

Offshore Banking Unit

Notes to the Financial Statements as at and for the year ended 31 December 2010

1 Background

The Hongkong and Shanghai Banking Corporation Limited (HSBC), Bangladesh Branches (the Bank) commenced its banking operations in Bangladesh on 3 December 1996 after obtaining its banking licence from Bangladesh Bank on 17 April 1996. HSBC is incorporated in Hong Kong and its ultimate holding company HSBC Holdings plc (the Group) is incorporated in England.

The Bank has established an Islamic Banking Branch (Amanah branch) from 26 February 2004, on Islamic Shariah Principles based banking which is governed by the HSBC Shariah Supervisory Committee in Dubai, after obtaining its licence from Bangladesh Bank on 31 August 2003.

HSBC also operates an Offshore Banking Unit (OBU) after obtaining its licence from Bangladesh Bank on 9 July 1998.

2 Principal activities

HSBC offers a comprehensive range of financial services in Bangladesh including commercial banking, consumer banking, payments and cash management, trade services, treasury, and custody and clearing.

2.1 Commercial Banking: Commercial banking is a traditional strength of HSBC. In Bangladesh, HSBC is a popular choice for customers because of our international reach and a wide range of financial services and products. HSBC has an offshore banking unit (OBU) licence and therefore also provides foreign currency financing to qualifying customers.

2.2 Corporate and Institutional Banking: Corporate and institutional banking provides dedicated relationship management services to HSBC's clients in major corporate and financial institutions. The Bank's focus is on fostering long-term relationship based on its international connections and extensive knowledge of Asia and Asian business.

2.3 Global Markets: HSBC's Global Markets business ranks among the largest in the world and provides foreign exchange and money market services to the Central Bank, supranational, international and local corporations, institutional investors, and financial institutions as well as other market participants.

2.4 Trade & Supply Chain: Trade finance and related services are a long-standing core business of HSBC based on the depth and spread of its corporate customer base, commitment to service, highly automated trade processing systems and extensive geographic reach.

The Bank has Seven Business Development Offices in Dhaka, Chittagong, Comilla, Mongla, Adamjee, Karnaphuli and Ishwardi export processing zone focused on handling of export-import documents.

2.5 Payments and Cash Management: HSBC is one of the leading providers of payments and related services to financial institutions, corporate and personal customers in Bangladesh. Underpinned by the bank's extensive global network of offices and capabilities, payments and cash management assists companies through the provision of payments, collections, liquidity and account services. HSBCnet, a proprietary computer-based software package, provides customers with an instant link to HSBC's international computer network, allowing customers to perform transactions and obtain a diverse range of up-to-date information 24 hours a day, 365 days a year.

3 Basis of Preparation

The financial statements of the Bank are prepared on the basis of historical cost and in accordance with the Bank Companies Act 1991, in particular, Banking Regulation and Policy Department (BRPD) Circular No 14 (25 June 2003), other Bangladesh Bank Circulars, and International Accounting Standards (IAS) and International Financial Reporting standards (IFRS) as adopted by the Institute of Chartered Accountants of Bangladesh (ICAB) into Bangladesh Accounting Standards (BAS) and Bangladesh Financial Reporting Standards (BFRS) where relevant to the Bank to the extent that these do not contradict the applicable statutory provisions of Bangladesh Bank.

4 Significant accounting policies

4.1 Functional and foreign currencies

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

According to BAS 21 'The Effects of Changes in Foreign Exchange Rates' transactions in foreign currencies are recorded in the functional currency at the rate of exchange prevailing on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rate of exchange ruling at the balance sheet date.

4.2 Loans and advances to customers

Loans and advances to customers are stated in the balance sheet on a gross basis.

4.3 Deposits by customers and banks

Deposits by customers and banks are recognised when the Bank enters into the contractual provisions of the arrangements with counterparties, which is generally on trade date, and initially measured at the consideration received.

4.4 Offsetting financial assets and financial liabilities

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.

4.5 Cash and cash equivalents

For the purpose of the cash flow statement, cash and cash equivalents include highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value. Such investments are normally those with less than three months' maturity from the date of acquisition and include cash and balances at central banks, treasury bills and other eligible bills and balances with other banks and financial institutions.

4.6 Revenue Recognition

Interest income

Interest income for all loans and advances are recognised in the profit and loss account using the effective interest method. The effective interest method is a way of calculating the amortised cost of a financial asset and of allocating the interest income over the relevant period.

The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial asset or, where appropriate, a shorter period, to the net carrying amount of the financial asset.

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 of a financial asset, including transaction costs and all other premiums or discounts.

Interest income from investments

Interest income on investments in Government and other securities and bonds is accounted for on an accrual basis.

Interest expense

Interest expenses for all deposits are recognised in the profit and loss account on an accrual basis.

Commission & fee income

The Bank earns commission and fee income from a diverse range of services provided to its customers. Commission and fee income is accounted for as follows:

- ▶ income earned on the execution of a significant act is recognised as revenue when the act is completed
- ▶ income earned from services provided is recognised as revenue as the services are provided
- ▶ income which forms an integral part of the effective interest rate of a financial instrument is recognised as an adjustment to the effective interest rate

Exchange income

Exchange income includes all gains and losses from foreign currency transactions.

4.7 Operating expenses

Operating expenses incurred for the operations of the OBU are incurred by the Bank and apportioned between the Bank and OBU on the basis of total operating income.

4.8 Income tax

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

Current tax is the tax expected to be payable on the taxable profit for the year, calculated using tax rates as prescribed in the Income Tax Ordinance (ITO) 1984 and relevant Special Regulatory Orders (SRO) and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the balance sheet and the amounts attributed to such assets and liabilities for tax purposes. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which deductible temporary differences can be utilised. Deferred tax is calculated using the tax rates as prescribed in the Income Tax Ordinance (ITO) 1984 and relevant Special Regulatory Orders (SRO).

4.9 Cash flow statement

Cash flow statement has been prepared in accordance with the BAS 7 Cash Flow Statements under direct method as recommended in the BRPD Circular No. 14 dated 25 June 2003 issued by the Banking Regulation and Policy Department of Bangladesh Bank.

4.10 New Accounting Standard not yet adopted

Bangladesh Accounting Standards (BAS) 8, Accounting Policies, Changes in Accounting Estimates and Errors, Para 28 requires that an entity makes certain disclosures relating to changes in accounting policy caused by a new standard. The Institute of Chartered Accountants of Bangladesh (ICAB) has made BAS 32: Financial Instruments: Presentation, BAS 39: Financial Instruments: Recognition Measurement and BFRS 7: Financial Instruments: Disclosures effective for accounting periods beginning on or after 01 January 2010. Some of the provisions of above standards are not aligned to the requirements of the local central bank (Bangladesh Bank). Neither the Bangladesh Bank nor ICAB has yet given any guidance regarding this matter. In such circumstances, it is not possible to assess the impact of these standards on the financial statements of the Bank and accordingly the extent of the impact has not been determined.

	2010 USD	2009 USD
5 Balance with other Banks and Financial Institutions		
Inside Bangladesh	-	-
Outside Bangladesh:		
HSBC Bank, USA - USD	38,173,748	343,629
HSBC Bank, UK - GBP	4,313,434	448,173
HSBC Bank, UK - EUR	1,163,448	402,762
HSBC Hongkong - USD	500,000	32,843,120
HSBC Hongkong - GBP	2,516,394	-
HSBC Hongkong - EUR	2,650,200	-
(For detail see Annexure - B)	49,317,222	34,035,584

6 Loans and advances

Loans:

Inside Bangladesh		
Overdraft	5,871,461	4,701,689
Term loans	29,080,278	17,111,448
Import loans	72,273,617	63,512,366
	107,225,346	75,325,501
Outside Bangladesh	-	-
	107,225,346	75,325,501

Bills purchased and discounted:

Inside Bangladesh		
Import bills	1,864,019	268,351
Export bills	113,720,546	141,182,035
	115,584,565	141,450,386
Outside Bangladesh	-	-
	115,584,565	141,450,386
	222,809,911	216,775,887

6.1 Maturity grouping of loans and advances including bills discounted and purchased

Payable on demand	27,585,377	11,324,429
Payable within one month	30,552,053	35,245,715
More than one month but less than three months	101,542,989	86,841,010
More than three months but less than one year	38,784,775	73,257,824
More than one year but less than five years	15,138,873	5,116,414
Over five years	9,205,844	4,980,495
	222,809,911	216,775,887

6.2 Maturity analysis of bills purchased and discounted

Within one month	36,268,141	27,106,045
More than one month but less than three months	62,973,129	59,532,424
More than three months but less than six months	16,343,295	45,154,823
More than six months	-	9,657,094
	115,584,565	141,450,386

6.3 Unclassified, classified, doubtful and bad loans

Unclassified	222,809,911	216,659,202
Substandard	-	116,685
Doubtful	-	-
Bad/Loos	-	-
	222,809,911	216,775,887

6.4 Sector-wise classification of loans and advances

Readymade Garments and Textile	132,882,612	93,473,570
Transport	726,432	699,171
Other Manufacturing company	89,400,867	122,603,146
	222,809,911	216,775,887

6.5 Particulars of loans and advances

i) Loans considered good in respect of which the banking company is fully secured;	222,809,911	216,659,202
ii) Loans considered good against which the banking company holds no security other than the debtor's personal guarantee;	-	-
iii) Loans considered good secured by the personal undertakings of one or more parties in addition to the personal guarantee of the debtor;	-	-
iv) Loans adversely classified; provision not maintained there against;	-	-
v) Loans due by directors or officers of the banking company or any of these either separately or jointly with any other persons;	-	-
vi) Loans due from companies or firms in which the directors of the banking company have interests as directors, partners or managing agents or in case of private companies as members;	-	-
vii) Maximum total amount of advance including temporary advance made at any time during the year to directors or managers or officers of the banking companies or any of them either separately or jointly with any other person;	-	-
viii) Maximum total amount of advances, including temporary advances granted during the year to the companies or firms in which the directors of the banking company have interest as directors, partners or managing agents or in case of private companies as members;	-	-
ix) Due from banking companies	-	-
x) Classified loans and advances		
a) Classified loans and advances on which no interest is credited to income;	-	116,685
b) Provision on classified loans and advances;	-	116,579
c) Provision kept against loan classified as bad debts	-	-
d) Interest credited to the interest suspense account	-	3,054
xi) Cumulative amount of written off loans		
Opening balance	-	-
Amount written off during the year	-	-
The amount of written off loan for which law suit has been filed	-	-
6.6 Geographical Segmentation of Loans and Advances		
Dhaka (Export Processing Zone)	219,880,428	212,736,882
Chittagong (Export Processing Zone)	2,929,483	4,039,005
	222,809,911	216,775,887

7 Other assets

Interest receivable from banks and other financial institutions	41,946	46,333
Deferred commission	3,887	-
Other	542	-
	46,375	46,333

8 Borrowings from other banks, financial institutions and agents

In Bangladesh		
Bangladesh Bank	-	76,874,322
Pubali Bank Limited, Dhaka	391,260	137,532
	391,260	77,011,854
Outside Bangladesh		
HSBC, Hong Kong	111,000,000	58,500,000
	111,000,000	58,500,000
	111,391,260	135,511,854

8.1 Classification based on type of security

Secured	-	-
Unsecured	111,391,260	135,511,854
	111,391,260	135,511,854

8.2 Maturity grouping of borrowings from other banks, financial institutions and agents

Payable on demand	-	-
Payable within one month	10,050,313	62,874,322
More than one month but less than three months	68,203,062	36,611,828
More than three months but less than one year	36,137,885	37,025,704
More than one year but less than five years	-	-
	111,391,260	135,511,854

9 Deposits and other accounts

Current account	6,577,901	4,726,687
Sundry deposits	6,711,545	4,143,073
Bills payable	1,801,311	620,500
Term deposits	1,352,696	3,846,099
	16,143,453	13,336,359

9.1 Maturity analysis of deposits and other accounts

Payable on demand	11,960,536	7,773,714
Payable within one month	618,041	3,079,878
More than one month but less than three months	1,290,364	427,760
More than three months but less than one year	2,254,513	2,054,889
More than one year but less than five years	-	-
Over five years	-	-
	16,143,453	13,336,359

10 Other liabilities

Interest payable	224,949	110,325
Commission received in advance	96,190	80,963
Items in course of transmission	75,131	-
HSBC Bangladesh Branches	140,102,061	99,305,568
Specific provision (Note 10.1)	-	116,579
Interest suspense account	2,506	3,054
Others	76,036	33,822
	140,578,873	99,650,311

10.1 Specific provision

Balance as at 01 January	116,579	-
Written off during the year	-	-
Recoveries during the year	(116,579)	-
Provision made during the year	-	116,579
Balance as at 31 December	-	116,579

11 Profit and loss account

Opening balance	2,358,300	2,856,182
Profit for the year	3,951,179	3,468,107
Profit remitted to Head office	(2,248,557)	(3,954,968)
Retained profit for the year	4,061,922	2,359,300

12 Contingent liabilities and commitments

Claim against the bank not acknowledge as debt	-	-
Acceptance and endorsement	41,828,907	26,264,215
	41,828,907	26,264,215

Letter of guarantees:

Money for which the bank is contingently liable in respect of guarantees given favoring:		
Government	1,174,648	1,179,303
Bank and other financial institution	-	-
Other	1,448	-
	1,176,096	1,179,303

Irrevocable letters of credit	75,331,153	24,021,901
	75,331,153	24,021,901
	118,334,156	51,465,419

13 Interest income

Overdraft	174,324	146,519
Term loans	775,337	528,803
Import loans	2,001,599	2,174,365
Income from money market	140,606	252,455
Export bills	2,042,804	2,496,757
	5,134,670	5,606,909

14 Interest paid on deposits and borrowings

Deposit by bank	1,028,308	1,079,184
Fixed deposits	8,234	10,052
	1,036,542	1,089,236

15 Commission, exchange and brokerage

Letter of Credit issuing commission	4,072,324	2,898,933
Credit facilities	215,248	202,621
Remittance	78,663	89,034
Commission on Letter of Guarantee	2,204	239
Dealing Profit	(5,225)	139
	4,363,214	3,170,966

16 Cash and cash equivalents

Balance with other banks (Note 5)	49,317,222	34,835,584
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17 Related party transaction

The OBU, not being incorporated in Bangladesh, operates in Bangladesh under the banking licence issued by Bangladesh Bank and therefore the key management personnel of the Bank for the purposes of BAS 24 are defined as those persons having authority and responsibility for planning, directing and controlling the OBU, are members of the Board of Directors of the Group, Group Managing Directors, and close members of their families and companies they control, or significantly influence, or for which significant voting power is held.

17.1 Transactions with key management personnel

There were no transaction between the OBU and the key Management Personnel of the OBU in 2010 (2009: BDT nil).

17.2 Transactions, arrangements and agreements involving key management personnel

The OBU provides and receives certain banking and financial services to/from entities within the Group. As at year end the balances with these entities is disclosed in Note 5, Balance with other banks and financial institutions and Note 8, Borrowings from other banks, financial institutions and agents.

The disclosure of the year end balance is considered to be the most meaningful information to represent transactions during the year. The outstanding balances includes loans made to or deposits by the OBU and arose in the ordinary course of business and are on substantially the same terms, including interest rates and security, as for comparable transactions with third party counterparties. Interest income received by the OBU from these entities during 2010 amounted to USD140,606 (2009:USD262,455) and interest expense paid to these entities during 2010 amounted to USD607,796 (2009:USD930,964), both of which is included in the net interest income disclosed in the profit and loss account.

17.3 Transactions with other related parties of the Bank

The OBU provides certain banking and financial services and administrative services to the Bank operating in Bangladesh under the banking licence issued by Bangladesh Bank. As at year end the balance with the Bank is disclosed in Note 10, Other Liabilities.

Operating expenses incurred by the Bank for the operations of the Bank and OBU are apportioned to each entity on the basis of total operating income and reported in the profit and loss account. Income tax assessed for the Bank and the OBU are paid by the Bank and the element relating to the OBU is recharged back to the OBU as disclosed in Note 10, Other liabilities. The Bank does not charge the OBU any fees for the provision of administrative services.

18 Events after the balance sheet date

There were no material adjusting events after the balance sheet date.

19 General

19.1 Audit Committee

According to BRPD Circular No.12 (23 December 2002), all banks are advised to constitute an Audit Committee comprising of members of the Board. The Audit Committee will assist the board in fulfilling its oversight responsibilities including implementation of the objectives, strategies and overall business plans set by the board for effective functioning of the bank. The committee will review the financial reporting process, the system of internal control and management of financial risks, the audit process, and the bank's process for monitoring compliance with laws and regulations and its own code of business conduct.


The Bank, being a foreign bank, does not have a local Board of Directors from whom to select an Audit Committee, however, the Bank has received a dispensation from Bangladesh Bank on 19 December 2006 with regards to this requirement. The Bank has an Internal Audit department reporting directly to the CEO of the Bank. In addition to this the Bank is subject to audit by the internal auditors of HSBC and the internal auditors of the Group.

The Group has an Audit Committee, comprising of four non-executive Directors of the Group, which meets on a regular basis with the senior management of the Group, and with the internal and external auditors to consider and review the nature and scope of the reviews and the effectiveness of the systems of internal control and compliance as well as the financial statements of the Group. All audit reports issued by local internal and external auditor and all inspection/ audit reports issued by Bangladesh Bank are sent to the Audit Committees of HSBC in Hongkong and the Group in the UK.

19.2 Assets and liabilities have been converted into Taka currency @ USD 1 = Tk 70.82 which represents the year-end middle rate of exchange as at 31 December 2010.

19.3 Previous year's figures have been rearranged, where necessary, to conform to current year's presentation.

19.4 Figures appearing in these Financial Statements have been rounded off to the nearest integer.


Sanjay Prakash
Chief Executive Officer, Bangladesh


Nayeem Rahman Chowdhury
Chief Financial Officer, Bangladesh

Dhaka, 14 February 2011

Statement of Liquidity (Assets & Liabilities Maturity Analysis) As at 31 December 2010

Annexure - A

Particulars	Maturity within	Maturity within	Maturity within	Maturity within	Maturity over	Total
	1 month	1 to 3 months	3 to 12 months	1 to 5 years	5 years	
	BDT	BDT	BDT	BDT	BDT	BDT
ASSETS						
Cash in hand	-	-	-	-	-	-
Balance with other banks and financial institutions	49,317,222	-	-	-	-	49,317,222
Money at call and short notice	-	-	-	-	-	-
Investment in Treasury Bills & others	-	-	-	-	-	-
Loans & advances to customers (Note 8.1)	58,137,430	101,542,989	38,784,775	15,138,873	9,205,844	222,809,911
Fixed assets	-	-	-	-	-	-
Other assets	46,375	-	-	-	-	46,375
Non-banking assets	-	-	-	-	-	-
Total Assets	107,501,027	101,542,989	38,784,775	15,138,873	9,205,844	272,173,508
LIABILITIES						
Borrowings from other banks & financial institutions (Note 8.2)	10,060,313	66,203,062	35,137,885	-	-	111,391,260
Deposits & other accounts	12,598,576	1,290,364	2,254,513	-	-	16,143,453
Other liabilities (including capital/shareholders equity)	40,102,061	474,812	4,061,922	-	-	144,638,795
Total Liabilities	162,750,950	67,968,238	41,454,320	-	-	272,173,508
Net Liquidity Difference	(55,249,923)	33,574,751	(2,669,545)	15,138,873	9,205,844	-

Balance with other banks and financial institutions - Outside Bangladesh (Note 5) As at 31 December 2010

Annexure - B

Name of the Banks	Currency Name	RCY	Rate	Foreign Currency (USD)	RCY	Rate	Foreign Currency (USD)
HSBC Bank USA	USD	38,173,748	1.0000	38,173,748	343,529	1.0000	343,529
HSBC Bank UK	GBP	2,794,037	1.5438	4,313,434	446,173	1.5874	446,173
HSBC Bank UK	EUR	878,007	1.3251	1,163,446	402,762	1.4358	402,762
HSBC, Hong Kong	USD	500,000	1.0000	500,000	-	-	-
HSBC, Hong Kong	GBP	1,630,000	1.5438	2,516,394	32,843,120	1.5874	32,843,120
HSBC, Hong Kong	EUR	2,000,000	1.3251	2,650,200	-	-	-
Total				49,317,222			34,035,584