate of the Group’s transactions with each one on any single day. Settlement risk on many transactions, particularly those involving securities and equities, is substantially mitigated by settling through assured payment systems or on a delivery-versus-payment basis.

Policies and procedures govern the protection of the Group’s position from the outset of a customer relationship, for instance in requiring standard terms and conditions or specifically agreed documentation permitting the offset of credit balances against debt obligations and through controls over the integrity, current valuation and, if necessary, realisation of collateral security.

Risk Weighted Capital Adequacy Framework (Basel II) Pillar 3 Disclosures (Cont'd)

(g) Risk management policies (Cont'd)

1) Credit Risk (Cont'd)

ii) Credit risk mitigation ("CRM") (Cont'd)

The valuation of credit risk mitigants seeks to monitor and ensure that they will continue to provide the secured repayment source anticipated at the time they were taken. Where collateral is subject to high volatility, valuation is frequent; where stable, less so. The Group's policy prescribes valuation at intervals of up to two years, or more frequently as the need may arise. For property taken as collateral for new or additional facilities, a valuation report must be obtained from a panel valuer. If the property value declined by a material extent, i.e. a drop in the value of the property by more than 20%, a formal written valuation should be obtained. For auction purposes, full valuations are compulsory. This is to avoid the risk of the settlement sum being challenged by the borrower / charger on the grounds that the correct valuation was not applied.

The Group's panel of approved valuation companies is subject to an annual review. This should take into consideration the company's financial standing, accreditations, experience, professional liability insurance, major clients and size of its branch network.

The table below shows on and off balance sheet exposures before and after credit risk management.

2010
Group (RM'000)

Exposure Class	**Exposures before CRM**	**Exposures Covered by Guarantees / Credit Derivatives**	**Exposures Covered by Eligible Collateral**
Credit Risk			
On-Balance Sheet Exposures			
Sovereigns/Central Banks	17,746,419	-	-
Banks, Development Financial Institutions & MDBs	6,656,772	-	-
Corporates	13,387,801	169,674	610,330
Regulatory Retail	6,845,700	48,115	163,081
Residential Mortgages	15,588,458	-	25,282
Higher Risk Assets	1,417	-	-
Other Assets	911,335	-	-
Equity Exposure	27,604	-	-
Defaulted Exposures	459,704	-	7,299
Total for On-Balance Sheet Exposures	61,625,210	217,789	805,992
Off-Balance Sheet Exposures			
OTC Derivatives	2,865,041	-	-
Off balance sheet exposures other than OTC derivatives or credit derivatives	4,507,094	170,660	114,820
Defaulted Exposures	90,973	-	6,874
Total for Off-Balance Sheet Exposures	7,463,108	170,660	121,694
Total On and Off-Balance Sheet Exposures	**69,088,318**	**388,449**	**927,686**

(g) Risk management policies (Cont'd)

1) Credit Risk (Cont'd)

iii) Counterparty Credit Risk ("CCR")

In respect of counterparty credit risk exposures which arise from over-the-counter (OTC) derivative transactions, repo-style transactions and credit derivative contracts, a credit limit for counterparty credit risk arising from the relevant transaction is assigned, monitored and reported in accordance with the Group risk methodology. The credit limit established takes into account the gross contract amount and the future potential exposure measured on the basis of 95 percentile potential worst case loss estimates for the product involved. These methods of calculating credit exposures apply to all counterparties and differences in credit quality are reflected in the size of the limits.

The credit equivalent amount and risk-weighted amount of the relevant transaction is determined following the regulatory capital requirements. The risk-weighted amount is calculated in accordance with the counterparty risk weighting as per the standardised approach.

The policy for secured collateral on derivatives is guided by the Group's Internal Best Practice Guidelines ensuring the due-diligence necessary to fully understand the effectiveness of netting and collateralisation by jurisdiction, counterparty, product and agreement type is fully assessed and that the due-diligence standards are high and consistently applied.

Collateral Arrangements

To calculate a counterparty's net risk position for counterparty credit risk, the Group revalues all financial instruments and associated collateral positions on a daily basis. A dedicated Collateral Management function independently monitors counterparties' associated collateral positions and manages a process which ensures that calls for collateral top-ups or exposure reductions are made promptly. Processes exist for the resolution of situations where the level of collateral is disputed or the collateral sought is not received.

Eligible collateral types are documented by Credit Support Annexes (CSA) of the International Swaps and Derivatives Association (ISDA) Master Agreement and are controlled under a policy which ensures the collateral agreed to be taken exhibits characteristics such as price transparency, price stability, liquidity, enforceability, independence, reusability and eligibility for regulatory purposes. A valuation 'haircut' policy reflects the fact that collateral may fall in value between the date the collateral was called and the date of liquidation or enforcement. In practice, at least 95 percent of collateral held as credit risk mitigation under CSAs is either cash or government securities.

(g) Risk management policies (Con'td)

1) Credit Risk (Cont'd)

iii) Counterparty Credit Risk ("CCR") (Cont'd)

Credit Ratings Downgrade
It has increasingly become the practice for market participants to employ credit ratings downgrade language clauses in industry standard market agreements such as the ISDA Master Agreement as a form of risk control. These clauses are designed to trigger a series of events which may include the termination of transactions by the non-affected party, or assignment by the affected party, if its credit rating falls below a specified level.

HSBC Group controls the inclusion of credit ratings downgrade language in industry standard master agreements by requiring each Group office to obtain the endorsement of a senior member of the Global Market function and the relevant local Credit authority prior to obtaining approval from HSBC Group Risk.

The Group's position with regard to credit ratings downgrade language is monitored through reports which are produced on a regular basis. A report is produced which identifies the trigger ratings and individual details for documentation where credit ratings downgrade exists within an ISDA Master Agreement. A further report is produced which identifies the additional collateral requirements where credit ratings downgrade language affects the threshold levels within a collateral agreement. Agreements that are structured with relatively large thresholds reducing significantly in the event of a credit ratings downgrade may (dependent upon the mark-to-market at that time) create a need for counterparties to deliver sizeable single collateral payments at a time of potential financial stress.

Refer to Note 38 of the financial statements for further disclosure of off-balance sheet and counterparty credit risk.

2) Equities

At at 31 December 2010, the Group's holdings of quoted shares were made up solely of HSBC Holdings plc share awards made under the HSBC Group's Restricted Share Plan ("RSP") and Achievement Share Award ("ASA") which have not vested at reporting date. The Group's holding of unquoted shares were mainly of shares held for socio-economic reasons. The unquoted shares portfolio as at reporting date consisted mainly of Credit Guarantee Corporation, Cagamas Holdings and Global Maritime Ventures shares. The Group's policy on valuation and accounting of equity holdings is disclosed in Note 3 k(ii) of the financial statements.

Quoted equities
These shares are not held for capital gains. A reversal of mark-to-market loss of RM5,822,450 on RSP and ASA shares vested during the year, together with a mark-to-market loss of RM317,690 on holdings as at reporting date was recognised in other comprehensive income in 2010. The quoted equities are classified under the institutional segment and risk weighted at 100%.

Unquoted equities
These shares are not held for capital gains and are recorded at cost due to the lack of quoted prices in an active market or /and the fair values of the equities cannot be reliably measured. The unquoted equities are classified under the non-institutional segment and risk weighted at 100%.

Refer to Note 9 of the financial statements for further information on the Group's holdings of equity investments.

3) Interest rate risk / rate of return risk

Qualitative and quantitative information on interest rate risk / rate of return risk in the banking book is presented in Note 4 d) to the financial statements.

(h) Disclosure on the Shariah Governance Framework of HSBC Amanah Malaysia Berhad

Preamble
Shariah compliance is a cornerstone of the Islamic banking and finance industry. An effective Shariah governance policy enhances the diligent oversight of the Board of Directors, the Shariah Committee and the Management to ensure that the operations and business activities of HSBC Amanah remain consistent with Shariah principles and its requirements.

To ensure Shariah compliance in all aspects of day-to-day Islamic finance activities, the Malaysian regulatory bodies such as Bank Negara Malaysia (BNM) and Securities Commission (SC) have spelled out several provisions in relation to the establishment of a Shariah Committee and an internal Shariah Department in an Islamic Financial Institution (IFI). The Shariah Committee is an independent Shariah advisory body which plays a vital role in providing Shariah views and rulings pertaining to Islamic finance. The Shariah Committee also acts as a monitoring body to maintain Shariah compliance in the operations and business activities of the IFI. At the institutional level, the Shariah Department acts as an intermediary between the Shariah Committee and the Management team of the IFI. The Shariah Department together with the Shariah Committee have the responsibility to ensure that all activities of the IFI are in compliance with the Shariah rules and principles.

Qualitative Disclosures

Core Shariah Functions

a. Shariah Compliance and Review
i. to ensure that the operations and businesses activities of HSBC Amanah, including the end-to-end product implementation and execution of the documents, are in compliance with the decisions made by the Shariah Committee and the SC; and
ii. to regularly review the operations and business activities of HSBC Amanah including conducting post-approval transaction review and site visits to the work places of HSBC Amanah including the head office and the branches of HSBC Amanah and HSBC Bank Malaysia Berhad, whenever necessary, and to submit reports of such review to the Shariah Committee.

b. Shariah Advisory, Research, Training and Secretariat
i. to advise, review and approve any structures of products and transactions, legal documentations/terms and conditions/marketing collaterals/procedure manual/revision and/or new proposal forms/sales illustrations, brochure used to describe any product and/or campaign through the delegation of functions by Shariah Committee, and any other material the Shariah Department deems necessary to be reviewed.
ii. to participate in the Shariah Committee meetings and present queries on Shariah issues related to the operations and business of HSBC Amanah, raised by the clients or the Management;
iii. to participate constructively in structuring and developing products, preparing marketing materials and other activities related to product development cycle;
iv. together with the Shariah Committee, to represent HSBC Amanah at meetings and scholarly discussions, whenever required;
v. to assist in educating the staff of HSBC Amanah and HSBC Bank Malaysia Berhad on the Shariah principles relating to Islamic finance through seminars, training programmes, dialogue sessions, intellectual discussions and developing necessary training materials; and
vi. together with the global Shariah research team to conduct in-depth research on related Shariah matters with reference to Islamic jurisprudence literature, rulings and resolutions, Shariah standards and other scholarly texts and to present the research findings to the Shariah Committee and other relevant parties for consideration or decision.
vii. as the secretariat to the Shariah Committee, to coordinate and attend the Shariah Committee meetings, compile proposal papers, prepare and keep accurate record of minutes of the decisions and resolutions made by the Shariah Committee, which will then be communicated to the Management;
viii. to communicate any amendment to the existing approved structure made by the Shariah Committee with the relevant parties and ensure the implementation of such amendment;

In line with the new Shariah Governance Framework for Islamic Financial Institutions issued by Bank Negara Malaysia on October 2010 which has taken effect on 1st January 2011, the above core Shariah functions of HSBC Amanah will be further strengthened by other additional Shariah functions such as Shariah Audit and Shariah Risk Management which will then form a full suite of Shariah Governance functions of HSBC Amanah in the financial year 2011.