

## REPORT OF THE DIRECTORS

The Directors have pleasure in presenting their report together with the audited financial statements for the year ended 31 December 2008.

### PRINCIPAL ACTIVITIES

The Bank and its subsidiaries and associates are engaged in the provision of banking and related financial services.

### PROFITS

The consolidated profit of the Bank and its subsidiaries and associates for the year together with particulars of dividends which have been paid or declared are set out on page 89 of the Annual Report.

### MAJOR CUSTOMERS

The Directors believe that the five largest customers of the Bank accounted for less than 30% of the total interest income and other operating income of the Bank for the year.

### SUBSIDIARIES

Particulars of the Bank's principal subsidiaries as at 31 December 2008 are set out in note 37 to the financial statements for the year ended 31 December 2008.

### SHARE CAPITAL

No change in either the authorised or issued share capital took place during the year.

### DONATIONS

Charitable donations made by the Bank and its subsidiaries during the year amounted to HK\$13.8 million.

### RESERVES

Profit attributable to shareholders, before dividends, of HK\$14,099 million (2007: HK\$18,242 million) have been transferred to reserves. Details of the movements in reserves, including the appropriations therefrom, are set out in note 53 to the financial statements.

### DIRECTORS

The Directors of the Bank who were in office as at the end of the year were Dr Raymond K F Ch'ien, Mr Raymond C F Or, Mr Edgar D Ancona, Mr John C C Chan, Mr Patrick K W Chan,

Dr Y T Cheng, Dr Marvin K T Cheung, Mr Alexander A Flockhart, Mr Jenkin Hui, Mr Peter T C Lee, Dr Eric K C Li, Dr Vincent H S Lo, Mr Joseph C Y Poon, Dr David W K Sin, Mr Richard Y S Tang and Mr Peter T S Wong.

The Directors retiring by rotation in accordance with the Bank's Articles of Association are Mr Raymond C F Or, Mr Patrick K W Chan, Mr Peter T C Lee, Mr Richard Y S Tang and Mr Peter T S Wong. Mr Raymond C F Or has informed the Board of his intention of not seeking re-election at the Bank's Annual General Meeting to be held on 6 May 2009 (the "2009 AGM") for the reason set out below. All the other above mentioned Directors will offer themselves for re-election at the 2009 AGM.

Mr Raymond C F Or will retire as Vice-Chairman and Chief Executive of the Bank and from the Board with effect from the conclusion of the 2009 AGM. Mrs Margaret K M Y Leung will be appointed a non-executive Director of the Bank with effect from 1 April 2009 until the conclusion of the 2009 AGM and being eligible, will offer herself for election by shareholders at the 2009 AGM. Subject to being elected by the shareholders and upon Mr Or's retirement as aforesaid, Mrs Leung will become Vice-Chairman and Chief Executive of the Bank with effect from the conclusion of the 2009 AGM.

Apart from the aforesaid prospective changes to the Board composition, Dr Y T Cheng and Dr David W K Sin have also tendered their resignation from the Board with effect from the conclusion of the 2009 AGM in order to devote more time to their own businesses.

The Board announces the above changes to the Board composition on 2 March 2009. For further details of the above changes to Board composition, shareholders may refer to the announcement issued by the Bank and uploaded on the Bank's website at [www.hangseng.com](http://www.hangseng.com).

No Director proposed for re-election at the forthcoming Annual General Meeting has a service contract with the Bank which is not determinable by the Bank within one year without payment of compensation (other than statutory compensation).

The biographical details of the Directors of the Bank are set out in the section "Biographical Details of Directors" of this Annual Report.

## STATUS OF INDEPENDENT NON-EXECUTIVE DIRECTORS

The Bank has received from each independent non-executive Director an annual confirmation of his independence pursuant to Rule 3.13 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Stock Exchange") ("the Listing Rules") and the Bank still considers the independent non-executive Directors to be independent.

## DIRECTORS' AND ALTERNATE CHIEF EXECUTIVES' INTERESTS

### Interests in shares

As at 31 December 2008, the interests of the Directors and Alternate Chief Executives in the shares, underlying shares of equity derivatives and debentures of the Bank and its associated corporations (all within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) disclosed in accordance with the Listing Rules were detailed below.

	Personal Interests (held as beneficial owner)	Family Interests (Interests of spouse or child under 18)	Corporate Interests (Interests of controlled corporation)	Other Interests	Total Interests	Total Interests as % of the relevant issued share capital
<b>Number of Ordinary Shares of HK\$5 each in the Bank</b>						
<b>Directors:</b>						
Mr Raymond C F Or	50,000	–	–	–	50,000	0.00
Mr John C C Chan	–	–	–	1,000 <sup>(1)</sup>	1,000	0.00
Mr Patrick K W Chan	–	1,000	–	–	1,000	0.00
Mr Joseph C Y Poon	5,000	10,000	–	–	15,000	0.00
<b>Number of Ordinary Shares of US\$0.50 each in HSBC Holdings plc</b>						
<b>Directors:</b>						
Dr Raymond K F Ch'ien	57,704	–	–	–	57,704	0.00
Mr Raymond C F Or	235,408	40,878	–	156,671 <sup>(6)</sup>	432,957	0.00
Mr Edgar D Ancona	253,195	–	–	499,504 <sup>(6)</sup>	752,699	0.01
Mr John C C Chan	14,283	–	–	3,000 <sup>(1)</sup>	17,283	0.00
Mr Patrick K W Chan	8,091	5,563	–	63,377 <sup>(6)</sup>	77,031	0.00
Mr Alexander A Flockhart	172,583	–	–	385,976 <sup>(6)</sup>	558,559	0.00
Mr Jenkin Hui	11,627	24,342	1,288,422 <sup>(2)</sup>	–	1,324,391	0.01
Dr Eric K C Li	–	18,132	79,622 <sup>(3)</sup>	–	97,754	0.00
Mr Joseph C Y Poon	24,304 <sup>(4)</sup>	66,314	–	55,886 <sup>(6)</sup>	146,504	0.00
Mr Peter T S Wong	131,786	23,164	–	142,171 <sup>(6)</sup>	297,121	0.00
<b>Alternate Chief Executives:</b>						
Mr William W Leung	19,740	–	–	47,673 <sup>(6)</sup>	67,413	0.00
Mrs Dorothy K Y P Sit	18,834 <sup>(5)</sup>	728	–	39,418 <sup>(6)</sup>	58,980	0.00

Notes:

- (1) 1,000 shares in the Bank and 3,000 shares in HSBC Holdings plc were held by a trust of which Mr and Mrs John C C Chan were beneficiaries.
- (2) Mr Jenkin Hui was entitled to fully control the voting power at general meetings of Parc Palais Incorporated, a private company, which beneficially held all of those shares referred to above as his corporate interests.
- (3) Dr Eric K C Li was entitled to control no less than one-third of the voting power at general meetings of a private company which beneficially held all of those shares referred to above as his corporate interests.
- (4) 22,599 shares were jointly held by Mr and Mrs Joseph C Y Poon.
- (5) 5,680 shares were jointly held by Mrs Dorothy K Y P Sit and her husband.

(6) These represented interests in (i) options granted to Directors and Alternate Chief Executives under the HSBC Share Option Plans/HSBC Finance 1996 Long-Term Executive Incentive Compensation Plan to acquire ordinary shares of US\$0.50 each in HSBC Holdings plc and (ii) conditional awards of shares under the HSBC Share Plans made in favour of Directors and Alternate Chief Executives and held by various trusts for ordinary shares of US\$0.50 each in HSBC Holdings plc, as set against their respective names below:

	Options (please refer to the options table below for details)	Conditional awards of shares under the HSBC Share Plans (please refer to the awards table below for further information)	Total
<b>Directors:</b>			
Mr Raymond C F Or	2,504	154,167	156,671
Mr Edgar D Ancona	394,913	104,591	499,504
Mr Patrick K W Chan	28,203	35,174	63,377
Mr Alexander A Flockhart	1,332	384,644	385,976
Mr Joseph C Y Poon	14,704	41,182	55,886
Mr Peter T S Wong	–	142,171	142,171
<b>Alternate Chief Executives:</b>			
Mr William W Leung	12,500	35,173	47,673
Mrs Dorothy K Y P Sit	5,435	33,983	39,418

## Options

As at 31 December 2008, the Directors and Alternate Chief Executives mentioned below held unlisted physically settled options to acquire the number of ordinary shares of US\$0.50 each in HSBC Holdings plc set against their respective names. These options were granted for nil consideration by HSBC Holdings plc.

	Options held as at 31 December 2008	Options exercised during the year (ordinary shares of US\$0.50 each)	Exercise price per share	Date granted	Exercisable from	Exercisable until
<b>Directors:</b>						
Mr Raymond C F Or	1,515	–	£6.4720	10 May 2004	1 Aug 2009	31 Jan 2010
	989	–	£6.6792	24 May 2005	1 Aug 2010	31 Jan 2011
	2,504					
Mr Edgar D Ancona	–	64,200 <sup>(1)&amp;(2)</sup>	US\$13.7100	9 Nov 1998	9 Nov 1999	9 Nov 2008
	80,250 <sup>(1)</sup>	–	US\$16.9600	8 Nov 1999	8 Nov 2000	8 Nov 2009
	85,600 <sup>(1)</sup>	–	US\$18.4000	13 Nov 2000	13 Nov 2001	13 Nov 2010
	93,625 <sup>(1)</sup>	–	US\$21.3700	12 Nov 2001	12 Nov 2002	12 Nov 2011
	33,438 <sup>(1)</sup>	–	US\$10.6600	20 Nov 2002	20 Nov 2003	20 Nov 2012
	51,000	–	£9.1350	3 Nov 2003	3 Nov 2006	3 Nov 2013
	51,000	–	£8.2830	30 Apr 2004	30 Apr 2007	30 Apr 2014
394,913						

	Options held as at 31 December 2008	Options exercised during the year (ordinary shares of US\$0.50 each)	Exercise price per share	Date granted	Exercisable from	Exercisable until
Mr Patrick K W Chan	6,500	–	£7.4600	3 Apr 2000	3 Apr 2003	2 Apr 2010
	6,000	–	£8.7120	23 Apr 2001	23 Apr 2004	22 Apr 2011
	6,500	–	£8.4050	7 May 2002	7 May 2005	6 May 2012
	7,000	–	£6.9100	2 May 2003	2 May 2006	1 May 2013
	2,203 <sup>(3)</sup>	–	HK\$108.4483	25 Apr 2007	1 Aug 2012	31 Jan 2013
	28,203					
Mr Alexander A Flockhart	–	22,500 <sup>(4)</sup>	£6.2767	16 Mar 1998	16 Mar 2001	16 Mar 2008
	1,332	–	£7.0872	25 Apr 2007	1 Aug 2010	31 Jan 2011
	1,332					
Mr Joseph C Y Poon	–	9,000 <sup>(5)</sup>	£6.3754	29 Mar 1999	29 Mar 2002	29 Mar 2009
	–	4,750 <sup>(5)</sup>	£7.4600	3 Apr 2000	3 Apr 2003	3 Apr 2010
	2,750	–	£8.7120	23 Apr 2001	23 Apr 2004	23 Apr 2011
	4,400	–	£8.4050	7 May 2002	7 May 2005	7 May 2012
	5,050	–	£6.9100	2 May 2003	2 May 2006	2 May 2013
	1,515	–	£6.4720	10 May 2004	1 Aug 2009	31 Jan 2010
	989	–	£6.6792	24 May 2005	1 Aug 2010	31 Jan 2011
	14,704					
<b>Alternate Chief Executives:</b>						
Mr William W Leung	6,000	–	£6.9100	2 May 2003	2 May 2006	1 May 2013
	6,500	–	£8.2830	30 Apr 2004	30 Apr 2007	29 Apr 2014
	12,500					
Mrs Dorothy K Y P Sit	3,000	–	£8.7120	23 Apr 2001	23 Apr 2004	22 Apr 2011
	2,435	–	£6.6792	24 May 2005	1 Aug 2010	31 Jan 2011
	5,435					

## Notes:

- (1) These represented Mr Edgar D Ancona's interests in options under HSBC Finance 1996 Long-Term Executive Incentive Compensation Plan. These options arise from options he held over shares of Household International, Inc. (now HSBC Finance Corporation) before its acquisition, which were converted into options over HSBC Holdings plc ordinary shares in the same ratio as the offer for HSBC Finance Corporation and the exercise prices per share adjusted accordingly. These options were granted at nil consideration.
- (2) As at the date of exercise, 26 September 2008, the market value per share was £8.7900.
- (3) Notification that Mr Patrick K W Chan held these unlisted physically settled options to acquire shares of US\$0.50 each in HSBC Holdings plc was given by him in January 2009 on his becoming aware of the same.
- (4) As at the date of exercise, 4 March 2008, the market value per share was £7.6900.
- (5) As at the date of exercise, 15 May 2008, the market value per share was £8.9200.

### Conditional awards of shares

As at 31 December 2008, the interests of the Directors and Alternate Chief Executives in the conditional awards of shares made in favour of them under the HSBC Share Plans and held by various trusts for ordinary shares of US\$0.50 each in HSBC Holdings plc were as follows:

	Awards held as at 1 January 2008	Awards made during the year	Shares awarded released during the year	Awards held as at 31 December 2008
<b>Directors:</b>				
Mr Raymond C F Or	198,569	62,060	35,587	154,167 <sup>(1)&amp;(2)</sup>
Mr Edgar D Ancona	103,733	33,333	38,327	104,591 <sup>(1)</sup>
Mr Patrick K W Chan	26,511	12,425	5,445	35,174 <sup>(1)</sup>
Mr Alexander A Flockhart	322,411	139,103	33,573	384,644 <sup>(1)&amp;(2)</sup>
Mr Joseph C Y Poon	38,100	14,545	6,836	41,182 <sup>(1)&amp;(2)</sup>
Mr Peter T S Wong	82,700	52,261	–	142,171 <sup>(1)</sup>
<b>Alternate Chief Executives:</b>				
Mr William W Leung	34,469	12,425	6,836	35,173 <sup>(1)&amp;(2)</sup>
Mrs Dorothy K Y P Sit	42,911	12,121	6,836	33,983 <sup>(1)&amp;(2)</sup>

Notes:

(1) This includes additional shares arising from scrip dividends.

(2) This takes into account the forfeiture of shares under the relevant Share Plan(s).

All the interests stated above represent long positions. As at 31 December 2008, no short positions were recorded in the Register of Directors' and Alternate Chief Executives' Interests and Short Positions required to be kept under section 352 of the SFO.

Save as disclosed in the preceding paragraphs, at no time during the year was the Bank or any of its holding companies or its subsidiaries or fellow subsidiaries a party to any arrangement to enable the Directors of the Bank to acquire benefits by means of the acquisition of shares in or debentures of the Bank or any other body corporate.

No right to subscribe for equity or debt securities of the Bank has been granted by the Bank to, nor have any such rights been exercised by, any person during the year ended 31 December 2008.

### DIRECTORS' INTERESTS IN CONTRACTS

No contract of significance, to which the Bank or any of its holding companies or any of its subsidiaries or fellow subsidiaries was a party and in which a Director of the Bank had a material interest, subsisted as at the end of the year or at any time during the year.

### DIRECTORS' INTERESTS IN COMPETING BUSINESSES

Pursuant to Rule 8.10 of the Listing Rules, as at the end of the year, the following Directors had declared interests in the following entities which compete or are likely to compete, either directly or indirectly, with the businesses of the Bank:

Mr Alexander A Flockhart is Group Managing Director Asia-Pacific and an executive Director of HSBC Holdings plc, a Director and the Chief Executive Officer of The Hongkong and Shanghai Banking Corporation Limited and Global Head of Commercial Banking of HSBC Group. He is also the Chairman and a non-executive Director of HSBC Bank Malaysia Berhad, Vice-Chairman and a Director of HSBC Bank (Vietnam) Limited, a Director of HSBC Bank Australia Limited and a non-executive Director of HSBC Bank (China) Company Limited.

Mr Raymond C F Or is a Director of The Hongkong and Shanghai Banking Corporation Limited.

Mr Edgar D Ancona is the Chief Financial Officer of The Hongkong and Shanghai Banking Corporation Limited. He is also a Director of certain subsidiaries of HSBC Holdings BV, including HSBC Asia Holdings BV, the immediate holding company of The Hongkong and Shanghai Banking Corporation Limited.

Mr Patrick K W Chan is a Director, an Executive Committee member and a Remuneration Committee member of Industrial Bank Co., Ltd (“Industrial Bank”), in which the Bank holds a 12.78% stake. Industrial Bank conducts general banking business in mainland China.

Mr Peter T S Wong is Group General Manager of HSBC Holdings plc and Executive Director, Hong Kong and mainland China of The Hongkong and Shanghai Banking Corporation Limited. He is a Director and Chairman of HSBC Insurance (Asia) Limited and HSBC Life (International) Limited, non-executive Director and Deputy Chairman of HSBC Bank (China) Company Limited and non-executive Director and Chairman of Hubei Suizhou Cengdu HSBC Rural Bank Company Limited, Chongqing Dazu HSBC Rural Bank Company Limited, Fujian Yongan HSBC Rural Bank Company Limited and Beijing Miyun HSBC Rural Bank Company Limited, all being subsidiaries of The Hongkong and Shanghai Banking Corporation Limited. He is a non-executive Director of Bank of Communications Co., Ltd, which conducts general banking business. He is also a non-executive Director of Ping An Insurance (Group) Company of China, Ltd, which conducts life insurance, property and casualty insurance and other financial services.

HSBC Holdings plc, through its subsidiaries and associated undertakings, including The Hongkong and Shanghai Banking Corporation Limited, the immediate holding company of the Bank, is engaged in providing a comprehensive range of banking, insurance and related financial services.

The entities in which the Directors have declared interests are managed by separate Boards of Directors and management, which are accountable to their respective shareholders.

Further, Industrial Bank has an Audit and Related Party Transactions Control Committee which is responsible for considering all matters concerning connected party transactions to be entered into by Industrial Bank as required by the laws of mainland China. All members of Industrial Bank’s Audit and Related Party Transactions Control Committee are independent non-executive Directors.

The Board of the Bank includes nine independent non-executive Directors whose views carry significant weight in the Board’s decisions. The Audit Committee of the Bank, which consists of three independent non-executive Directors, meets regularly to assist the Board of Directors in reviewing the financial performance, internal control and compliance systems of the Bank and its subsidiaries. The Bank is, therefore, capable of carrying on its businesses independently of, and at arm’s length from, the businesses in which Directors have declared interests.

### DIRECTORS’ EMOLUMENTS

The emoluments of the Directors of the Bank (including executive Directors and independent non-executive Directors) on a named basis are set out in note 19 to the financial statements for the year ended 31 December 2008.

### SUBSTANTIAL INTERESTS IN SHARE CAPITAL

The register maintained by the Bank pursuant to the SFO recorded that, as at 31 December 2008, the following corporations had interests or short positions in the shares or underlying shares (as defined in the SFO) in the Bank set opposite their respective names:

Name of Corporation	Number of Ordinary Shares of HK\$5 each in the Bank (Percentage of total)
The Hongkong and Shanghai Banking Corporation Limited	1,188,057,371 (62.14%)
HSBC Asia Holdings BV	1,188,057,371 (62.14%)
HSBC Asia Holdings (UK) Limited	1,188,057,371 (62.14%)
HSBC Holdings BV	1,188,057,371 (62.14%)
HSBC Finance (Netherlands)	1,188,057,371 (62.14%)
HSBC Holdings plc	1,188,057,371 (62.14%)

The Hongkong and Shanghai Banking Corporation Limited is a subsidiary of HSBC Asia Holdings BV, which is a wholly-owned subsidiary of HSBC Asia Holdings (UK) Limited (formerly known as "HSBC Asia Holdings (UK)"), which in turn is a wholly-owned subsidiary of HSBC Holdings BV. HSBC Holdings BV is a wholly-owned subsidiary of HSBC Finance (Netherlands), which in turn is a wholly-owned subsidiary of HSBC Holdings plc. Accordingly, The Hongkong and Shanghai Banking Corporation Limited's interests are recorded as the interests of HSBC Asia Holdings BV, HSBC Asia Holdings (UK) Limited, HSBC Holdings BV, HSBC Finance (Netherlands) and HSBC Holdings plc.

The Directors regard HSBC Holdings plc to be the beneficial owner of 1,188,057,371 ordinary shares in the Bank (62.14%).

All the interests stated above represent long positions. As at 31 December 2008, no short positions were recorded in the Register of Interests in Shares and Short Positions required to be kept under section 336 of the SFO.

#### **PURCHASE, SALE OR REDEMPTION OF THE BANK'S LISTED SECURITIES**

During the year, there was no purchase, sale or redemption by the Bank, or any of its subsidiaries, of the Bank's listed securities.

#### **PUBLIC FLOAT**

As at the date of this report, the Bank has maintained the prescribed public float under the Listing Rules, based on the information that is publicly available to the Bank and within the knowledge of the Directors of the Bank.

#### **CODE ON CORPORATE GOVERNANCE PRACTICES**

Details of the Bank's corporate governance practices are set out in the "Corporate Governance and Other Information" section in this Annual Report.

#### **AUDITORS**

KPMG retire and, being eligible, offer themselves for re-appointment. A resolution for the re-appointment of KPMG as auditors of the Bank will be proposed at the forthcoming Annual General Meeting.

On behalf of the Board

#### **Raymond Ch'ien**

Chairman

Hong Kong, 2 March 2009