HSBC Holdings plc

Strategic Report 2016

HSBC

Connecting customers to opportunities

Our purpose is to be where the growth is, enabling businesses to thrive and economies to prosper, and ultimately helping people to fulfil their hopes and realise their ambitions.

Contents

As a reminder

Reporting currency
We use US dollars.

Adjusted measures
We supplement our IFRS figures with adjusted measures used by management internally. These measures are highlighted with the following symbol:

Further explanation may be found on page 30 of the *Annual Report and Accounts 2016*.

Unless stated otherwise, risk-weighted assets and capital are calculated and presented on a transitional CRD IV basis as implemented by the Prudential Regulation Authority.

Our photo competition winners

In 2016, we ran a Group-wide photo competition which attracted over 6,200 submissions from 1,100 employees. The joint overall winning photos are featured in this report. The image on the inside front cover shows a rice farmer at harvest time in north-east Vietnam, and the photo on the inside back cover was taken at sunrise at Situ (Lake) Patenggang, West Java, Indonesia.

Cover image
The Hong Kong-Zhuhai-Macau Bridge is one of the most ambitious infrastructure projects in the Pearl River Delta. It will link three key cities, cutting transport costs and travelling times, and boosting economic development. HSBC has extended a HK$700m receivables finance facility to one of the companies building the bridge. Receivables finance is an area where HSBC has particular expertise, and this facility is the largest it has provided for infrastructure in the region.

Overview

This Strategic Report was approved by the Board on 21 February 2017.

Douglas Flint, Group Chairman

Highlights

We are one of the most international banking and financial services organisations in the world.

Group

For year ended 31 Dec 2016

Reported profit before tax ($bn)

2016	7.1
2015	18.9
2014	18.7

(2015: $18.9bn)

$7.1bn

Adjusted profit before tax ($bn)

2016	19.3
2015	19.5
2014	21.6

(2015: $19.5bn)

$19.3bn

Reported revenue ($bn)

2016	48.0
2015	59.8
2014	61.2

(2015: $59.8bn)

$48.0bn

At 31 Dec 2016

Risk-weighted assets ($bn)

2016	857
2015	1,103
2014	1,220

(2015: $1,103bn)

$857bn

Common equity tier 1 ratio (%)

2016	13.6
2015	11.9
2014	10.9

(2015: 11.9%)

13.6%

Total assets ($bn)

2016	2,375
2015	2,410
2014	2,634

(2015: $2,410bn)

$2,375bn

Our operating model consists of four global businesses, a Corporate Centre and five geographical regions, supported by 11 global functions.

During the year, we changed our reportable segments from regions to global businesses. We also moved certain business portfolios and functions into the newly created Corporate Centre.

For further details, see page 19.

Performance highlights for 2016

Strategy execution

- Following our sale of operations in Brazil, we completed a $2.5bn share buy-back.
- We further reduced our risk-weighted assets ('RWAs') as a result of our sale of operations in Brazil and other management actions.
- Investment in costs to achieve of $4.0bn to date has generated annual run rate savings of $3.7bn.
- We now expect to deliver annualised cost savings of around $6bn by the end of 2017, around $1bn above the top end of our original target, while continuing to invest in regulatory programmes and compliance. We will invest an equivalent total of around $6bn over the same timeframe.
- We increased market share in a number of key markets and international product areas, including trade finance in Hong Kong and Singapore.

Financial performance

- Reported profit before tax of $7.1bn was $11.8bn lower than in 2015, and was adversely impacted by significant items of $12.2bn. These included a $3.2bn write-off of goodwill in our Global Private Banking ('GPB') business in Europe, costs to achieve of $3.1bn, adverse fair value movements of $1.8bn arising from changes in credit spreads on our own debt designated at fair value, and the impact of our sale of operations in Brazil.
- Reported revenue of $48.0bn was down $11.8bn. Loan impairment charges and other credit risk provisions ('LICs') fell by $0.3bn and reported operating expenses rose by $40m.
- Adjusted profit before tax of $19.3bn, down $0.2bn, reflected lower revenue and higher LICs, partly offset by a reduction in operating expenses. In 2016, we achieved positive adjusted jaws of 1.2%.
- Adjusted revenue fell by $1.3bn or 2% despite improved performance in Commercial Banking ('CMB') and Global Banking and Markets ('GB&M'). Retail Banking and Wealth Management ('RBWM') and GPB were impacted by challenging market conditions.
- Adjusted operating expenses fell by $1.2bn or 4%, reflecting our cost-saving initiatives and focus on cost management. We continued to invest in regulatory programmes and compliance.

Capital

- Our capital position further strengthened during the year, with a common equity tier 1 ('CET1') ratio at 31 December 2016 of 13.6%, up from 11.9% at 31 December 2015, mainly due to RWA reduction initiatives and the change in the regulatory treatment of our holding in Bank of Communications Co., Limited ('BoCom').

0.8%
Return on equity

1.2%
Adjusted jaws
(see page 17)

$0.51
Dividends per ordinary share in respect of 2016

Our global businesses

Retail Banking and Wealth Management ('RBWM')

We help millions of people across the world to manage their finances, buy their homes, and save and invest for the future. Our Insurance and Asset Management businesses support all our global businesses in meeting their customers' needs.

Commercial Banking ('CMB')

We support approximately two million business customers in 54 countries with banking products and services to help them operate and grow. Our customers range from small enterprises focused primarily on their domestic markets, through to large companies operating globally.

Global Banking and Markets ('GB&M')

We provide financial services and products to companies, governments and institutions. Our comprehensive range of products and solutions, across capital financing, advisory and transaction banking services, can be combined and customised to meet clients' specific objectives.

Global Private Banking ('GPB')

We help high net worth individuals and their families to grow, manage and preserve their wealth.

	RBWM	CMB	GB&M	GPB
Adjusted profit before tax	$5.3bn	$6.1bn	$5.6bn	$0.3bn
Risk-weighted assets	$115.1bn	$275.9bn	$300.4bn	$15.3bn

Geographical regions

	Reported profit/(loss) before tax ($bn)	Adjusted profit before tax ($bn)	Risk-weighted assets* ($bn)
Europe	(6.8)	1.6	298.4
Asia	13.8	14.2	334.0
Middle East and North Africa	1.5	1.6	59.1
North America	0.2	1.3	150.7
Latin America	(1.6)	0.6	34.3

* RWAs are non-additive across geographical regions due to market risk diversification effects within the Group.

Group Chairman's Statement

The Group has improved its productivity, embraced technological change and continues to reinforce its standards of business conduct. It has a strong capital position and is gaining market share in important areas.

Douglas Flint Group Chairman

2016 will be long remembered for its significant and largely unexpected economic and political events. These foreshadowed changes to the established geopolitical and economic relationships that have defined interactions within developed economies and between them and the rest of the world. The uncertainties created by such changes temporarily influenced investment activity and contributed to volatile financial market conditions. Against this background, HSBC's performance in 2016 was broadly satisfactory. Encouragingly, operating performance in the second half of the year was much stronger than expected and compared with the prior year, as businesses and financial markets responded more optimistically than predicted to these events.

'Greater focus on the trade and investment corridors where HSBC has strong market positioning generated solid market share gains and broader product penetration'

The Group's reported profit before tax amounted to $7.1bn, some 62% lower than the prior year. This decline principally reflected the impact of significant items, most of which had no impact on capital, even though they were material in accounting terms. On the adjusted basis used to measure management and business performance, profit before tax was $19.3bn, broadly in line with the $19.5bn achieved in the prior year. This outcome was largely driven by improved cost performance as prior year initiatives gained traction and substantially offset lower revenues, while loan impairment charges were marginally higher. Earnings per share of $0.07 compared with $0.65 in 2015.

The Group's core capital position improved materially. A change to the regulatory treatment of our associate in mainland China, continued run-off of legacy assets, planned reduction in certain segments of our trading books and inadequately remunerated assets, together with capital released from business disposals, notably our operations in Brazil, drove this improvement. This created the capacity to return $2.5bn of capital by way of a share buy-back, which was completed in December. We met our objective of maintaining the annual dividend in respect of the year at $0.51, as indicated at the interim stage. This was delivered through the declaration today of a fourth interim dividend of $0.21. Reflecting on the strength of the Group's capital position, the Board also approved a further share buy-back of up to $1bn, which is expected to commence shortly.

Strategic actions are now bearing fruit

In reviewing performance in 2016, the Board noted with approval the traction now evidenced from management actions to reshape the Group and address the challenges brought about by the continuing low interest rate environment.

Greater focus on the trade and investment corridors where HSBC has strong market positioning generated solid market share gains and broader product penetration, particularly in servicing outbound China investment flows. This is recognised in the leading industry awards highlighted in Stuart Gulliver's review.

Significant investment in technology and process redesign is now not only delivering greater cost efficiency but also is poised to markedly enhance our ability to detect and prevent financial crime. In addition, 2017 will see the progressive launch of applications that will materially improve our customers' digital experience, enhance their online security and bring greater personalisation of product offerings.

While there is still a long way to go, it was encouraging to see the significant improvement in performance across all business units in Mexico following the substantial repositioning of the Group's operations there. This contributed to the Group's success in replacing substantially all of the revenues given up through continuing run-off of legacy portfolios, risk mitigation in areas exposed to higher threat of financial crime and reduction in trading books.

Furthermore, HSBC is safer today from the threat of financial crime because of the investments we have been making in our Global Standards programme. The Board remains fully committed to our work in this area in 2017 and beyond.

Regulatory matters

It was extremely disappointing that the regulatory community was unable to achieve its targeted completion of the Basel III framework in January 2017 on the consensual basis expected. It is now almost 10 years since the commencement of the global financial crisis and it is time to draw a line under further regulatory changes, particularly since there is no doubt that our industry is more strongly capitalised, better governed and more risk aware than it was a decade ago. Finalisation of the structure and calibration of the capital framework is crucial to give banks certainty over prospective capital allocations in support of lending and market activities. This is particularly important at this time when public policy is focusing on encouraging greater support for longer-dated assets, including infrastructure, and seeking to build out the capital markets of Europe and emerging markets. It is hugely important that regulators and policy makers now move as quickly as possible to finalise the capital framework in line with their stated commitment to deliver that framework without a significant, broad-based increase in capital requirements. Equally important is the avoidance of fragmentation in the global regulatory architecture as the new US administration reconsiders its participation in international regulatory forums. The best outcome would be early global agreement on unresolved issues, followed by an extended period of regulatory stability to allow familiarity and experience to be gained from what has been put in place.

We made further progress in 2016 on completing the resolution planning required of us as a global systemically important bank ('G-SIB'). This involved removing or mitigating residual constraints on the clarity of the Group's core college of regulators' approach to winding down the Group, should this ever be necessary. While clearly we do not envisage such circumstances as other than extremely remote, completion of a comprehensive resolution framework is a necessary pillar supporting HSBC's ability to continue to operate as one of the world's G-SIBs. Indeed, our strategy is built around maintaining the scale and the reach of our international network, which in 2016 again demonstrated its resilience and competitive advantages.

Tangible benefits accrue to our shareholders from the detailed work done with our regulators to demonstrate the strength of our capital position and the effectiveness of our resolution planning. Beyond supporting the maintenance of our dividend, in 2016 management's efforts created the capacity to return capital to shareholders by way of a share buy-back and demonstrated justification for a reduction in the additional capital buffer applied to HSBC as a G-SIB.

UK referendum on EU membership

Not a great deal has changed since we reported at the interim stage, given that the UK has still to trigger its formal exit notice and so no negotiations have taken place. We welcomed, however, the additional clarity given to the Government's position in the recent speech by the Prime Minister. The scale of the challenge of negotiating across the entire economic landscape, as well as addressing the legislative and other public policy adjustments that will be required, has become clearer. We believe there is now, as a consequence, a widely shared recognition that an implementation phase between the current position and the one that is ultimately negotiated will be necessary; we strongly endorse this view.

Since the referendum we have focused on advising clients on the implications of leaving the EU for their businesses. We have also been responding to UK Government outreach seeking guidance on which elements of the current EU-based legal and regulatory arrangements it should focus on to preserve the essential role that financial markets based in the UK play in supporting European trade and investment activity.

For our own part, we have broadly all the licences and infrastructure needed to continue to support our clients once the UK leaves the EU. This largely derives from our position in France where we are the sixth largest bank with a full range of capabilities. Current contingency planning suggests we may need to relocate some 1,000 roles from London to Paris progressively over the next two years, depending on how negotiations develop.

Board changes

We welcomed Jackson Tai to the Board on 12 September last year. Jack brings a rare combination of hands-on banking expertise, top level governance experience and a deep knowledge of Asia and China. These attributes were accumulated in a 25-year career at J.P. Morgan & Co., both in the US and in Asia, and subsequently in senior roles at DBS, the leading Singapore-based regional banking group, where Jack latterly led its regional expansion as Vice Chairman and CEO. Jack was appointed a member of the Financial System Vulnerabilities Committee and the Group Risk Committee.

At the forthcoming AGM we shall bid farewell to our two longest-serving independent directors, namely, our Senior Independent Director, Rachel Lomax, and Sam Laidlaw. Rachel during her tenure has served on the Audit, Risk and Nomination Committees, and took responsibility as the first Chair of the Conduct & Values Committee to establish its terms of reference and its agenda. Sam served on, and latterly chaired, both the Remuneration and Nomination Committees. Together, Rachel and Sam have also been leading the process to manage my own succession. Their combined knowledge of regulatory and public policy, business leadership, corporate governance and consumer issues has been invaluable to the Board. On behalf of all shareholders, I want to thank them for their dedication and commitment.

Chairman succession

In the Circular inviting shareholders to the 2016 AGM, I indicated that the process to find my own successor had been initiated with the intention of having this concluded during 2017. This process remains on track and an announcement will be made in due course.

Outlook

We have recently upgraded our forecasts for global economic growth reflecting the likelihood of a shift in US fiscal policy and a broader based cyclical recovery. As in recent years, incremental growth is expected to be driven by emerging economies in which HSBC is well represented. Risks to this central scenario, however, remain high. In particular, we highlight the threat of populism impacting policy choices in upcoming European elections, possible protectionist measures from the new US administration impacting global trade, uncertainties facing the UK and the EU as they enter Brexit negotiations, and the impact of a stronger dollar on emerging economies with high debt levels.

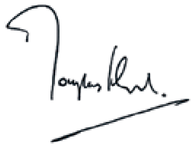
Countering these factors are signs of a cyclical upturn. Global purchasing manager indices are at their strongest for some time, the US economy looks robust and growth in China has held up well, defying the concerns reflected in the market retrenchment seen in the first quarter of 2016. Additionally, commodity prices have risen, reflecting optimism regarding growth in infrastructure investment as well as agreement reached to cut oil supply. These factors also imply reflation across the major economies and rising interest rates, which would benefit HSBC's conservative balance sheet structure.

> 'We enter 2017 with the restructuring of the Group essentially completed, and with a strong capital position and a conservative balance sheet'

However, it is fair to reflect that the upgrades to economic growth we are now forecasting are largely the partial reversal of downgrades made last year when uncertainty was elevated as a result of the unexpected political events. Forecast global growth remains slightly lower than its long-term trend with risks largely to the downside.

We enter 2017 with the restructuring of the Group essentially completed, and with a strong capital position and a conservative balance sheet. We are gaining market share in areas of importance to HSBC as others scale back and our offerings become more competitive. Much of the heavy investment in reshaping the Group to improve productivity, embrace technological change and reinforce global standards of business conduct has been made.

As ever, we owe a huge amount to our 235,000 colleagues who have delivered this change at the same time as working tirelessly to meet customers' expectations of them. On behalf of the Board, I want to thank them all for their dedication and commitment.



Douglas Flint
Group Chairman
21 February 2017

Group Chief Executive's Review

The strength of our network gives us an unrivalled ability to help clients navigate complexity and uncover new opportunities.

Stuart Gulliver Group Chief Executive

We made good progress in 2016. The implementation of our strategic actions is well advanced and our global universal business model performed well in challenging conditions. Our reported profit before tax reflected a number of large significant items, including a write-off of all the remaining goodwill in Global Private Banking in Europe, an accounting loss on the sale of our Brazil business, and investments to achieve our cost-saving target. Our adjusted profits were broadly unchanged year on year following solid performances by our global businesses. These enabled us to capture market share in strategic product areas and build a platform for future growth. We delivered positive adjusted jaws in 2016.

Performance

Global Banking and Markets recovered from a sector-wide slow start to generate higher adjusted revenue than for 2015. Our Markets businesses performed well in challenging conditions, particularly in Fixed Income products. Our transaction banking businesses also grew revenue, especially Global Liquidity and Cash Management. We made market share gains in Fixed Income in Europe, and achieved our best ever league table rankings in global debt capital markets and cross-border mergers and acquisitions. HSBC was recognised as the 'World's Best Investment Bank' and 'World's Best Bank for Corporates' at the *Euromoney* Awards for Excellence 2016.

Commercial Banking performed well, particularly in the UK and Hong Kong, growing adjusted revenue in spite of a slow-down in global trade. Gains in Global Liquidity and Cash Management, and Credit and Lending, exceeded the reduction in trade finance revenue. Global Trade and Receivables Finance continued to capture market share in major markets including Hong Kong and Singapore, maintaining our position as the world's number one trade finance bank.

Retail Banking and Wealth Management performance was mixed. Overall adjusted revenue was down, due largely to the impact of reduced client activity in Hong Kong on our Wealth Management businesses. At the same time, strong mortgage balance growth in the UK, Hong Kong and mainland China, and higher current account and savings balances in the UK and Hong Kong, helped increase revenue in Retail Banking. These increased balances should support revenue growth in 2017 and beyond.

We have considered it appropriate to write off the remaining goodwill in the European private banking business. This goodwill relates principally to the original purchase of Safra Republic Holdings in 1999. The restructuring of Global Private Banking is now largely complete, and although Global Private Banking is now much smaller than it was three years ago, it is deliberately positioned for sustainable growth with a focus on serving the personal wealth management needs of the leadership and owners of the Group's corporate clients.

Our cost-reduction programmes continue to bring down our adjusted operating expenses. The traction that these programmes have gained in the last 18 months has enabled us to increase the amount of costs that we are able to remove from the business. We now expect to deliver annualised cost savings of around $6bn by the end of 2017, and will invest an equivalent total of around $6bn over the same time-frame in order to achieve this.

These savings should more than compensate for additional investment in regulatory programmes and compliance.

We continue to make strong progress in implementing our strategic actions to improve returns and gain maximum value from our international network. We are on course to complete the majority of these actions by the end of 2017 (see pages 12 to 13), in line with our targets. Our targeted reduction of risk-weighted assets is 97% complete, and the success of our cost saving programmes means that we now expect to exceed our cost reduction target.

The turnaround of our Mexico business continues to accelerate. Improved lending and deposit balances, interest rate rises and better collaboration between businesses helped generate significantly higher profits compared with 2015. We also made significant market share gains, particularly in consumer lending.

We have continued to enhance our business in Asia-Pacific, launching our first exclusively HSBC-branded credit card in mainland China, growing assets under management and insurance new business premiums, and increasing loans in the Pearl River Delta. We also extended our leadership of the offshore renminbi bond market and achieved our best ranking for China outbound mergers and acquisitions since 2003.

We are better protected from financial crime because of the investment we have made in our Global Standards programme. Our Monitor has raised certain concerns, but we have continued to progress and our commitment remains unwavering. By the end of this year, we are on track to have our anti-money laundering and sanctions policy framework in place and to have introduced major compliance IT systems across the Group. Beyond 2017, we will continue to work to fine tune those systems and to ensure that our improvements are fully integrated into our day-to-day risk management practices.

Our strong common equity tier 1 ratio of 13.6% reinforces our ability to support the dividend, invest in the business and manage the continuing uncertain regulatory environment.

Delivering value for shareholders

In December, we completed the $2.5bn equity buy-back that we commenced at the half-year. We are also now in a position to retire more of the capital that previously supported the Brazil business. Having received the appropriate regulatory clearances, we will therefore execute a further share buy-back of up to $1bn in the first half of 2017. This will bring the total value of shares repurchased since last August to $3.5bn.

We will continue to contemplate further share buy-backs as circumstances permit, and we remain confident of sustaining the annual dividend at the current level for the foreseeable future through the long-term earnings capacity of the business.

A business fit for the future

While our strategic actions are improving our network, we are also anticipating and adapting to the social, economic and technological trends that are changing our operating environment and our customers' needs and expectations.

The adoption of rapidly evolving digital technologies by our customers is arguably the most transformative force for the financial services industry. Through our global network, we are able to identify and respond to digital trends across 70 countries and territories, applying the technologies that provide the greatest benefit to our customers. We are investing $2.1bn in digital transformation in Retail Banking and Wealth Management, Commercial Banking, and Global Banking and Markets between 2015 and the end of 2020, and we have already launched innovative ways to make banking faster, easier and safer. HSBC is now the biggest financial services user of biometrics globally, and we continue to roll out voice recognition and fingerprint technology across our network. In 2016, we enhanced our internet and mobile banking platforms in several of our key markets, including the UK and Hong Kong, and launched innovation labs around the world dedicated to the application of artificial intelligence, data management and improvements in cybersecurity. These labs, together with our fintech partnerships, will help us use technology to deliver better banking for our customers.

If digital technology is mankind's greatest opportunity, preventing climate change is its greatest challenge. The Paris Agreement of December 2015 reflected a new consensus on the need to strengthen the global response to climate change. Major injections of capital are now required to finance new technologies, infrastructure and the transition of traditional industries from high to low carbon, and to cover the costs of climate adaptation. As the principal intermediaries between entrepreneurs, businesses and investors, banks have a responsibility to help direct this flow of capital. We are already working with our clients and with investors to help them allocate capital and direct finance towards lower-carbon, carbon-resilient activities, and in 2016 we established a Sustainable Financing Unit to coordinate this work across business lines. Headquartered in London, but with resources in New York and Hong Kong, this new unit will support colleagues tasked with creating and delivering innovative climate products, and help them uncover new sources of sustainable finance.

> 'The changes we have made since 2011 have equipped HSBC to improve returns and gain maximum value from our international network'

We are also seeking to influence client practices and to build the data, the tools and the transparency necessary to embed understanding of climate risk into the way that markets function. In 2016, HSBC Global Research expanded its coverage of environment, social and corporate governance factors to give our clients the information they need to inform their investment decisions. This builds on the work of the world-leading HSBC Climate Change Centre for Excellence, which in 2017 celebrates 10 years of delivering market-leading information on climate policy to clients across the globe. Work is also underway to expand the Group's disclosure of non-financial data to meet the needs of shareholders and other stakeholders.

We are investing to adapt to the changing face of trade. As the world's largest trade finance bank with more than 150 years' experience at both ends of the world's busiest trade routes, we are perfectly placed to help modernise and digitise long-standing trade finance methods, many of which would still be recognisable to HSBC's founders. We are already working with a broad coalition of partners around the world to make the promise of blockchain technology a reality with regards to trade finance. HSBC has already helped develop a blockchain prototype for a letter of credit that confirms the possibility of sharing information between all parties on a private distributed ledger. In early 2017, we signed a memorandum of understanding with six other banks to make domestic and cross-border commerce easier for European SMEs using blockchain technology. We are also seeking to create ways of financing the growing services trade, which we estimate will account for a quarter of global trade by 2030. At a time when international politics threaten to increase rather than decrease the cost of trade, we will continue to invest both time and resources to find ways of making trade finance cheaper, faster, simpler and more secure for our customers.

Looking forward

We anticipate new challenges in 2017 from geopolitical developments, heightened trade barriers and regulatory uncertainty. However, the changes we have made since 2011 have equipped HSBC to manage the complexity of today's global business environment. HSBC is a strong and resilient business with a global universal business model geared to find growth opportunities in a low-growth world. If globalisation continues to retreat, as seems likely, we are in a strong position to capitalise on the regional opportunities that this will present, particularly in Asia and Europe. Most importantly, the strength of our network gives us an unrivalled ability to help our clients navigate that same complexity and overcome their own challenges, whether exploring new markets or making the transition to a low-carbon economy.

Stuart Gulliver
Group Chief Executive
21 February 2017

Our strategy

We have developed a long-term strategy that reflects our purpose and enables us to capture value from our international network.

Two-part long-term strategy

Develop our international network

To facilitate international trade and capital flows and serve our clients, with potential to help them grow from small enterprises into large multinationals.

Invest in wealth and retail businesses with local scale

To make the most of global social mobility, wealth creation and long-term demographic changes in our priority markets.

Value of the network and our strategy

Access to global growth opportunities

Our unparalleled network covers countries accounting for more than 90% of global GDP, trade and capital flows. We have a leading presence in large and fast-growing economies.

Our priority markets cover both sides of 11 of the world's 15 largest trade corridors for goods and services forecast for 2030, and represent at least one side of the other four corridors. Six of the 15 corridors are within Asia and five connect countries between two geographical regions.

Lower risk profile and volatility from our diversified, universal banking model

Our 10-year profit before tax volatility of 0.9x compares favourably with our peers.

Transaction banking product revenue of $14.7bn on an adjusted basis leads the industry. More than 45% of our client revenue comes from businesses and individuals with an international presence.

Business synergies of $10.5bn, equivalent to 22% of reported revenue reflect products and services provided across our global businesses.

Strong capital and funding base

CET1 ratio of 13.6%, supported by increased shareholders' equity to meet new regulatory requirements since the end of 2010.

Four interconnected, global businesses share balance sheets and liquidity in addition to strong commercial links.

Stable shareholder returns

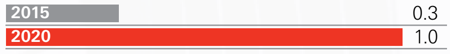
Industry leading dividend – approximately $55bn declared from 2011 to 2016, as well as circa $2.5bn of share repurchases.

Long-term trends

Our strategy positions us to capitalise on several long-term trends.

Increasing connectivity and global flows of trade, finance and data are key drivers of GDP growth.

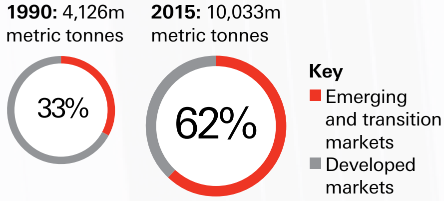
Business to consumer cross-border e-commerce transactions
($tn)



Source: McKinsey Global Institute, *Digital globalization: The new era of global flows* (2016)

Economic weight is shifting to Asian and Middle Eastern economies, which are expected to grow GDP threefold by 2050.

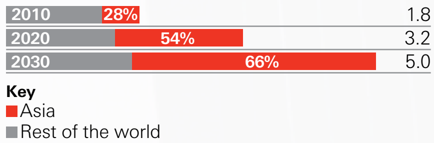
Shipping volumes, measured by weight of goods unloaded



Source: United Nations Conference on Trade and Development

The middle class is expected to grow from one-third to two-thirds of the world's population by 2030, while the number of people over age 60 is expected to more than double by 2050.

Size of middle class population
(bn)



Source: OECD Development Centre, *Emerging Middle Class in Developing Countries* (2010)

Client examples

ATN International ('ATNI'): US, telecommunications and renewable energy

International portfolio of businesses in US and elsewhere. ATNI sought out HSBC's international capabilities while pursuing renewable energy investments in India. In 2016, we helped ATNI with custodian services and provided finance structuring advice for its Singaporean and Indian subsidiaries. We provide ATNI with trade, cash management, foreign exchange and other services.

Mubea: Germany, automotive

Automotive parts manufacturer operating across 20 countries in Europe, Asia and the Americas. HSBC expanded its relationship with Mubea to also serve its subsidiaries in the US and Mexico, and provide centralised international cash and liquidity management.

Tangle Teezer: UK, consumer goods

UK-based hairbrush manufacturer with its first product launch in 2008, and a range of products now sold in more than 70 markets. Since 2009, HSBC has helped Tangle Teezer expand internationally through our knowledge and capabilities around the world. In 2016, we assisted it in developing its presence in the US, China and Hong Kong.

Grupo Aeroportuario ('GACM'): Mexico, infrastructure

Responsible for the construction, administration and operation of Mexico City's new international airport. In 2016, we advised and coordinated financing for GACM including a $1bn 30-year green bond issuance, the largest green bond in Latin America, and the first emerging market green bond to receive a Green Bond Assessment grade from Moody's.

Strategic actions

We are well on our way towards achieving the actions outlined in our June 2015 Investor Update.

Capturing value from our international network

In June 2015, we outlined a series of strategic actions to make the most of our competitive advantages and respond to a changing environment.

These actions are focused on improving efficiency in how we use our resources, and on investing for growth in line with our strategy. Each action has targets defined to the end of 2017. The table opposite contains a summary of our progress in 2016 with additional details provided below.

Resizing and simplifying our business

We have made significant progress in resizing and simplifying our business. In 2016, management actions reduced RWAs in GB&M and legacy credit by $46bn and we completed asset sales totalling $10.1bn from our US consumer and mortgage lending ('CML') run-off portfolio.

As part of our initiative to optimise our network, we completed the sale of HSBC Bank Brazil on 1 July 2016. We will continue to serve the international and cross-border needs of our large corporate clients in Brazil through HSBC Brasil S.A. – Banco de Investimento.

In the NAFTA region, we grew adjusted revenue in Mexico by 18% compared with 2015, supported by market share gains in RBWM across key lending products and a doubling of personal loans issued. In the US, we grew adjusted revenue in GB&M and RBWM compared with 2015 and continued to support our clients internationally. Revenues from international subsidiaries of our US clients increased by 11% compared with 2015.

We have made good progress in our cost-saving programme and are on track to exceed our exit rate target set for the end of 2017. We expect to achieve total cost savings of $6.0bn through one-off investments ('costs to achieve') of $6.0bn. The additional savings will fund increased costs related to regulatory programmes and compliance. In 2016, operating expenses fell by 4% on an adjusted basis compared with 2015, facilitated by increased efficiency in our processes. For example, we launched a new customer-facing digital portal to standardise and accelerate the onboarding process in 26 markets covering more than 70% of CMB corporate clients, and we decreased the number of manual payments by 80%.

Redeploying capital to grow our business

At the heart of our business is our international network. We are focusing efforts to grow our businesses by looking at customers' needs across products, geographies and supply chains. In 2016, revenue from transaction banking products was up 2% despite difficult macroeconomic conditions. We grew revenues in our Global Liquidity and Cash Management (GLCM) business. In 2016, we were named 'Best Bank for Corporates' by *Euromoney* and 'Best Supply-Chain Finance Bank Global' by the *Trade Finance* Awards.

We continue to invest for growth in Asia. In December, we launched our own HSBC-branded credit cards in mainland China with a full range of digital features. We increased the number of new RBWM clients in China's Pearl River Delta by 51% compared with 2015, and grew our mortgage loan books by more than 51%. We grew revenues from international subsidiaries of our ASEAN-region commercial banking clients, and in Singapore our innovation lab is developing cloud-based treasury services for businesses and exploring blockchain technology to support documentary trade transactions.

We remain recognised as the leading bank for international renminbi ('RMB') products and services. We were the first bank to facilitate overseas institutional investment into the China interbank bond market since access was expanded in early 2016. We were also the first to be appointed custodian bank in the two newly active RMB qualified foreign institutional investor ('RQFII') markets of the US and Thailand this year.

Finally, we continue to strengthen our efforts to protect customers and the wider financial system from financial crime. In 2016, this included further upgrades to our systems, as well as additional training for our employees. Further detail can be found under the Financial Crime Risk section of www.hsbc.com/financial-crime-risk.

Selected awards and recognition 2016

***Euromoney* Awards for Excellence 2016**

Best Bank for Corporates

Best Investment Bank

***Euromoney* Cash Management Survey 2016**

Best Global Cash Manager (Non-Financial Institutions)

#1 Global For All Transactions (Financial Institutions)

***Trade Finance* Awards 2016**

Best Supply-Chain Finance Bank Global

***Asiamoney* Offshore RMB Poll 2016**

Best Overall Offshore RMB Products / Services

Progress against strategic actions

Actions to resize and simplify the Group

Strategic actions	Targeted outcome by the end of 2017	Progress	Key performance indicators	Status
Reduce Group risk-weighted assets ('RWAs') by circa $290bn	– Group RWA reduction $290bn – Return GB&M to Group target profitability; <1/3 of Group RWAs	– Further reduction of $143.2bn in 2016, notably in GB&M – GB&M RWAs of $300.4bn, 37% of the Group total	– RWA reduction from management actions: circa $267bn (circa 97% of 2015–17 target on a constant currency basis)	✓
Optimise global network	– Reduced footprint	– Completed our sale of Brazil operations on 1 July 2016; maintained a Brazil presence to serve large corporate clients' international needs	– Present in 70 countries and territories at end of 2016 (down from 73 at end of 2014)	✓
Rebuild NAFTA region profitability	– US profit before tax circa $2bn – Mexico profit before tax circa $0.6bn	– Successfully achieved a non-objection to our US capital plan, which includes a dividend payment to HSBC Holdings plc in 2017, as part of the Comprehensive Capital Analysis and Review ('CCAR') – Mexico market share gains across key RBWM lending products	– US (excluding CML run-off portfolio) adjusted profit before tax: $0.4bn (down 22% on 2015) – Mexico adjusted profit before tax: $0.3bn (up 354% on 2015)	– ✓[1]
Set up UK ring-fenced bank	– Completed by 2018	– Appointed Chair and CEO of HSBC UK; other senior appointments in progress – Migration of key roles underway with circa 35% of Birmingham positions filled	– Implementation in progress	✓
Deliver $4.5-5.0bn of cost savings	– 2017 exit rate to equal 2014 operating expenses	– $2.2bn cost savings realised in 2016 – Positive jaws in 2016 compared with 2015 – FTE reduction of circa 900 in 2016	– Adjusted costs (excluding Brazil) down 4% on 2015	✓

Actions to redeploy capital and invest

Strategic actions	Targeted outcome by the end of 2017	Progress	Key performance indicators	Status
Deliver growth above GDP from international network	– Revenue growth of international network above GDP	– GLCM revenue up 6% on 2015 driven by growth in deposits and the effect of US rate rises – Global Trade and Receivables Finance ('GTRF') revenue down 7% on 2015, reflecting a decline in market conditions	– Transaction banking revenue: $14.7bn (up 2% on 2015) – Revenue synergies: $10.5bn (down 5% on 2015)	–
Investments in Asia – prioritise and accelerate	– Market share gains – Circa 10% growth per annum in assets under management in Asia	– Awarded Asia's 'Best Investment Bank' and Asia's 'Best Bank for Financing' by *Euromoney* Awards for Excellence 2016 – Launched digital banking platform (HSBCnet) for SMEs in Guangdong allowing faster payment services with Hong Kong – Growing business around China's Belt and Road initiative, including energy sector deals linking China to Malaysia and Egypt	– Guangdong loans: $4.7bn (up 16% on 2015) – ASEAN adjusted revenue: $3.1bn (down 2% on 2015) – Asset Management assets under management distributed in Asia: $143bn (up 11% on 2015) – Insurance manufacturing annualised new business premiums in Asia: $2.3bn (up 13% on 2015)	✓
Grow business from renminbi ('RMB') internationalisation	– $2.0–2.5bn revenue	– 52% RQFII custodian market share (in Securities Services); ranked first by market share in all active RQFII markets – Joint lead manager for China's Ministry of Finance RMB3bn bond in the UK, the first sovereign RMB bond issued outside China	– RMB internationalisation revenue, from offshore business partly or wholly denominated in RMB as well as selected products in mainland China: $1.25bn (down 25% on 2015)	–
Global Standards – safeguarding against financial crime[3]	– Implementation completed	– Continued progress towards putting in place an effective and sustainable AML and sanctions compliance programme, including through the creation of a new Financial Crime Risk function and improvements in technology and systems to manage financial crime risk	– By end 2017: AML and sanctions policy framework in place; major compliance IT systems introduced across the Group, including for customer due diligence, transaction monitoring and sanctions screening – Post-2017: Policy framework and associated operational processes fully integrated in day-to-day financial crime risk management practices in an effective and sustainable way; IT systems continue to be fine-tuned	✓[2]

1 On track to achieve equivalent profit before tax target on a local currency basis; US dollar target set using the 2014 average exchange rate.

2 As set out under 'Key performance indicators'.

3 Further detail on the Monitor and the US deferred prosecution agreement and related agreements and consent orders can be found on pages 82 and 66, respectively, of the *Annual Report and Accounts 2016*.

Financial overview

Reported results

This table shows our reported results for the last three years, ended 31 December 2016, 2015 and 2014.

Reported results	2016 $m	2015 $m	2014 $m
Net interest income	**29,813**	32,531	34,705
Net fee income	**12,777**	14,705	15,957
Net trading income	**9,452**	8,723	6,760
Other income	**(4,076)**	3,841	3,826
Net operating income before loan impairment charges and other credit risk provisions ('revenue')	**47,966**	59,800	61,248
Loan impairment charges and other credit risk provisions ('LICs')	**(3,400)**	(3,721)	(3,851)
Net operating income	**44,566**	56,079	57,397
Total operating expenses	**(39,808)**	(39,768)	(41,249)
Operating profit	**4,758**	16,311	16,148
Share of profit in associates and joint ventures	**2,354**	2,556	2,532
Profit before tax	**7,112**	18,867	18,680

Reported profit before tax

Reported profit before tax of $7.1bn was $11.8bn or 62% lower than in 2015. This was primarily due to net adverse movements relating to significant items and the unfavourable effects of foreign currency translation, which are described in more detail on page 30 of the *Annual Report and Accounts 2016*. Excluding significant items and currency translation, profit before tax fell by $0.2bn.

Reported revenue

Reported revenue of $48.0bn was $11.8bn or 20% lower than in 2015, in part due to a net unfavourable movement in significant items of $7.6bn, which included:

- adverse fair value movements of $1.8bn arising from changes in credit spreads on our own debt designated at fair value, compared with favourable movements of $1.0bn in 2015;
- a $3.6bn reduction in revenue resulting from our sale of operations in Brazil to Banco Bradesco S.A., which includes a $1.7bn accounting loss recognised on the sale; and
- the non-recurrence of a $1.4bn gain on the sale of part of our shareholding in Industrial Bank Co. Limited ('Industrial Bank') in 2015; partly offset by
- a $0.6bn gain on the disposal of our membership interest in Visa Europe in the second quarter of 2016 and a $0.1bn gain on disposal of our membership interest in Visa US in the fourth quarter of 2016.

In addition, foreign currency translation differences between the periods had an adverse effect of $3.0bn.

These factors contributed to a fall in reported revenue in all our global businesses and Corporate Centre. Excluding significant items and the adverse effects of foreign currency translation differences between the periods, revenue fell by $1.3bn or 2%.

Reported LICs

Reported LICs of $3.4bn were $0.3bn lower than in 2015 as reductions in RBWM and CMB more than offset an increase in GB&M. The reduction included favourable effects of foreign currency translation differences between the periods of $0.2bn, and the impact of LICs incurred in the disposed Brazil operations of $0.7bn compared with $0.9bn in 2015.

Reported operating expenses

Reported operating expenses of $39.8bn were $40m or 0.1% higher than in 2015. This includes favourable effects of currency translation differences of $2.1bn between the periods, and an increase in significant items of $3.3bn, including:

- a $3.2bn write-off of goodwill in our GPB business in Europe; and
- costs to achieve of $3.1bn compared with $0.9bn in 2015; partly offset by
- a reduction of $1.0bn in settlements and provisions in connection with legal matters.

In addition, the reported results include the operating expenses incurred in our Brazil business of $1.1bn compared with $2.5bn in 2015.

Excluding significant items and the adverse effects of foreign currency translation differences between the periods, operating expenses fell by $1.2bn. Reductions in all our global businesses reflected the effects of our cost-saving initiatives.

Reported income from associates

Reported income from associates and joint ventures of $2.4bn decreased by $0.2bn.

On 21 February 2017, the Board announced a fourth interim dividend of $0.21 per ordinary share.

Adjusted performance

Our reported results are prepared in accordance with IFRSs as detailed in the Financial Statements on page 194 of the *Annual Report and Accounts 2016*. We also present adjusted performance measures to align internal and external reporting, identify and quantify items management believes to be significant, and provide insight into how management assesses period-on-period performance. Adjusted performance measures are highlighted with the following symbol: ◆

To derive adjusted performance, we adjust for:

– the year-on-year effects of foreign currency translation differences; and
– the effect of significant items that distort year-on-year comparisons and are excluded in order to understand better the underlying trends in the business.

For reconciliations of our reported results to an adjusted basis, including lists of significant items, see page 47 of the *Annual Report and Accounts 2016*.

Adjusted results ◆

This table shows our adjusted results for 2016 and 2015. These are discussed in more detail on the following pages.

Adjusted results ◆	2016 $m	2015 $m
Net operating income before loan impairment charges and other credit risk provisions (revenue)	**50,153**	51,419
Loan impairment charges and other credit risk provisions ('LICs')	**(2,652)**	(2,604)
Total operating expenses	**(30,556)**	(31,730)
Operating profit	**16,945**	17,085
Share of profit in associates and joint ventures	**2,355**	2,443
Profit before tax	**19,300**	19,528

Adjusted profit before tax ◆

On an adjusted basis, profit before tax of $19.3bn was $0.2bn or 1.2% lower than in 2015. This primarily reflected lower revenue, higher LICs and a reduction in our share of profits from associates. This was partly offset by a decrease in operating expenses.

Movement in adjusted profit before tax compared with 2015 ◆

	2016 ($m)	Adverse	Favourable	(%)
Revenue	**50,153**	**(1,266)**		**(2)**
LICs	**(2,652)**	**(48)**		**(2)**
Operating expenses	**(30,556)**		**1,174**	**4**
Share of profits in associates and joint ventures	**2,355**	**(88)**		**(4)**
Profit before tax	**19,300**	**(228)**		**(1)**

Adjusted performance continued

Movement in adjusted revenue compared with 2015

	2016 $m	2015 $m	Variance $m	%
RBWM	**18,925**	19,242	(317)	(2)
CMB	**12,887**	12,753	134	1
GB&M	**14,919**	14,566	353	2
GPB	**1,757**	1,965	(208)	(11)
Corporate Centre	**1,665**	2,893	(1,228)	(42)
Total	**50,153**	51,419	(1,266)	(2)

Adjusted revenue

Adjusted revenue of $50.2bn was $1.3bn or 2% lower. The reduction reflected the following:

- In RBWM, lower revenue (down $0.3bn) was mainly a result of a fall in income in our Wealth Management business. The reduction resulted from lower investment distribution income compared with a strong performance in 2015, notably in the first half of the year, and adverse market impacts in Insurance Manufacturing. By contrast, revenue grew in savings and deposits, as we grew balances in Hong Kong, the UK and Mexico, and from wider spreads in Hong Kong and Latin America.
- In GPB, lower revenue (down $0.2bn) reflected reduced brokerage and trading activity due to the continued repositioning of the business, together with adverse market sentiment and unfavourable market conditions.
- In Corporate Centre, revenue fell (down $1.2bn), partly due to the US CML portfolio (down $0.5bn) as a result of continued run-off and portfolio sales. Revenue also fell in Central Treasury as a result of higher adverse fair value movements relating to the economic hedging of our long-term debt ($0.2bn) and higher interest expense on our debt ($0.2bn).

These were partly offset:

- In GB&M, revenue increased (up $0.4bn) despite adverse movements in credit and funding valuation adjustments of $0.3bn. In Rates and Credit, higher revenue reflected growth in market share in Europe. We also increased revenue in Global Liquidity and Cash Management ('GLCM') from balance growth and wider spreads. By contrast lower trading volumes in Europe and Asia resulted in a reduction in Equities revenue.
- In CMB, revenue rose (up $0.1bn), notably in GLCM reflecting balance growth and wider spreads in Hong Kong. Revenue also increased in Credit and Lending as a result of loan growth in the UK.

For further details on the performance of our global businesses, see page 18.

Adjusted LICs

Adjusted LICs of $2.7bn were $48m higher than in 2015, reflecting increases in GB&M resulting from a small number of individually assessed LICs within the oil and gas, and metals and mining sectors, notably in the first half of 2016 in the US. LICs also increased in RBWM, particularly in Mexico. These increases were largely offset by a reduction in LICs in CMB.

Adjusted operating expenses

Adjusted operating expenses of $30.6bn were $1.2bn or 4% lower than in 2015. This primarily reflected cost savings of $2.2bn realised in 2016, with run-rate savings of around $3.7bn since the commencement of our cost-saving programme. The fall in operating expenses also included a reduction of $0.5bn in the UK bank levy. These reductions were partly offset by the impact of inflation and our continued investment in regulatory programmes and compliance.

Run-the-bank costs of $26.9bn were $0.3bn lower, and change-the-bank costs of $2.7bn were $0.4bn lower, both compared with 2015. Within these, our total expenditure on regulatory programmes and compliance, comprising both run-the-bank and change-the-bank elements, was $3.0bn, up $0.4bn or 14% compared with 2015. This reflected the ongoing implementation of our Global Standards programme to enhance our financial crime risk controls and capabilities, and to meet our external commitments.

In the fourth quarter of 2016, our adjusted operating expenses increased compared with the third quarter reflecting a small number of specific items. This included the write-off of software.

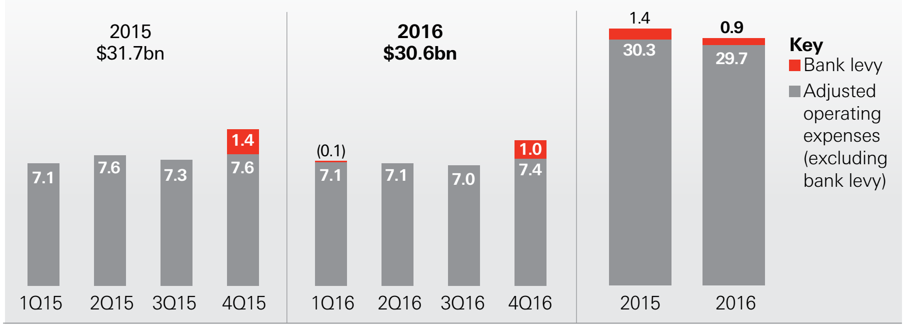
The number of employees expressed in full-time equivalent staff ('FTEs') at 31 December 2016 was 235,175, a decrease of 20,028 from 31 December 2015. This included a 19,145 reduction following our disposal of operations in Brazil. Excluding Brazil, the decrease in FTEs was 883, as a reduction of 17,855 FTEs realised across global businesses and global functions was partly offset by investment in our Global Standards Programme of 5,694 FTEs, costs to achieve FTEs of 8,073 and investment for growth.

For further details on the categorisation of run-the-bank and change-the-bank costs, see page 38 of the *Annual Report and Accounts 2016*.

Adjusted income from associates and joint ventures

Adjusted income from associates and joint ventures of $2.4bn fell by $0.1bn compared with 2015.

Adjusted operating expenses
($bn)



Balance sheet and capital

Balance sheet strength

Total reported assets were $2.4tn, 1% lower than at 31 December 2015 on a reported basis, and 5% higher on a constant currency basis. We have maintained the strength of our balance sheet, as targeted asset growth was partly offset by reductions in our legacy portfolios and the completion of our sale of operations in Brazil to Banco Bradesco S.A. We also issued more than $30bn of senior debt during the year from HSBC Holdings plc ('HSBC Holdings') to build up the Group's total loss absorbing capacity in line with anticipated regulatory requirements.

Distributable reserves

The distributable reserves of HSBC Holdings at 31 December 2016 were $42bn, and at 31 December 2015 were $47bn. The reduction was driven by our share buy-back ($2.5bn) and the effects of dividends paid ($11bn), which more than offset profits of $7bn.

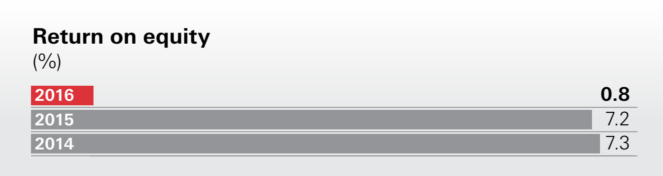
Capital strength

We manage our capital in an effort to ensure we exceed current regulatory requirements and are well placed to meet those expected in the future. We monitor our position using capital ratios. These measure capital relative to a regulatory assessment of risks taken. We quantify how these risks relate to our businesses using RWAs.

Our CET1 ratio at 31 December 2016 was 13.6%, up from 11.9% at 31 December 2015.

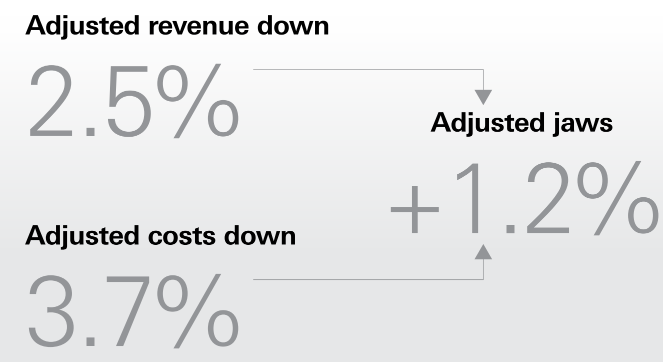
Details of these risks are included on page 127 of the *Annual Report and Accounts 2016.*

Delivery against Group financial targets



Return on equity

Our medium-term target is to achieve a return on equity ('RoE') of more than 10%. In 2016, we achieved an RoE of 0.8% compared with 7.2% in 2015. In 2016, significant items, which included a write-off of goodwill in GPB in Europe, costs to achieve and adverse fair value movements arising from changes in credit spread on our own debt designated at fair value, had a significant effect on our reported RoE. Together with the UK bank levy, significant items reduced the return achieved by 6.9 percentage points.

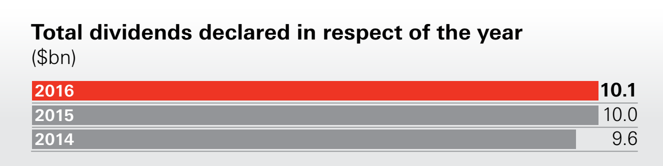


Adjusted jaws

Jaws measures the difference between the rates of change for revenue and costs. Positive jaws occurs when the figure for the annual percentage change in revenue is higher than, or less negative than, the corresponding rate for costs.

We calculate adjusted jaws using adjusted revenue and costs. Our target is to maintain positive adjusted jaws.

In 2016, adjusted revenue fell by 2.5%, whereas our adjusted operating expenses reduced by 3.7%. Adjusted jaws was therefore positive 1.2%.



Dividends

In the current uncertain environment, we plan to sustain the annual dividend in respect of the year at its current level for the foreseeable future. Growing our dividend in the future will depend on the overall profitability of the Group, delivering further release of less efficiently deployed capital and meeting regulatory capital requirements in a timely manner. Actions to address these points were core elements of our Investor Update in June 2015.

Global businesses

We manage our products and services globally through our global businesses.

Commentary is on an adjusted basis, which is the GAAP measure for our global businesses.

The comparative period has been restated to reflect changes to reportable segments, as described on page 44 of the *Annual Report and Accounts 2016*.

Retail Banking and Wealth Management ('RBWM')

RBWM serves close to 36 million customers worldwide through four main business areas: Retail Banking, Wealth Management, Asset Management and Insurance.

RBWM provides services to individuals under the HSBC Premier and Advance propositions aimed at mass affluent and emerging affluent customers who value international connectivity and benefit from our global reach and scale. For customers who have simpler everyday banking needs, RBWM offers a full range of banking products and services reflecting local requirements.

Higher Retail Banking revenue, but challenging market conditions in Wealth Management

- Adjusted profit before tax of $5.3bn was $0.4bn or 6% lower compared with 2015. This was driven by lower revenue in our Wealth Management business, together with higher LICs. By contrast, lower operating expenses reflected our continued focus on cost management.
- Adjusted revenue of $18.9bn was $0.3bn or 2% lower, as growth in Retail Banking revenue was more than offset by a fall in Wealth Management. The reduction in Wealth Management (down 0.5bn) was driven by decreased investment distribution revenue as a result of lower mutual fund and retail securities turnover due to weaker market sentiment. This compared with a strong performance in the first half of 2015. In addition, insurance manufacturing revenue fell, reflecting adverse market impacts ($345m), although this was partly offset by the value of new business. However, in Retail Banking revenue rose $0.2bn or 1%, as revenue increased in current accounts and savings (up $0.4bn) from growth in balances, notably in Hong Kong and the UK. We also benefited from wider deposit spreads in Hong Kong and Mexico. By contrast, revenue in personal lending fell (down $0.2bn), despite growth in balances of $9bn or 3%, notably in Hong Kong, the UK and Mexico, driven by spread compression (mainly in the UK).
- LICs increased by $0.1bn, notably in Mexico, reflecting growth in unsecured lending balances.
- Operating expenses were 1% lower as inflation and investments were more than offset by transformation and other cost-saving initiatives.

Key events:

- Our retail banking revenue rose by 1%, with increases in current account and savings partly offset by falls in credit card and mortgage revenue, reflecting spread compression, mainly in the UK.
- In the UK, growth in mortgage balances was facilitated by our expansion into the mortgage intermediary market, with 12 brokers added in 2016, which accounted for 7% of our new mortgage originations during 2016.

Profit before tax ($bn)
2016 2015 2014

Change in adjusted profit before tax

-6%

Commercial Banking ('CMB')

CMB serves approximately two million customers in 54 countries and territories. Our customers range from small enterprises focused primarily on their domestic markets through to corporates operating globally.

It supports our customers with tailored financial products and services to allow them to operate efficiently and to grow.

Services provided include working capital, term loans, payment services and international trade facilitation, among other services, as well as expertise in mergers and acquisitions, and access to financial markets.

Revenue growth in a challenging market

- Adjusted profit before tax of $6.1bn was 12% higher than in 2015 primarily because of lower LICs, and revenue growth despite challenges in global trade.
- Adjusted revenue rose by $0.1bn or 1%. This included growth of $0.2bn in GLCM driven by increased balances and wider spreads in Hong Kong. Revenue in Credit and Lending also increased (up $0.1bn), reflecting continued loan growth in the UK. This was partly offset by lower revenue in Global Trade and Receivables Finance ('GTRF').
- LICs reduced by $0.4bn as 2016 included lower levels of individually assessed LICs, as well as a net release of collective allowances primarily relating to charges made in the fourth quarter of 2015, notably in the oil and gas sector.
- Operating expenses reduced compared with 2015 as the effect of inflation was more than offset by ongoing cost discipline and the impact of our transformation initiatives. This helped us achieve positive jaws of 2.1%.
- Management initiatives drove a further reduction in RWAs of $23bn in 2016, leading to a cumulative reduction of $46bn since our Investor Update in 2015, $18bn above our target.

Key events:

- Despite the fall in global trade, we gained market share in key markets, including trade finance in Hong Kong and Singapore, and Receivables Finance in the UK.
- HSBC was named '2016 Best Trade Bank in the World' by *Trade and Forfaiting Review*, and won the 'Best Global Cash Manager for Non-Financial Institutions' at the *Euromoney* Awards 2016.

Profit before tax ($bn)
2016 2015 2014

Change in adjusted profit before tax

+12%

Global Banking and Markets ('GB&M')

GB&M serves approximately 4,100 clients in more than 50 countries and territories. It supports major government, corporate and institutional clients worldwide. Our product specialists continue to deliver a comprehensive range of transaction banking, financing, advisory, capital markets and risk management services.

Markets revenue up despite challenging market conditions

- Adjusted profit before tax of $5.6bn was $63m higher than in 2015, as revenue increased and operating expenses decreased, reflecting transformational cost savings, partly offset by an increase in LICs.
- Adjusted revenue of $14.9bn rose $353m or 2%, despite adverse movements in Credit and Funding valuation adjustments compared with favourable movements in 2015 (net effect, down $297m), primarily relating to movements on our own credit spreads on structured liabilities. Excluding these, revenue rose $650m or 5%, mainly in Rates and Credit, as we gained market share in Europe. In GLCM, revenue increased as we grew average balances and benefited from wider spreads. By contrast, revenue fell in Equities, reflecting lower trading volumes in Europe and Asia.
- LICs increased (up $0.4bn), predominantly driven by a small number of individually assessed exposures within the oil and gas, and metals and mining sectors, notably in the first half of 2016 in the US.
- Operating expenses fell by $93m, reflecting reduced performance-related pay, disciplined cost management, efficiency improvements including technology delivery rationalisation, and FTE reductions. These reductions more than offset the investments we made in the business.

Key events:

- Through 2016, we continued to focus on delivery of our RWA reductions, and achieved a reduction of $8bn, which included $39bn through management initiatives, partly offset by business growth.
- 'World's Best Investment Bank' – *Euromoney* Awards for Excellence 2016

Profit before tax ($bn)

Adjusted	
2016	5.6
2015	5.5
2014	4.9

Change in adjusted profit before tax

+1%

Global Private Banking ('GPB')

GPB serves high net worth individuals and families, including those with international banking needs, through 13 booking centres covering our priority markets.

Our products and services include Investment Management, incorporating advisory, discretionary and brokerage services; Private Wealth Solutions, comprising trusts and estate planning, designed to protect wealth and preserve it for future generations; and a full range of private banking services.

Lower revenue reflecting repositioning and adverse market conditions

- Adjusted profit before tax of $0.3bn fell by $0.1bn as revenue decreased, partly offset by a reduction in costs.
- Adjusted revenue of $1.8bn fell by $0.2bn or 11%, as brokerage and trading activity in both Europe and Asia decreased. This reflected the continued impact of client repositioning, in addition to adverse market sentiment and unfavourable market conditions throughout the year.
- Operating expenses decreased by $0.1bn, primarily as a result of reduced FTEs and cost-saving initiatives.

Key events:

- There was negative net new money of $17bn, reflecting the repositioning of the business. However, we attracted positive net new money in key markets targeted for growth, notably in the UK, Channel Islands and Hong Kong.
- We recognised a $3.2bn write-off relating to the goodwill of the business in Europe, which is not reflected in the adjusted performance. For additional information, refer to Note 20 on page 238 of the *Annual Report and Accounts 2016*.

Profit before tax ($bn)

Adjusted	
2016	0.3
2015	0.4
2014	0.5

Change in adjusted profit before tax

-25%

Corporate Centre

During 2016, we established the Corporate Centre, to better reflect the way we manage our businesses. Corporate Centre comprises Central Treasury, including Balance Sheet Management ('BSM'), our legacy businesses, interests in associates and joint ventures, central stewardship costs that support our businesses and the UK bank levy.

Lower revenue due to continued disposal of legacy portfolios and Central Treasury, partly offset by a reduction in costs

- Adjusted profit before tax of $2.0bn was $0.5bn or 19% lower, driven by a fall in revenue and lower income from associates, partly offset by lower operating expenses, notably a reduced charge relating to the UK bank levy.
- Revenue fell by $1.2bn, partly driven by reductions in our US CML portfolio ($0.5bn) as a result of lower average lending balances and portfolio sales. Revenue also fell in Central Treasury as a result of higher adverse fair value movements relating to the economic hedging of our long-term debt ($0.2bn) and higher interest expense ($0.2bn).
- LICs were broadly unchanged as increased charges in the US CML portfolio were broadly offset by higher releases of credit risk provisions in the legacy credit portfolio.
- Operating expenses were $0.8bn lower, partly reflecting the benefits of transformational savings in our technology, operations and other functions, and a lower UK bank levy charge (down $0.5bn).
- Income from associates was $0.1bn lower, primarily in Saudi Arabia.

Key events:

- Completed asset sales of $10bn from our US CML run-off portfolio. As at 31 December 2016, gross lending balances in this portfolio were $5.7bn.

Profit before tax ($bn)

Adjusted	
2016	2.0
2015	2.5
2014	3.8

Change in adjusted profit before tax

-19%

For further details on the financial performance of our global businesses, see pages 45 to 51 of the *Annual Report and Accounts 2016*.

Regions

We coordinate activities across global businesses and supporting functions through a regional structure.

Europe

We serve clients in Europe with a broad range of services, and facilitate international trade and investment. London is the strategic hub for GB&M.

Reported loss before tax included significant items of $8.4bn

– Reported loss before tax was $6.8bn. This compared with a reported profit before tax of $688m in 2015, with the fall driven by a net adverse movement in significant items, including the write-off of goodwill relating to our GPB business, adverse fair value movements arising from changes in credit spreads on our own debt designated at fair value compared with favourable movements in 2015, and higher costs to achieve.

– On an adjusted basis, profit before tax of $1.6bn fell by $0.5bn or 26%, as revenue decreased by $0.9bn (5%), partly offset by lower costs (down by $369m or 2%), which included a reduction of $0.5bn related to the UK bank levy, and a reduction in LICs of $37m (8%).

– Reported revenue fell by $5.0bn, primarily as a result of adverse movements of $1.8bn arising from changes in credit spread on our own debt, compared with favourable movements of $0.8bn in 2015, and the adverse effects of currency translation differences ($1.6bn). Adjusted revenue fell by $945m or 5%, reflecting a reduction in RBWM of $465m (7%), notably in life insurance manufacturing in France as a result of adverse market updates, and in GPB reflecting the repositioning of the business. In Corporate Centre, lower adjusted revenue (down $0.8bn), partly reflected higher adverse fair value movements of $0.2bn relating to the economic hedging of our long-term debt, and higher interest expense of $0.2bn. These reductions were partly offset by growth in revenue in GB&M ($0.2bn), notably in Rates, GLCM and Global Banking, and in CMB ($0.2bn), in Credit and Lending.

– Reported costs rose by $2.6bn, primarily reflecting a write-off of goodwill relating to our GPB business of $3.2bn and an increase of $1.5bn in costs to achieve, partly offset by the favourable effects of currency translation of $1.3bn. Adjusted costs fell by $0.4bn (2%). Excluding the reduction in the UK bank levy ($0.5bn), costs rose by 1% driven by higher charges from our global service and technology centres due to increased transformation activities relating to IT transformation and process improvement.

Profit before tax ($bn)
■ 2016 ■ 2015

Asia

HSBC's history is founded on financing trade with Asia, and the continent remains central to our strategy. We aim to grow our business in China's Pearl River Delta and the ASEAN region, and we continue to strengthen our leadership position in the internationalisation of China's renminbi currency.

Lower revenue, notably in Wealth Management, offset by cost management initiatives

– Reported profit before tax was $13.8bn, $2.0bn lower than for 2015, notably due to the non-recurrence of a gain of $1.4bn on the disposal of part of our shareholding in Industrial Bank.

– On an adjusted basis, profit before tax was broadly unchanged, as a decrease in revenue was offset by a reduction in costs.

– Reported revenue fell by $2.0bn, driven by the non-recurrence of the gain on Industrial Bank, as noted above, and the adverse effects of currency translation differences of $0.3bn. Adjusted revenue decreased by $253m (1%). Lower adjusted revenue in RBWM resulted from investment distribution income falling, reflecting weaker market sentiment compared with a strong performance in the first half of 2015. This was partly offset by wider deposit spreads and deposit balance growth. In GB&M, adjusted revenue also declined, mainly in Equities and Foreign Exchange, partly offset by increases in Rates. By contrast, revenue in Corporate Centre increased, notably as income from Balance Sheet Management, within Central Treasury, rose.

– Reported costs decreased by $104m, as an increase in costs to achieve of $354m was partly offset by the favourable effects of currency translation differences of $177m. Adjusted costs decreased by $227m (2%), notably as a result of cost management initiatives, which more than offset the effects of inflation and our investment growing our business in China's Pearl River Delta and the ASEAN region.

Profit before tax ($bn)
■ 2016 ■ 2015

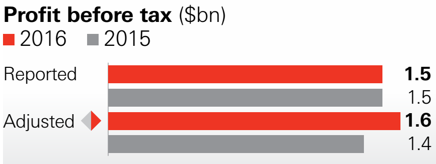
Middle East and North Africa

HSBC is the longest-serving international bank in the region, with one of the largest networks there, offering a universal banking model and playing a vital role in facilitating international trade. Our priority markets in the region are Saudi Arabia, Egypt and the United Arab Emirates ('UAE').

Strong performance reflecting robust cost management and lower LICs

- Reported profit before tax was $1.5bn, and was broadly unchanged from 2015.
- On an adjusted basis, profit before tax increased by $178m (13%), primarily reflecting a reduction in costs of $142m, and a decrease in LICs of $135m, partly offset by lower share of profit in associates and joint ventures.
- Reported revenue fell by $210m, primarily due to the adverse effects of currency translation differences ($182m). Adjusted revenue decreased marginally, mainly reflecting reductions in RBWM in Turkey as we restructured our business there, and in CMB in the UAE, mainly within GTRF, in part reflecting customer exits. This was partly offset by GB&M with growth in GLCM, which benefited from interest rate rises across the region, in Global Banking mainly driven by infrastructure and real estate fee income in the UAE and Egypt, and Securities Services due to higher balances and spreads.
- Reported LICs fell by $154m with adjusted LICs decreasing by $135m, mainly in CMB in the UAE due to lower charges and the release of provisions taken in 2015, notably relating to exposures in the oil and gas sector.
- Costs were $137m lower on a reported basis, and $142m (9%) lower on an adjusted basis, mainly in the UAE and Turkey due to cost-saving initiatives, which more than offset our continued investment in compliance.
- Share of profit in associates and joint ventures fell by $70m (14%), mainly due to higher impairment charges in Saudi British Bank and lower revenue in HSBC Saudi Arabia reflecting lower asset management and investment banking revenues. This was partly offset by revenue growth in Saudi British Bank and well-managed costs in both associates.

Profit before tax ($bn)



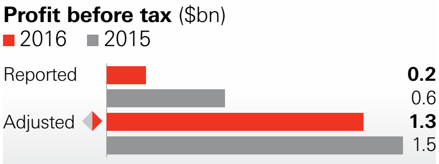
North America

The US is a key partner in global trade, and the US dollar remains the primary currency for global trade and payments. We support our North American customers within the NAFTA region and around the world, helping them grow their businesses.

Continued run-off of the US CML portfolio led to a fall in revenue, partly offset by cost reductions across all businesses

- Reported profit before tax was $185m, and fell by $429m from 2015, partly reflecting the net adverse effects of significant items, notably higher costs to achieve of $298m.
- Adjusted profit before tax fell by $208m (14%) from the continued reduction in our US CML run-off portfolio.
- Reported revenue fell $592m, and included the adverse effects of significant items ($57m) and currency translation of $59m. Movements in significant items were primarily driven by minimal fair value movements arising from changes in credit spread on our own debt in 2016, compared with favourable movements of $219m in 2015, although these movements were partly offset by a gain of $116m recorded on our sale of Visa US shares in 2016 and lower losses on disposal in our CML run-off portfolio of $77m. Adjusted revenue was $475m lower, primarily from a decrease in income in the US CML run-off portfolio in Corporate Centre. By contrast, adjusted revenue in GB&M increased by 6%, notably as a result of increased income in Rates and Credit driven by higher client flows and collateralised financing activity.
- LICs increased by $188m on a reported basis and $191m on an adjusted basis, primarily as a result of a small number of individually assessed charges in the mining sector in GB&M, as well as higher charges in the US CML run-off portfolio. In CMB, there were net collectively assessed releases in 2016, compared with charges in 2015, relating to exposures in the oil and gas sector.
- Reported costs fell by $353m, although this included a rise of $298m in costs to achieve in significant items, partly offset by a reduction in fines, penalties and charges in relation to legal matters of $128m. Adjusted costs fell by $460m, reflecting lower staff costs across all businesses.

Profit before tax ($bn)



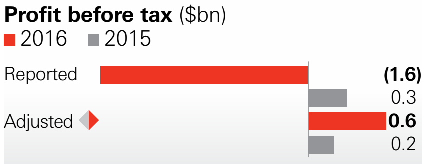
Latin America

We are focusing on growing our business in Mexico, where we are among the top five banks by assets and our branch network has a market share of more than 10%. On 1 July 2016, we completed our sale of operations in Brazil, but we will continue to provide access to the region for large multinational companies.

Continued progress in strategic initiatives with a strong business performance

- Reported loss before tax was $1.6bn. This compared with a profit of $310m in 2015, with the loss driven by a number of significant items, primarily the accounting loss on our sale of Brazil operations which totalled $1.7bn.
- On an adjusted basis, profit before tax rose by $0.4bn due to higher revenue, partly offset by higher LICs and costs.
- Reported revenue fell by $3.9bn, partly driven by the accounting loss on our sale of Brazil operations ($1.7bn). The reported results also include the revenue earned in our Brazil business of $1.5bn in 2016, compared with $3.3bn in 2015, and the adverse effects of currency translation differences of $0.9bn. However, adjusted revenue was $0.7bn (29%) higher than for 2015. We increased revenue in RBWM in Mexico with lending growth and an increase in market share across core retail portfolios, and in Argentina, reflecting wider spreads and growth in deposits, together with higher income from insurance. Revenue also increased in GB&M, partly due to increased client activity, and in CMB from lending and deposit balance growth.
- Reported LICs fell by $266m, primarily driven by a reduction in Brazil ($184m) and favourable effects of currency translation ($120m). By contrast, adjusted LICs rose by $38m due to higher LICs in RBWM in Mexico of $124m reflecting growth in unsecured lending and a rise in delinquency rates, partly offset by lower LICs in CMB and GB&M.
- Reported costs fell by $1.7bn, and included $1.1bn of costs relating to Brazil in 2016, compared with $2.5bn in 2015. These also included the favourable effects of currency translation differences ($0.6bn). Excluding these factors, adjusted costs increased by $0.3bn (or 16%), although this was below the average rate of inflation in the region as we continued to control our costs.

Profit before tax ($bn)



How we do business

We conduct our business intent on supporting the sustained success of our customers, people and communities.

Building lasting business relationships

We serve more than 37 million customers around the world, ranging from individuals to the largest companies. We are committed to conducting our business in a way that delivers fair value to customers and supports them in realising their ambitions.

Conduct and ensuring fair outcomes

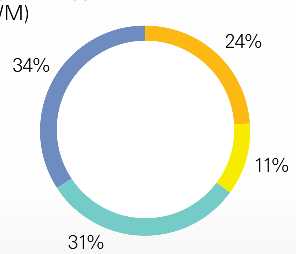
Operating with high standards of conduct is central to our long-term success and ability to serve customers. In 2016, we continued to embed good conduct practice across all our businesses, with a range of initiatives to further improve the service and experience we offer to customers.

For example, in the UK we have introduced a simplified overdraft charging structure with real time notifications to prompt customers whenever they are at risk of incurring unarranged overdraft charges. In the UAE, we automated pricing for foreign exchange to provide clients with consistent and competitive rates for cross-currency payments. We also enhanced our investment advice processes and introduced tools and guidelines to make all our customer communication clear and easy to understand.

These and related initiatives are guided by our Conduct Framework, which focuses on delivering fair customer outcomes and improved market integrity through our behaviours. The Conduct Framework guides activities to strengthen our business, and increases our understanding and awareness of how the decisions we make affect customers and other stakeholders.

Additional detail on the Conduct Framework is available online at www.hsbc.com/conduct. For further details on regulatory compliance risk and on conduct-related costs included in significant items, see pages 81 and 62, respectively, of the *Annual Report and Accounts 2016*.

Complaint types
(RBWM)



Key
- Product – features and policy
- Product – fees and charges
- Other product-related complaints
- Service complaints

Our values

Our values define who we are as an organisation and make us distinctive.

Open

We are open to different ideas and cultures, and value diverse perspectives.

Connected

We are connected to our customers, communities, regulators and each other, caring about individuals and their progress.

Dependable

We are dependable, standing firm for what is right and delivering on commitments.

Increasing quality of service

We rely on customer feedback to help determine where we can make improvements. In RBWM, we conducted more than 1.6 million customer surveys in 2016 across multiple points of customer interaction, including live online chat. We also improved the speed and quality of complaint resolution with more than two-thirds of retail customer complaints resolved on first contact, an improvement of 9% compared with 2015.

Customer feedback helps us to identify and address root causes of complaints. For example, we increased capacity in our call centres in response to concerns about long waiting times in the UK. We also addressed the most common complaints related to fees and charges through increased staff training and customer communication. As a result, complaints of this type reduced significantly in a number of our markets, including a 35% reduction in Hong Kong and a 27% reduction in France.

Innovation and technology

Our customers increasingly use digital channels to interact, including mobile banking. We are investing in innovation and technology to serve customers better and enhance security around financial transactions and customer data. In 2016, we introduced voice biometric identification technology for retail customers globally. HSBC is one of the first large-scale global users of this technology.

In the UK, we also launched a mobile application for commercial banking customers that allows them to digitally verify their identity. Since its launch, nearly 80% of the customers able to use this digital channel have chosen to do so. We have also adjusted our branch network to reflect changing customer needs and concluded our retail branch review in the UK, with a further reduction of 117 branches in 2016.

In Hong Kong, we launched a research and development lab in partnership with the government to promote technology development for the financial sector. Areas of focus include biometrics, data analytics, cybersecurity and internet finance. Separately, we are developing a mobile application to help retail customers manage all of their finances more effectively through a single interface.

Sustainable finance

We recognise that reducing global carbon dioxide emissions is a critical challenge for society. We seek to be a leader in managing climate change risk while developing opportunities with our customers. We continue to facilitate investment in areas such as infrastructure and renewable energy that help lower carbon dioxide emissions.

In 2016, for example, we helped issue the largest-ever renewable energy bond in Canada to support a solar power farm. In the UK, we provided financing and asset management expertise to support deployment of energy smart meters throughout the country. In December, we established a team dedicated to sustainable finance within the business in order to engage clients more effectively in assessing and responding to potential impacts from climate change.

255,000
workday hours volunteered

$137m
charitable giving in 2016

Empowering people

Valuing diversity

Building a more diverse and inclusive workforce is critical to developing a sustainable and successful business. Our approach aims to increase and leverage diversity of thought to improve workforce agility, enhance our risk management capability, drive innovation and grow markets.

Our diversity and inclusion ambitions focus on attracting, developing and retaining talent that reflects our customers and the communities where we do business, and deploying that talent effectively to anticipate and address expectations. Our seven global employee networks support this strategy and focus on gender, age, ethnicity, LGBT+, faith, working parents and carers, and ability. We have continued our focus on improving gender balance within senior leadership.

Supporting our employees

We believe that if someone is worth talking to, they are worth listening to. Exchange meetings are our way of doing that: meetings with no agendas and where managers are participants rather than leaders. These meetings bring people together to listen to each other, and allow people to express themselves without interruption or rebuttal. Our employee surveys indicate that Exchange participants respond positively by 11% more than others when asked if there is honest, two-way communication.

Similarly, our At Our Best programme reinforces the habits required for a strong culture, including asking for feedback, being mindful of one's own emotions and deploying tools for making better decisions. In 2016, nearly 100,000 employees attended an At Our Best training course, and a further 18,000 managers attended similar training centred on managing teams.

The programme is supported through a behaviour recognition scheme and the launch of Our Charter, a framework for good decision-making.

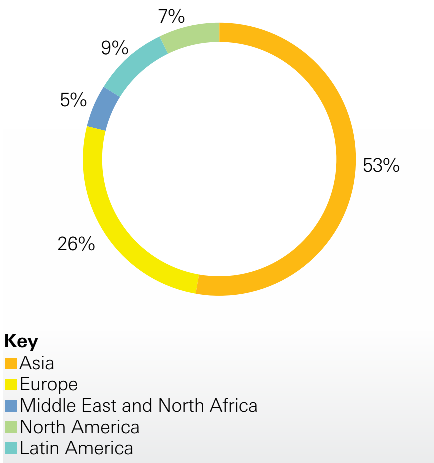
To further strengthen our culture and promote positive behaviours, we have developed culture change plans that are regularly discussed in global and local management forums. The plans emphasise enabling a speak-up culture, principles-based judgement and other behaviours that are key to supporting the Group's strategic objectives such as managing financial crime risk. In 2016, our employees completed more than eight million courses in person or through online learning in order to build skills and reinforce behaviours more broadly.

We have a wellbeing programme that provides benefits and services to support employees' wellness. For example, we offer free, confidential counselling to address personal issues at home or work. We also allow employees who have been at HSBC for five years or more to apply to take a sabbatical. Above all, we aim to provide a working environment where colleagues can talk openly about wellbeing issues, including anxiety and stress. Such measures are particularly valuable amid the demands of multiple change programmes and financial crime remediation initiatives.

Whistleblowing

We operate a global whistleblowing platform, HSBC Confidential, which allows staff to report matters of concern confidentially. During 2016, employees have raised more than 1,100 cases. Common themes among the cases raised included concerns regarding staff behaviour and recruitment practices, allegations of fraud perpetrated by staff, and weaknesses in incentive arrangements and information security.

Employees (FTEs) by region



Exchange meeting insights

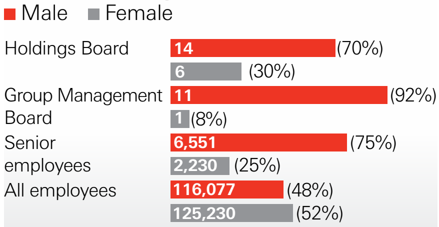
(% of employees who believe Exchange allows them to talk freely about issues important to them)

84%

Employee retention

81.7%

Gender diversity statistics



Ensuring sustainable outcomes

Our Global Sustainability function works with our global businesses, global functions and our regions to manage environmental and social issues that affect the Group and on which we can have an impact. Key issues are reviewed below and further details are available online at www.hsbc.com/sustainability. Sustainability performance data for 2016 will be available in spring 2017.

Climate change

We have committed to supporting the global shift to a low-carbon economy. Our award-winning Global Research team published 60 reports on sustainability topics in 2016. These included the implications of the Paris Agreement on climate change.

In light of the Paris Agreement, we reviewed our mining and metals policy, and included restrictions on lending to new thermal coal mines, in addition to our existing policies on coal-fired power plants and deforestation. We also added more specific guidance on human rights impacts that could arise in the mining sector.

For more information about our sustainability risk policies see page 84 of the *Annual Report and Accounts 2016*.

We completed a number of GB&M and CMB client transactions that help lower carbon dioxide emissions in areas including infrastructure and renewable energy. In 2016, HSBC was the third-ranked bookrunner for green, social and sustainability bonds that exceeded $250m excluding self-led transactions by Dealogic. We also published a report on our own green bond, issued in 2015.

We scored the highest grade in a global index run by CDP, a not-for-profit organisation that rates companies and governments on how they are tackling the climate change challenge. We also published an HSBC Statement on Climate Change, providing a summary of our approach and initiatives.

We are reducing the amount of energy we consume, and increasing the proportion from renewable sources. By the end of 2016, more than 17% of our electricity was from wind or solar farms, compared with 9% in 2015. We signed additional agreements in 2016 to increase the percentage of the electricity we use from new wind and solar sources. In total, we have agreements in place to meet 23% of our global electricity needs from these sources by 2018.

We report our carbon dioxide emissions on page 62 of the *Annual Report and Accounts 2016*.

Sustainable investment

Our Global Research team has expanded its environmental, social and governance research offering, hiring analysts to specifically cover social and governance drivers, and to cover the fast-growing green bond market.

Our Global Asset Management business published a new climate change policy to encourage the transition to a low-carbon economy and increase the climate resilience of clients' investments.

Human rights

We have issued our first statement as required by the UK's Modern Slavery Act, which can be found at www.hsbc.com.

We updated our supplier code of conduct to take account of revised legislation on modern slavery and human rights. More than 240 of our largest suppliers have already accepted this code.

Community investment

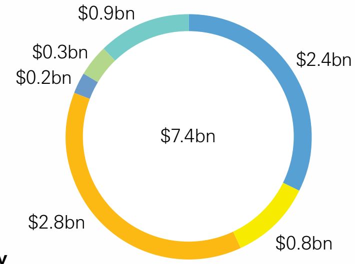
In 2016, we contributed $137m to charitable programmes, and our employees volunteered 255,000 hours in community activities during the working day.

Our flagship environmental partnership, the HSBC Water Programme, exceeded its five-year targets at the end of 2016. Building on this success, we are extending the programme for a further three years.

In 2016, we renewed our commitments to our two flagship global education programmes, the HSBC Youth Opportunities Programme and Junior Achievement More than Money, for another three years. These programmes help young people access education and realise their potential.

Tax

Taxes paid by region



Key
- UK
- Rest of Europe
- Asia
- Middle East and North Africa
- North America
- Latin America

Taxes paid by HSBC relate to HSBC's own tax liabilities including tax on profits earned, employer taxes, bank levy and other duties/levies such as stamp duty.

Our approach to tax

We apply the spirit and the letter of the law in all territories where we operate. We have adopted the UK Code of Practice for the Taxation of Banks. As a consequence, we pay our fair share of tax in the countries in which we operate. We continue to strengthen our processes to help ensure our banking services are not associated with any arrangements known or suspected to facilitate tax evasion. HSBC continues to apply global initiatives to improve tax transparency such as:

- the US Foreign Account Tax Compliance Act ('FATCA');
- the OECD Standard for Automatic Exchange of Financial Account Information (also known as the Common Reporting Standard);
- the Capital Requirements Directive IV ('CRD IV') Country by Country Reporting; and
- the OECD Base Erosion and Profit Shifting ('BEPS') initiative.

We do not expect BEPS or similar initiatives adopted by national governments to adversely impact HSBC's results. Further financial and tax information for the countries in which we operate will be published in 2017 in a CRD IV Country by Country report at www.hsbc.com/tax.

Risk overview

We actively manage risk to protect and enable the business.

Managing risk

HSBC has maintained a conservative and consistent approach to risk throughout its history, helping to ensure we protect customers' funds, lend responsibly and support economies. By carefully aligning our risk appetite to our strategy, we aim to deliver long-term shareholder returns.

All employees are responsible for the management of risk, with the ultimate accountability residing with the Board. We have a strong risk culture, which is embedded through clear and consistent communication and appropriate training for all employees. A comprehensive risk management framework is applied throughout the Group, with effective governance and corresponding risk management tools. This framework is underpinned by our risk culture and reinforced by the HSBC Values and our Global Standards programme.

Our Global Risk function oversees the framework, and is led by the Group Chief Risk Officer, an executive Director. It is independent from the global businesses, including our sales and trading functions, to provide challenge, appropriate oversight, and balance in risk/reward decisions.

HSBC's risk appetite defines its desired forward-looking risk profile, and informs the strategic and financial planning process. It is articulated in our Risk Appetite Statement, which is approved by the Board. Key elements include:

- risks that we accept as part of doing business, such as credit risk and market risk;
- risks that we incur as part of doing business, such as operational risk, which are actively managed to remain below an acceptable tolerance; and
- risks for which we have zero tolerance, such as knowingly engaging in activities where foreseeable reputational risk has not been considered.

We operate a comprehensive stress testing programme to help ensure the strength and resilience of HSBC, taking part in regulators' as well as our own internal stress tests. In 2016, we participated in the annual stress test by the Bank of England, our lead regulator, and again exceeded its requirements comfortably. This reflected our conservative risk appetite, and our diversified geographical and business mix. It also reflected our ongoing strategic actions, including the sale of our operations in Brazil, RWA reductions in GB&M and continued sales from our US CML run-off portfolio. Our internal stress test scenarios include potential macroeconomic, geopolitical and operational risk events, and events that are applicable to HSBC. The results help management understand material risks and consider potential mitigants.

Our risk management framework and risks associated with our banking and insurance manufacturing operations are described on pages 68 and 82, respectively, of the *Annual Report and Accounts 2016*.

Key risk appetite metrics

Component	Measure	Risk appetite	2016
Returns	Return on average ordinary shareholders' equity	≥10.0%	**0.8%**
Capital	Common equity tier 1 ratio – CRD IV end point basis	≥11.0%	**13.6%**
Liquidity	HSBC consolidated balance sheet advances-to-deposits ratio	≤90%	**67.7%**
Loan impairment charges	Loan impairment charges as % of advances: RBWM	≤0.50%	**0.37%**
	Loan impairment charges as % of advances: wholesale (CMB, GB&M and GPB)	≤0.45%	**0.27%**

Top and emerging risks

Our top and emerging risks framework helps enable us to identify current and forward-looking risks so that we may take action to either prevent them materialising or limit their effect.

Top risks are those that may have a material impact on the financial results, reputation or business model of the Group in the year ahead. Emerging risks are those that have large unknown components and may form beyond a one-year horizon. If these risks were to occur, they could have a material effect on HSBC.

During 2016, we made two changes to our top and emerging risks to reflect our assessment of their effect on HSBC. Firstly, 'IT systems infrastructure and resilience' was added as a new risk due to the need to ensure core banking systems remain robust as digital and mobile banking services continue to evolve. Secondly, 'Dispute risk' was removed as the key drivers of this thematic issue have already materialised and are therefore reported through other reporting channels. In addition, three thematic risks were renamed to better reflect the challenges facing HSBC. We use the new names in the table that follows.

Our current top and emerging risks are summarised on the next page and discussed in more detail on page 64 of the *Annual Report and Accounts 2016*.

Our approach to identifying and monitoring top and emerging risks is described on page 70 of the *Annual Report and Accounts 2016*.

Risk	Trend	Mitigants
Externally driven		
Economic outlook and capital flows	▲	We are actively monitoring our wholesale credit and trading portfolios to identify areas of stress following the UK electorate's vote to leave the European Union. We have also undertaken stress tests on our businesses and portfolios to assess potential impacts under a range of possible exit scenarios.
Geopolitical risk	▲	We have increased physical security at our premises where the risk of terrorism is heightened and have enhanced our major incident response capabilities.
Turning of the credit cycle	▶	A number of sectors remain under enhanced monitoring with risk appetite and new lending significantly curtailed, including our oil and gas and commodities lending portfolios.
Cyber threat and unauthorised access to systems	▲	We have brought all cybersecurity initiatives together under one programme in order to strengthen our resilience and defence capabilities. We have revised our cybersecurity risk appetite to reflect our evolving defence approach.
• Regulatory and technological developments with adverse impact on business model and profitability	▶	We are actively engaged with regulators and policy makers to help ensure that new regulatory requirements are considered fully and can be implemented in an effective manner. We have established a specialist digital solutions team to lead our response to new technologies.
Regulatory focus on conduct of business and financial crime	▶	We created a new function, Financial Crime Risk, which brings together all areas of financial crime risk management at HSBC and continued to enhance our management of conduct in areas including the treatment of potentially vulnerable customers, market surveillance, employee training and performance management.
US deferred prosecution agreement and related agreements and consent orders	▶	We are continuing to take concerted action to remediate anti-money laundering and sanctions compliance deficiencies and to implement Global Standards.
Internally driven		
IT systems infrastructure and resilience	▲	We have invested in specialist teams and are upgrading our systems capability to enhance data and digital capabilities and help ensure strong delivery quality and resilience to customers.
• Impact of organisational change and regulatory demands on employees	▶	We have increased our focus on resource planning and employee retention and well-being, and are developing initiatives to equip line managers with skills to both manage change and support their employees.
Execution risk	▶	The Group Change Committee monitored the progress of the high priority programmes across the Group that support the strategic actions, reviewing progress on deliverables and addressing resource prioritisation issues as they arose.
Third-party risk management	▶	To help enable a consistent risk assessment of the third-party services that the Group utilises, we are implementing a framework to provide a holistic view of third-party risks, which assesses third parties against key criteria, combined with associated control monitoring, testing and assurance throughout the third-party lifecycle.
• Enhanced model risk management expectations	▲	We have implemented a new global policy on model risk management and updated the model governance framework to address key internal and regulatory requirements. Additional resources have also been recruited to support the independent model review function.
Data management	▶	We continued to enhance our data governance, quality and architecture to help enable consistent data aggregation, reporting and management.

▲ Risk heightened during 2016

▶ Risk remained at the same level as 2015

• Thematic risk renamed during 2016

Remuneration

Our remuneration policy supports the achievement of our strategic objectives by balancing reward for short- and long-term sustainable performance.

Remuneration principles

The remuneration strategy for our employees is based on a series of key principles.

What we do

- Focus on total compensation with a strong link between pay and performance
- Judge not only what is achieved, but also how it is achieved, in line with the HSBC Values
- Operate a thorough performance management and HSBC Values assessment process
- Recognise and reward our employees for outstanding positive behaviour
- Design our policy to align compensation with long-term stakeholder interests
- Apply consequence management to strengthen the alignment between risk and reward

What we don't do

- Reward inappropriate or excessive risk taking or short-term performance at the expense of long-term company sustainability
- Use only a formulaic approach to determine bonuses for our executives
- Award discretionary bonuses to employees rated unacceptable against the HSBC Values and behaviours
- Allow our employees to hedge against their unvested or retained awards
- Offer employment contracts with a notice period of more than 12 months
- Have pre-arranged individual severance agreements

Embedding our values in our remuneration framework

Instilling the right behaviours, and driving and encouraging actions that are aligned to organisational values and expectations, are essential. We therefore have a number of programmes to reinforce our values.

Pay	Outcomes
Positive adjustments	– Individuals who exhibit exceptional conduct and behaviours are awarded positive variable pay adjustments during the year.
Global consequence management policy	– Ensures clear messaging to employees on the impact of any inappropriate conduct as part of reward communications, with consistency in approach and actions taken depending on the severity of the misconduct.
Global recognition programme	– Our global recognition programme is now available in more than 50 countries. – In 2016, approximately 600,000 recognitions were made with a total value of $8.1m.
Performance management	– Employees set objectives, which connect business, team and individual goals and are guided by expected behaviours aligned to our core values. – All employees receive a behaviour rating based on their adherence to HSBC Values to ensure performance is judged not only on what is achieved, but also on how it is achieved. – Employees and managers are encouraged to hold frequent conversations throughout the year, exploring alternative ways to stay connected outside the regular performance management cycle using a mix of informal and formal check-ins on a range of topics, including performance, development and wellbeing.

How we set our variable pay pool

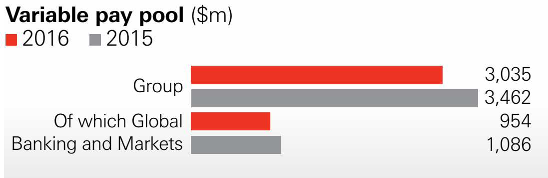
When deciding on the variable pay pool, the Remuneration Committee considers a number of factors, which are set out in the following table:

Performance and risk appetite statement	– Our variable pay pool takes into account our performance in the context of our risk appetite.
Countercyclical funding methodology	– To dampen effects of economic cycles, the variable pay pool's size has a floor and a ceiling, and we also limit the payout ratio as performance increases to prevent the risk of inappropriate behaviour.
Distribution of profits	– Our funding methodology ensures that the distribution of post-tax profit between capital, shareholders and variable pay is appropriate, and that the majority of post-tax profit is allocated to capital and shareholders.
Commerciality and affordability	– We face challenges arising from being headquartered in the UK, which has more stringent reward practices. We take into account these challenges in determining the size of the variable pay pool to ensure we can continue to attract and retain talent in key markets.

Our variable pay pool for 2016

Our variable pay pool is $3,035m, a decrease of 12.3% compared with 2015.

Variable pay pool ($m)



Remuneration for our executive Directors

Our remuneration policy for executive Directors was approved at our 2016 Annual General Meeting and implemented for the first time in 2016. Full details of our remuneration policy can be found online in our Directors' Remuneration Policy Supplement 2016.

The table below shows the amount our executive Directors earned in 2016.

For details of Directors' pay and performance for 2016, see the Directors' Remuneration Report on page 153 of the *Annual Report and Accounts 2016.*

(Audited)

(in £000)		Base salary	Fixed pay allowance	Pension	Annual incentive	GPSP/LTI [1]	Sub-total	Taxable benefits	Non-taxable benefits	Notional returns	Total
Douglas Flint	**2016**	**1,500**	**–**	**450**	**–**	**–**	**1,950**	**100**	**86**	**–**	**2,136**
	2015	1,500	–	750	–	–	2,250	151	95	–	2,496
Stuart Gulliver	**2016**	**1,250**	**1,700**	**375**	**1,695**	**–**	**5,020**	**557**	**71**	**27**	**5,675**
	2015	1,250	1,700	625	1,072	1,969	6,616	662	53	9	7,340
Iain Mackay	**2016**	**700**	**950**	**210**	**987**	**–**	**2,847**	**52**	**37**	**17**	**2,953**
	2015	700	950	350	1,068	1,101	4,169	54	28	5	4,256
Marc Moses	**2016**	**700**	**950**	**210**	**1,005**	**–**	**2,865**	**15**	**38**	**18**	**2,936**
	2015	700	950	350	827	1,101	3,928	6	29	5	3,968

[1] Executive Directors received Group Performance Share Plan ('GPSP') awards for 2015. For 2016, executive Directors will receive a long-term incentive ('LTI') award, with a performance period ending in 2019, which will be included in the single figure table for the financial year ending on 31 December 2019. If target performance is achieved for this award, LTI payout would be 50% of grant value. In this case, the 2016 total single figure for year-on-year comparison would be (in £000) £7,670 for Stuart Gulliver, £4,069 for Iain Mackay and £4,052 for Marc Moses.

Supplementary information

Status of the *Strategic Report 2016*

This is a part of HSBC Holdings plc's *Annual Report and Accounts 2016* and is not the Group's statutory accounts. It does not contain the full text of the Directors' Report, and it does not contain sufficient information to allow as full an understanding of the results and state of affairs of the Group and of its policies and arrangements concerning Directors' remuneration as would be provided by the full *Annual Report and Accounts 2016*.

Copies of the *Annual Report and Accounts 2016*

Further copies of the *Strategic Report 2016* and the *Annual Report and Accounts 2016* may be obtained from:

External Affairs
HSBC Holdings plc
8 Canada Square
London E14 5HQ
United Kingdom

Communications (Asia)
The Hongkong and Shanghai Banking Corporation Limited
1 Queen's Road Central
Hong Kong

US Communications
HSBC Bank USA, N.A.
1 West 39th Street, 9th Floor
New York, NY 10018
USA

The *Strategic Report 2016* and the *Annual Report and Accounts 2016* may also be downloaded from the HSBC website, www.hsbc.com.

Shareholder enquiries and communications

Enquiries

Any enquiries relating to your shareholdings on the share register, for example, transfers of shares, change of name or address, lost share certificates or dividend cheques should be sent to the Registrars at an address given below.

The Registrars offer an online facility, Investor Centre, which enables shareholders to manage their shareholding electronically.

Principal Register
Computershare Investor Services PLC
The Pavilions
Bridgwater Road
Bristol BS99 6ZZ
United Kingdom

Telephone: +44 (0) 870 702 0137

Email via website:
www.investorcentre.co.uk/contactus

Investor Centre:
www.investorcentre.co.uk

Hong Kong Overseas Branch Register
Computershare Hong Kong Investor Services Limited
Rooms 1712-1716, 17th Floor
Hopewell Centre
183 Queen's Road East
Hong Kong

Telephone: +852 2862 8555

Email: hsbc.ecom@computershare.com.hk

Investor Centre: www.investorcentre.com/hk

Holders of shares through Euroclear France
HSBC France
103 avenue des Champs Elysées
75419 Paris Cedex 08
France

Telephone: +33 1 40 70 22 56

Email: ost-agence-des-titres-hsbc-reims.hbfrdo@hsbc.fr

Website: www.hsbc.fr

Holders of ADSs
The Bank of New York Mellon
Depositary Receipts
PO Box 43006
Providence
RI 02940-3006
USA

Telephone (US): +1 877 283 5786
Telephone (international): +1 201 680 6825

Email: shrrelations@bnymellon.com

Website: www.bnymellon.com/shareowner

Bermuda Overseas Branch Register
Investor Relations Team
HSBC Bank Bermuda Limited
6 Front Street
Hamilton HM 11
Bermuda

Telephone: +1 441 299 6737

Email: hbbm.shareholder.services@hsbc.bm

Investor Centre:
www.investorcentre.co.uk/bm

Shareholder enquiries and communications (continued)

Enquiries (continued)

Persons whose shares are held on their behalf by another person may have been nominated to receive communications from HSBC pursuant to section 146 of the UK Companies Act 2006 ('nominated person'). The main point of contact for a nominated person remains the registered shareholder (for example, your stockbroker, investment manager, custodian or other person who manages the investment on your behalf).

Any changes or queries relating to a nominated person's personal details and holding (including any administration thereof) must continue to be directed to the registered shareholder and not HSBC's Registrars. The only exception is where HSBC, in exercising one of its powers under the UK Companies Act 2006, writes to nominated persons directly for a response.

Electronic communications

Shareholders may at any time choose to receive corporate communications in printed form or to receive notifications of their availability on HSBC's website. To receive future notifications of the availability of a corporate communication on HSBC's website by email, or revoke or amend an instruction to receive such notifications by email, go to www.hsbc.com/ecomms. If you provide an email address to receive electronic communications from HSBC, we will also send notifications of your dividend entitlements by email. If you received a notification of the availability of this document on HSBC's website and would like to receive a printed copy, or if you would like to receive future corporate communications in printed form, please write or send an email (quoting your shareholder reference number) to the appropriate Registrars at an address given on the previous page. Printed copies will be provided without charge.

A Chinese translation of this and future documents may be obtained on request from the Registrars. Please also contact the Registrars if you have received a Chinese translation of this document and do not wish to receive such translations in future.

Persons whose shares are held on their behalf by another person may have been nominated to receive communications from HSBC pursuant to section 146 of the UK Companies Act 2006 ('nominated person'). The main point of contact for a nominated person remains the registered shareholder (for example, your stockbroker, investment manager, custodian or other person who manages the investment on your behalf). Any changes or queries relating to a nominated person's personal details and holding (including any administration thereof) must continue to be directed to the registered shareholder and not HSBC's Registrars. The only exception is where HSBC, in exercising one of its powers under the UK Companies Act 2006, writes to nominated persons directly for a response.

股東可隨時選擇收取公司通訊的印刷本或收取有關公司通訊已上載於滙豐網站的通知。如欲以電郵方式收取日後有關公司通訊已上載於滙豐網站的通知，或撤銷或更改以電郵方式收取該等通知的指示，請登入www.hsbc.com/ecomms。若閣下提供電郵地址以收取滙豐發出的電子通訊，本公司亦會以電郵通知閣下應得的股息。若閣下收到本文件已上載於滙豐網站的通知，而欲獲得本文件的印刷本，或欲於日後收取公司通訊的印刷本，請致函或電郵（附上股東參考編號）至適用的股份登記處（地址見上頁）。印刷本將免費供應。

本文件及日後的相關文件均備有中譯本，如有需要，請向股份登記處索取。股東如收到本報告的中譯本，但不希望再收取此等譯本，亦請聯絡股份登記處。

股東如已委託其他人士代為持有股份，可能會獲提名（「獲提名人士」）收取滙豐根據英國《2006年公司法》第146條的規定發出的通訊。獲提名人士之主要聯絡人仍為登記股東（例如：股票經紀、投資經理、託管商或代表閣下管理投資的其他人士）。獲提名人士的個人資料及持股量（包括任何相關管理事宜）如有任何變更或查詢，必須繼續交由登記股東而非滙豐的股份登記處辦理，除非滙豐根據英國《2006年公司法》行使其中一項權力時，直接致函獲提名人士要求回應，則屬例外。

Report of the auditors

The auditors' report on the full accounts for the year ended 31 December 2016 was unqualified, and their statement under section 496 (whether the *Strategic Report 2016* and the *Annual Report and Accounts 2016* and the Directors' Report are consistent with the accounts) of the Companies Act 2006 was unqualified.

Certain defined terms

Unless the context requires otherwise, 'HSBC Holdings' means HSBC Holdings plc and 'HSBC', the 'Group', 'we', 'us' and 'our' refer to HSBC Holdings together with its subsidiaries. Within this document, the Hong Kong Special Administrative Region of the People's Republic of China is referred to as 'Hong Kong'. When used in the terms 'shareholders' equity' and 'total shareholders' equity', 'shareholders' means holders of HSBC Holdings ordinary shares and those preference shares and capital securities issued by HSBC Holdings classified as equity. The abbreviations '$m', '$bn' and '$tn' represent millions, billions (thousands of millions) and trillions of US dollars, respectively.

Published by Global Finance, HSBC Holdings plc, London

Designed by Addison Group, London

Printed by Park Communications Limited, London, on Revive 100 Offset board and paper using vegetable oil-based inks. Made in Austria, the stocks comprise 100% de-inked post-consumer waste. Pulps used are totally chlorine-free.

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Photography
Cover: courtesy of Dragages-China Harbour-VSL JV

Inside front cover: Huynh Nguyen Minh Thu, HSBC Bank (Vietnam) Ltd

Pages 2–3, 10–11, 12–13, 18–19, 20–21, 26–27: Getty Images

Pages 4 (Group Chairman), 7 (Group Chief Executive), 22–23: Charles Best

Inside back cover: Nurwata Yuda Pradana, The Hongkong and Shanghai Banking Corporation Limited, Indonesia

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