HSBC Bank plc

Annual Report and Accounts 2018

HSBC

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Presentation of Information

This document comprises the *Annual Report and Accounts 2018* for HSBC Bank plc ('the bank') and its subsidiaries (together 'the group'). 'We', 'us' and 'our' refer to HSBC Bank plc together with its subsidiaries. It contains the Strategic Report, the Report of the Directors, the Statement of Directors' Responsibilities and Financial Statements, together with the Independent Auditors' Report, as required by the UK Companies Act 2006. References to 'HSBC', 'HSBC Group' or 'Group' within this document mean HSBC Holdings plc together with its subsidiaries.

HSBC Bank plc is exempt from publishing information required by The Capital Requirements Country-by-Country Reporting Regulations 2013, as this information is published by its parent, HSBC Holdings plc. This information will be available in June 2019 on HSBC's website: www.hsbc.com.

Pillar 3 disclosures for the group are also available on www.hsbc.com, under Investors.

All narrative disclosures, tables and graphs within the Strategic Report and Report of the Directors are unaudited unless otherwise stated.

Our reporting currency is £ sterling.

Unless otherwise specified, all $ symbols represent US dollars.

Cautionary Statement Regarding Forward-Looking Statements

This *Annual Report and Accounts 2018* contains certain forward-looking statements with respect to the financial condition, results of operations and business of the group.

Statements that are not historical facts, including statements about the group's beliefs and expectations, are forward-looking statements. Words such as 'expects', 'anticipates', 'intends', 'plans', 'believes', 'seeks', 'estimates', 'potential' and 'reasonably possible', variations of these words and similar expressions are intended to identify forward-looking statements. These statements are based on current plans, estimates and projections, and therefore undue reliance should not be placed on them. Forward-looking statements speak only as of the date they are made. HSBC Bank plc makes no commitment to revise or update any forward-looking statements to reflect events or circumstances occurring or existing after the date of any forward-looking statement.

Forward-looking statements involve inherent risks and uncertainties. Readers are cautioned that a number of factors could cause actual results to differ, in some instances materially, from those anticipated or implied in any forward-looking statement.

Highlights

The group transferred its UK retail and qualifying commercial banking activities to HSBC UK Bank plc ('HSBC UK') on 1 July 2018 to meet the ring-fencing requirements of the Financial Services (Banking Reform) Act 2013 and related legislation.

The 2018 financial performance and position as disclosed in the Financial Statements and Notes on the Financial Statements on pages 87 to 165, and sections within the Strategic Report and Report of the Directors therefore reflect the transfer. The 2018 results include the income, expenses and cash flows associated with the transferred activities during the six months to 30 June 2018, which are disclosed as discontinued operations in Note 35 on the Financial Statements. Further details are provided in the Structural Reform section on page 18.

	Footnotes	2018	2017
For the year (£m)	1, 2		
Profit before tax (reported basis)		**1,974**	2,370
Profit before tax (adjusted basis)	3	**2,100**	3,832
Net operating income before change in expected credit losses and other credit impairment charges	4	**9,468**	13,052
Profit/(loss) attributable to shareholders of the parent company		**1,506**	1,809
At year-end (£m)	1, 2		
Total equity attributable to shareholders of the parent company		**26,878**	43,462
Total assets		**604,958**	818,868
Risk-weighted assets	5	**143,875**	233,073
Loans and advances to customers (net of impairment allowances)		**111,964**	280,402
Customer accounts		**180,836**	381,546
Capital ratios (%)	1,6		
Common equity tier 1		**13.8**	11.8
Tier 1		**16.0**	13.8
Total capital		**26.2**	16.9
Performance, efficiency and other ratios (annualised %)	1, 2		
Return on average ordinary shareholders' equity	7	**4.2**	4.4
Return on average risk-weighted assets		**1.1**	1.0
Adjusted return on average risk-weighted assets	5	**1.1**	1.6
Cost efficiency ratio (reported basis)	8	**77.6**	78.2
Cost efficiency ratio (adjusted basis)	8	**76.1**	67.5
Jaws (adjusted basis)	9	**(9.1)**	(5.8)
Ratio of customer advances to customer accounts		**61.9**	73.5

1 *The group adopted IFRS 9, as well as the European Union's regulatory transitional arrangements for IFRS 9, on 1 January 2018. Comparative information has not been restated. For further details, refer to 'Changes to accounting from 1 January 2018' on page 10, 'Standards adopted during the year ended 31 December 2018' on page 97 and Note 34 'Effects of reclassifications upon adoption of IFRS 9' on page 158.*

2 *HSBC completed the ring-fencing of its UK retail banking activities on 1 July 2018, six months in advance of the legal requirement coming into force, transferring circa 14.5 million qualifying RBWM, CMB and GPB customers from the group to HSBC UK, HSBC's ring-fenced bank. This included the transfer of relevant retail banking subsidiaries. We have retained the non-qualifying components, primarily the UK GB&M business and the overseas branches and subsidiaries. For further details, refer to 'Ring-fenced bank' on page 18 and Note 35 'Discontinued operations' on page 161.*

3 *Adjusted performance is computed by adjusting reported results for the effect of significant items as detailed on pages 12 to 15.*

4 *Net operating income before change in expected credit losses and other credit impairment charges is also referred to as revenue.*

5 *The group has adopted the European Union's regulatory transitional arrangements for IFRS 9, on 1 January 2018. These apply to reported and adjusted RWAs for 2018 (and related ratios) throughout the* Annual Report and Accounts 2018 *unless otherwise stated.*

6 *Capital ratios are detailed in the Capital section on pages 69 to 71.*

7 *The return on average ordinary shareholders' equity is defined as profit attributable to shareholders of the parent company divided by the average total shareholders' equity. The return on average ordinary shareholders' equity at 31 December 2017 has been restated by 20 basis points to incorporate the tax effect for dividends paid on Additional Tier 1 ('AT1') capital. Dividends paid on AT1 should be net of tax in the calculation.*

8 *Reported cost efficiency ratio is defined as total operating expenses (reported) divided by net operating income before change in expected credit losses and other credit impairment charges (reported), while adjusted cost efficiency ratio is defined as total operating expenses (adjusted) divided by net operating income before change in expected credit losses and other credit impairment charges (adjusted).*

9 *Adjusted jaws measures the difference between adjusted revenue and adjusted cost growth rates.*

Purpose and strategy

Our purpose

Our purpose is to be where the growth is, connecting customers to opportunities. We enable businesses to thrive and economies to prosper, helping people to fulfil their hopes, dreams and realise their ambitions.

We operate in 18 countries. Our operating entities represent the group to customers, regulators, employees and other stakeholders.

At 31 December 2018, the bank and its subsidiaries had a physical presence in Armenia, Belgium, Czech Republic, France, Germany, Greece, Ireland, Israel, Italy, Luxembourg, Malta, the Netherlands, Poland, Russia, South Africa, Spain, Switzerland and the United Kingdom. Two of these subsidiaries are located in Continental Europe's largest economies (i.e. France and Germany), with a universal banking presence in France.

Preparing for the UK's withdrawal from the European Union

The UK is due to formally leave the European Union (EU) on 29 March 2019. However, there is no certainty on the future relationship between the UK and the EU or indeed on an implementation period. Throughout this period of uncertainty, our priority is to support our clients and continue to service them, independent of the outcome of negotiations.

In preparation for potential outcomes including a possible departure without a Withdrawal Agreement, and to further strengthen our pan-European proposition, we have made changes to our legal entity structure and product offerings.

Legal entity structure

The group currently has branches in seven European Economic Area ('EEA') countries (Belgium, the Netherlands, Luxembourg, Spain, Italy, Ireland and Czech Republic) which rely on passporting out of the UK. Following regulatory approval in 2018, and on the assumption that the UK leaves the EU without the existing passporting or regulatory equivalence framework that supports cross-border business, the branch network is in the process of transferring to HSBC France ('HBFR'), as HSBC's primary banking entity authorised in the EU. We are on track to complete the business transfer in the first quarter of 2019 and good progress is being made on the operational integration with HBFR of its branches in Belgium, Czech Republic, Luxembourg, the Netherlands, Ireland, Italy and Spain.

Product offerings

To accommodate customer migrations and new business after the UK's EU departure, we are expanding and enhancing our capabilities across Europe, where we already have a strong foundation, with a focus on France, the Netherlands and Ireland. Euro clearing capabilities in HBFR are now available and further product launches are planned during the first quarter of 2019.

Potential outcomes arising from the UK's departure from the EU will impact our clients and our employees. Our focus is on mitigating this impact and providing support and guidance throughout the withdrawal process.

Clients

The UK's departure from the EU is likely to have an impact on our clients' operating models including their working capital requirements, investment decisions and financial markets infrastructure access. Our priority is to provide continuity of service and our intention is to minimise the level of change for our customers. However, we will be required to migrate some EEA-incorporated clients from the UK to HSBC France (or another EEA entity). We are in active dialogue with impacted clients to make the transition as smooth as possible.

Employees

The migration of EEA-incorporated clients will require us to strengthen our local teams in Continental Europe and France in particular. We expect the majority of roles to be filled through hires and we have started a recruitment process. Given the scale of our existing business in France, which already has more than 8,000 employees, a strong balance sheet and extensive product capabilities, we are already well prepared to handle the transfer of activities. Throughout, our objective is to minimise the level of change for our people. We are therefore also providing support on settlement applications to EEA staff resident in the UK and UK staff resident in EEA countries.

Nevertheless, London will continue to be an important global financial centre and the best location for our global headquarters. At 31 December 2018, HSBC employed approximately 39,000 people in the UK.

We have made good progress in terms of ensuring we are prepared for potential outcomes from the UK leaving the EU in the first quarter of 2019 under the terms described above, but there remain execution risks, many of them linked to the uncertain outcome of negotiations and potentially tight timelines to implement significant changes to our UK and European operating models.

HSBC worldwide

The group is part of HSBC, which has approximately 229,000 employees working around the world to provide more than 38 million customers with a broad range of banking products and services to meet their financial needs.

HSBC values

HSBC values define who we are as an organisation and what makes us distinctive.

Dependable

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

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.

Our role in society

How we do business is as important as what we do. Our responsibilities to our customers, employees and shareholders as well as to wider society go far beyond simply being profitable.

We seek to build trusting and lasting relationships with our many stakeholders to generate value in society.

Our strategy

HSBC Bank plc's strategic vision is to be the leading international bank in Europe.

The Group's strategy and strategic direction is embedded in HSBC Bank plc's strategy which aims to capture value from its international network.

This strategy is supported by long-term global trends and the Group's combination of strategic advantages.

Long-term trends

Increasing global connectivity

The international flow of goods, services and finance continues to expand, aided by the development of technology and data in personal and commercial exchanges.

Growing individual wealth

Studies indicate half of the world's population is now considered middle class or wealthier and this proportion is expected to grow to approximately two thirds by 2030. The majority of the middle class consumers are expected to be Asian. (Source: Brookings, "A Global Tipping Point: Half the world is now middle class or wealthier" (2018)).

Increasing need for sustainable finance

Climate change is accelerating and global temperatures are trending significantly higher. Investment in renewable energy capacity will be increasingly required. (Source: OECD, Investing in Climate, Investing in Growth (2017); BP, Statistical Review of World Energy; HSBC analysis)

Strategic advantages

Leading international bank

The group derives value from HSBC's network of businesses and geographical reach to support future growth and increase global connectivity. More than 50% of HSBC Group's client revenue is linked to international clients (revenue from international clients is derived from an allocation of adjusted revenue based on internal management information. International clients are businesses and individuals with an international presence). HSBC Group has been chosen by large corporates across regions as their lead international bank (Source: Greenwich Associates - Large Corporate Banking; percentage of large corporates choosing HSBC as their lead international bank).

Exceptional access to high-growth markets

HSBC's network provides access to high-growth developing markets in Asia, the Middle East and Latin America. We use it to enable clients to participate in global growth opportunities and our investments are aligned to high-growth markets to deliver shareholder value. We remain committed to enhanced customer service and investments in technology

Balance sheet strength

The group's diversified business model enables us to support a strong capital, funding and liquidity position, adopt a conservative approach to credit risk and liquidity management and generate stable returns for shareholders.

Strategic priorities

In June 2018, HSBC Group outlined eight strategic priorities to return HSBC to growth, improve returns and enhance customer and employee experience. HSBC Group aim to achieve this through accelerating growth in areas of strength, embracing new technologies, simplifying the organisation and investing in capabilities for the future. As a result of these strategic priorities, HSBC Group has defined overall financial targets.

We aim to:

- Accelerate growth from our Asian businesses, including in Hong Kong, the Pearl River Delta, ASEAN, and Wealth in Asia, including Insurance and Asset Management; and be the leading bank to support the transition to a low-carbon economy and the China-led Belt and Road Initiative
- Complete the establishment of our UK ring-fenced bank, increase mortgage market share, grow our commercial customer base, and improve customer service
- Gain market share and deliver growth from our international network
- Turn around our US business
- Improve capital efficiency and redeploy capital into higher-return businesses
- Create the capacity for increasing investments in growth and technology through efficiency gains
- Improve our customer service by investing further in technology and our digital capabilities; increasing our reach; and delivering industry-leading financial crime standards
- Simplify the organisation and invest in future skills

HSBC Bank plc delivers the relevant elements of HSBC Group strategy across Europe and overseas branches.

Value of the network

HSBC's network of businesses covers the world's largest and fastest growing trade corridors and economic zones.

Services around the world

We provide products and services to meet our clients' diverse financial needs. HSBC's geographic reach and network of clients allows greater insight into the trade and capital flows across supply chains.

Business synergies

We share resources and product capabilities across our businesses and leverage these synergies when serving our customers. We are able to provide global markets products, for example, to large multinationals as well as to small businesses. We issue insurance products to individuals and corporations alike. Many of our private banking clients are business owners who we also serve as corporate clients.

Products and services

The group manages its products and services through its four businesses: RBWM; CMB; GB&M; GPB; and Corporate Centre.

Retail Banking and Wealth Management ('RBWM')

Customers

RBWM helps over 1.2 million customers across Europe to manage their finances, buy their homes, and save and invest for the future. Our Insurance and Asset Management businesses support all HSBC's global businesses in meeting their customers' needs.

Products and services

RBWM offers a range of services, including personal banking, mortgages, loans, credit cards, savings and investments and insurance. This includes HSBC Jade, Premier and Advance propositions, wealth solutions and financial planning, personal banking and international services. We serve our customers through four main channels: branches, self-service terminals, telephone service centres and digital (internet and mobile banking).

Business synergies

RBWM makes a significant contribution to the overall success of the group. Insurance and Asset Management provide services to clients across all of the global businesses; and the foreign exchange and wealth management needs of RBWM clients create opportunities for GB&M and the Private Bank. There is also successful collaboration between CMB and RBWM in order to provide services to a broad range of business customers.

Areas of focus

RBWM's priorities are to deliver growth, improve returns and enhance customer and employee experience, as it continues to enhance customer centricity and customer service through investments in technology.

Commercial Banking ('CMB')

Customers

CMB customers range from small enterprises focused primarily on their domestic markets through to corporates operating globally.

Products and services

We support our customers with a range of financial products and services to enable them to operate efficiently and meet their business aspirations. We support our customers' operational and transaction banking needs through working capital facilities, payment services and trade solutions. We also offer expertise in capital financing, mergers and acquisitions, and access to financial markets to our customers.

Business synergies

CMB is at the centre of creating revenue synergies within the group. For instance, we work closely with our GB&M colleagues to provide expertise in capital finance solutions to support our CMB clients. Our trade teams within CMB also provide import and export finance solutions to GB&M clients.

Areas of focus

HSBC is focused on creating value from its network.

The group is investing heavily in digital and technology aspects of its core Global Liquidity and Cash Management ('GLCM') and Global Trade and Receivables Finance ('GTRF') propositions.

Global Banking and Markets ('GB&M')

Customers

HSBC Global Banking and Markets is a client-focused business that provides tailored financial solutions to major government, corporate and institutional clients worldwide. We operate in 18 countries across Europe and contribute significant revenues to other regions through our European client base. Managed as a global business, we offer clients geographical reach and deep local knowledge.

Products and services

Our clients are served by teams that bring together relationship managers and product specialists to develop financial solutions that meet individual client needs. We deliver a comprehensive range of services including capital financing, transaction and advisory banking services, trade services, research, securities services and global liquidity and cash management.

Areas of focus

Deepening client relationships, maximising our synergies with the Group and other Businesses, investments in transaction banking platforms and digital programmes focused on clients remains a priority.

Ongoing focus on cost discipline should result in further simplification of the business through streamlining business lines, operations and technology.

Our growth will be underpinned by a focus on highest standards of conduct and financial crime risk management.

Global Private Banking ('GPB')

Customers

GPB serves high net worth individuals and families, including those with international banking needs, through 6 strategic booking centres located in the EMEA region covering 19 target markets.

Products and services

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.

Business synergies

GPB collaborates closely with GB&M, CMB and RBWM, to offer propositions to clients that leverage the Group's expertise in asset management, research, insurance, trade finance and capital financing.

Areas of focus

GPB aspires to be the Private Bank of choice to the families of owners and principals of our best corporate clients, and help them preserve their wealth from generation to generation.

Corporate Centre

Corporate Centre comprises Central Treasury, including Balance Sheet Management ('BSM'), certain legacy assets, interests in our associates and joint ventures, and central stewardship costs.

How we do business

We conduct our business intent on supporting the sustained success of our people, customers and communities. To achieve our purpose, we need to build strong relationships with all of our stakeholders – including customers, employees, and the communities in which we operate. In 2018, we launched our ambition to become the healthiest human system in the financial services industry as a way to create stronger connections across these groups. This will enable us to deliver our strategy with our long-term values, and operate the business in a way that is sustainable.

Customers

We create value by providing the products and services our customers need, we aim to do so in a way that makes it easy for them. This helps us to build healthy and sustainable relationships with our customers.

Our customers range from individuals to major international corporate clients.

Taking responsibilities for the service we deliver

We define conduct as delivering fair outcomes for customers and not disrupting the orderly and transparent operation of financial markets. This is central to our long-term success and ability to serve customers. We have clear policies, frameworks and governance in place to protect them. These cover the way we behave, design products and services, train and incentivise employees, and interact with customers and each other. Our Conduct Framework guides activities to strengthen our business and increases our understanding of how the decisions we make affect customers and other stakeholders. Details on our Conduct Framework are available at www.hsbc.com

Acting on feedback

We listen to our customers and know that asking their opinion on our service is core to understanding their needs and concerns. For more details on how we perform with respect to non-financial metrics related to customer, refer to pages 8 and 9.

Acting on customer feedback has helped make our services more accessible and transparent.

Investing in digital

As part of our strategy, HSBC Bank plc is committed to using technology to enhance our customer experience.

Sustainable finance

Supporting sustainable growth

We recognise our wider obligations to the communities where we operate, and understand economic growth must also be sustainable. We will continue to engage with our stakeholders, and set policies that change in line with technology, science and societal expectations.

Our sustainable growth initiatives are set out in an integrated strategy aligned to our Group strategy and our global business operations. These initiatives are managed across three pillars: sustainable finance; sustainable networks and entrepreneurship; and future skills. Our progress update on sustainable finance is included below. The updates on sustainable networks and entrepreneurship and future skills will be published in our 2019 Environmental, Social and Governance ('ESG') Update.

Each and every one of us has a stake in developing a sustainable economic system. It is the combined responsibility of all players in society to respond to climate change, rapid technological change and continuing globalisation to secure a prosperous future. Since its foundation in 1865, HSBC Group has adapted to and helped serve the needs of a changing world. It has financed economic growth, fostered international trade and overcome events such as economic crises. We recognise that governments, corporations, the financial system and civil society are all stakeholders in climate change and sustainability challenges. Now more than ever, there is a need to develop the skills, business innovation and low-carbon solutions needed to secure long-term prosperity for all.

In 2017, HSBC Group launched its sustainability strategy focusing on three main areas: sustainable finance; sustainable networks and entrepreneurship; and future skills. This is underpinned by the Group's sustainability risk policies and approach to sustainable operations. We recognise our wider obligations to the communities in which we operate, and understand economic growth must also be sustainable. We will continue to engage with our stakeholders, and set policies that change in line with technology, science and societal expectations.

Our global progress update on our sustainability strategy is published annually in our HSBC ESG Update. (www.hsbc.com/our-approach/measuring-our-impact).

We define sustainable finance as any form of financial service that integrates ESG criteria into business or investment decisions. Sustainable finance covers the financing and investment activities needed to support the United Nations Sustainable Development Goals ('SDGs'), and the Paris Agreement.

A key objective for HSBC is to provide financing to enable the transition to a low-carbon economy and to help clients manage transition risk. Sustainable financing includes providing credit and lending facilities, as well as advisory services or access to capital markets. In 2017 HSBC committed to USD100 billion of financing and investments by 2025 to develop clean energy, lower-carbon technologies, and projects that contribute to the delivery of the Paris Climate agreement and the UN SDGs.

Sustainable finance case study

Société du Grand Paris ('SGP'), a state owned infrastructure entity established the first ever 100% Green Euro Medium Term Note ('EMTN') Programme and the net proceeds of the inaugural bond will be exclusively dedicated to finance the Grand Paris Express automatic metro, which is a key feature of the French Government Climate Plan. The project is anticipated to help create between 250,000 to 400,000 housing units, reduce 27 million tons of CO2 emissions by 2050 and substantially reduce commuting travel time on various journeys throughout the Greater Paris area.

In October 2018, HSBC France acted as joint Bookrunner on SGP's 10-year inaugural green benchmark of their Green EMTN Programme, a EUR 1.75 billion 1.125% green bond.

Sustainable finance training

In order to raise awareness of the transition to a low-carbon economy, the bank ran Sustainability training programmes in conjunction with Earthwatch, an environmental charity. In 2018 we ran 5 off-site training programmes where 87 employees attended the 2-day offsite Sustainability Training Programme whilst 11 senior leaders attended a 3-day Sustainability Leadership Programme. In addition, we launched on-line training in collaboration with the Cambridge Institute of Sustainability Leadership on our HSBC University platform.

How we do business in the community

Future skills

As part of HSBC's sustainability strategy the bank is focusing on Future Skills - for our customers, employees and for the people in our local communities. This is being achieved by concentrating on two key areas: employability and financial capability.

Employability

In France, HSBC is supporting Fondation Entreprende in order to increase Senior entrepreneurship. Due to high levels of unemployment of senior people (50% of 55-64 year olds), an increasing number of these people are choosing to become entrepreneurs as a way to maintain a social and economic activity (90,000 enterprises created by senior people in 2017). HSBC France supports Fondation Entreprendre to conduct market surveys, create an incubator to support Senior company creation and allow staff to volunteer as coaches in order to further develop the incubator.

Financial capability

Providing our customers, our communities and our employees with the skills and knowledge needed to thrive in the global economy, we are helping people secure their financial futures through building financial capability.

Community investment

We have a proud record of supporting the local communities and environments in which we operate. Thousands of HSBC employees across Europe are involved every year by volunteering with our charity partnerships and programmes. All employees can take a minimum of two days to volunteer for a charity of their choice in work time. There is also a fund to match fundraising or volunteering in their own time for up to three charities. Our local charity funding supports vulnerable people through the generations. We supported 43 charities across Europe raising a total of USD 7.9 million. Across their own time as well as work time our employees volunteered a total of 22,227 hours.

Empowering people

Enabling a diverse and inclusive environment for all

Our commitment

We are committed to a thriving environment where people are valued, respected and supported to fulfil their potential. By building upon the extraordinary range of ideas, backgrounds, styles and perspectives of our employees we can drive better outcomes for our stakeholders including customers, communities, suppliers and shareholders.

Gender balance at senior levels

We continue to focus on improving gender balance in senior leadership in line with our 30% Club CEO Campaign commitment to reach 30% women in senior leadership roles by 2020. In order to achieve that aspirational target, we set an objective of at least a 21.8% female share of our senior leadership by the end of 2018 in Europe. We achieved 23.3%, a 2.7 percentage point increase on our 2017 position.

Employee networks

We have seven global employee networks as well as our HSBC Communities, which include common interest groups. They provide spaces for colleagues to speak up about internal and commercial issues and opportunities, make connections, and learn from each other. The networks focus on gender, age, ethnicity, LGBT+, faith, working parents and carers, and ability.

More information about our diversity and inclusion activity is available at www.hsbc.com/our-approach/measuring-our-impact

Whistleblowing

It is important to have a culture where our people feel able to speak up. Individuals are encouraged to raise concerns about wrongdoing or unethical conduct through the usual reporting and escalation channels. However, we understand that there are circumstances where people need to raise concerns more discreetly. HSBC Confidential is a global whistleblower platform that enables all of our people, past and present, to raise issues in confidence and without fear of retaliation.

Whistleblowing concerns are investigated thoroughly and independently. Some of the common themes that have been referred to HSBC Confidential include behaviour and conduct, allegations of fraud, and weaknesses with information security. Remedial activity has been undertaken where appropriate, including disciplinary action and adjustments to variable pay, performance ratings and behaviour ratings. Processes have also been enhanced where needed. HSBC does not condone or tolerate any acts of retaliation against those who raise concerns, and has a strict policy prohibiting any such acts. Senior management are made aware of the existence and the outcome of cases where retaliation has been alleged. Making malicious or false claims is incompatible with our values.

The Group Audit Committee has responsibility for oversight of HSBC's whistleblowing arrangements and receives regular updates on the status of whistleblowing arrangements and outcomes.

363 cases were raised during 2018 (2017: 461 cases). All cases were subject to investigation. In 24% of the closed cases in 2018 (2017: 33%), allegations were substantiated in whole or in part and appropriate remedial action taken.

From 1 July 2018, cases relating to the ring-fenced activities of HSBC UK Bank plc have been excluded from the group's totals.

Tax

Our approach to tax

We apply the spirit as well as the letter of the law in all territories where we operate, and 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;
- the OECD Base Erosion and Profit Shifting ('BEPS') initiative; and
- the UK legislation on the corporate criminal offence ('CCO') of failing to prevent the facilitation of tax evasion.

We do not expect the BEPS or similar initiatives adopted by national governments to adversely impact our results.

Key Performance Indicators

The Board of Directors tracks the group's progress in implementing its strategy with a range of financial and non-financial measures or key performance indicators ('KPIs'). Progress is assessed by comparison with the group strategic priorities, operating plan targets and historical performance.

The group reviews its KPIs regularly in light of its strategic objectives and may adopt new or refined measures to better align the KPIs to HSBC's strategy and strategic priorities.

Financial KPIs

	2018	2017
Profit before tax (reported) (£m)	**1,974**	2,370
Profit before tax (adjusted) (£m)	**2,100**	3,832
Jaws (adjusted) (%)	**(9.1)**	(5.8)
Cost efficiency ratio (reported) (%)	**77.6**	78.2
Cost efficiency ratio (adjusted) (%)	**76.1**	67.5
Return on average risk-weighted assets (%)	**1.1**	1.0
Adjusted return on average risk-weighted assets (%)	**1.1**	1.6
Common equity tier 1 capital ratio (%)	**13.8**	11.8

Profit before tax (reported/adjusted): Reported profit before tax is the profit as reported under IFRS. Adjusted profit before tax adjusts the reported profit for the effect of significant items as detailed on pages 12 to 15.

Reported profit before tax was lower year-on-year. This was primarily in GB&M due to lower revenue, mainly in Global Markets, and higher operating expenses due to the non-repeat of 2017 provision releases relating to legal and regulatory matters. This was partly offset by lower Expected Credit Losses/Loan Impairment Charges (ECL/LICs).

Adjusted profit before tax decreased due to the impact of the discontinued operations from 1 July 2018. Revenue was also lower in GB&M, mainly in Global Markets, and in Corporate Centre due to losses on Legacy Credit portfolio disposals. Lower revenue was partly offset by lower ECL/LICs in GB&M.

Adjusted jaws measures the difference between adjusted revenue and adjusted cost growth rates (excluding the effects of costs-to-achieve and other significant items as detailed on pages 12 to 15). Our target is to grow revenues faster than operating expenses on an adjusted basis. This is referred to as positive jaws.

In 2018, revenue reduced by 29% and our operating expenses also went down, but by 19.9%. Jaws was therefore a negative 9.1%.

Adjusted costs decreased due to the impact of discontinued operations. Costs were also lower due to the transfer of costs from the bank to a separate service company in 2018. Since these costs had been recharged to other entities in the Group in 2017, there was an offsetting reduction in intercompany revenue. Adjusted revenue decreased due to the impact of discontinued operations, lower income in GB&M, mainly in Global Markets, and lower intercompany revenue in Corporate Centre.

Cost efficiency ratio (reported/adjusted) is measured as total operating expenses divided by net operating income before expected credit losses and other credit impairment charges.

In 2018, reported revenue decreased by 27% while reported operating expenses decreased by 28%. The cost efficiency ratio therefore improved by 0.6 percentage points.

Reported revenue and operating expenses decreased due to the impact of the discontinued operations on 1st July 2018. Excluding this, the cost efficiency ratio worsened by 7.1 percentage points mainly due to lower revenue and higher costs in GB&M.

The cost efficiency ratio (adjusted) worsened by 8.7 percentage points from 2017 as costs increased by more than revenue.

Return on risk-weighted assets ratio (reported/adjusted) is measured as pre-tax profit divided by average risk-weighted assets.

The reported return on average risk-weighted assets has increased by 0.1%. Of this, an increase of 0.3% was due to the impact of discontinued operations. Excluding this, the decrease in return on average risk-weighted assets was driven by lower profitability in GB&M.

The adjusted return on average risk-weighted assets has decreased by 0.5%. Of this, a decrease of 0.2% was due to the impact of discontinued operations. Excluding this, the decrease in return on average risk-weighted assets was driven by lower profitability in GB&M and Corporate Centre.

Common equity tier 1 ('CET1') capital ratio represents the ratio of common equity tier 1 capital to total risk-weighted assets. CET1 capital is the highest quality form of capital comprising shareholders' equity and related non-controlling interests less regulatory deductions and adjustments. The group seeks to maintain a strong capital base to support the development of its business and meet regulatory capital requirements at all times.

The CET1 capital ratio increased during the year mainly due to the implementation of the ring-fencing transfer scheme alongside the capital contribution from HSBC Holdings plc and HSBC UK Holdings Ltd.

Non-financial KPIs

We also monitor a range of non-financial KPIs focusing on customers, people, culture and values including customer service satisfaction, employee involvement and engagement, and diversity and sustainability.

For details on customer service and satisfaction please refer below; for the remaining non-financial KPIs refer to the Corporate Governance section on pages 72 to 78.

Customer service and satisfaction

RBWM

For RBWM in France the core metric used to assess performance is the Customer Recommendation Index (CRI), which measures customers' likelihood to recommend the banks' products and services, tracked relative to the competitor set.

In 2018, the CRI score remains consistent year on year and similar to the 2017 score. HSBC ranks in the top 3 banks within the competitive set and as such meets the target. HSBC performs well on key attributes versus competition, particularly on wealth solutions, reliability, relationship manager, customer service and international. However, there has been a slight decline in HSBC's performance compared with 2017, particularly in areas such as Customer Service and understanding.

HSBC will build on the positive momentum since 2017 in perceptions of its digital services, making it essential to continue supporting investments in Digital banking. This will help further boost perceptions of accessibility.

CMB

Customer experience, satisfaction and conduct are key priorities for CMB in Continental Europe. We continue to remain focused on enhancing our insights through relevant and measurable metrics that enables us to improve understanding of our customers. This in turn continues to help us to drive appropriate actions across our customers' experience with us.

In 2018, our customers have indicated that the key strengths of our existing franchise are the skills and knowledge of our people and our global international network. This is further complemented by our product and service capabilities which support our customers' business aspirations. We have received a number of external recognitions including 'Best in service for Trade Finance in Western Europe' from Euromoney in 2018.

Conversely, we acknowledge that we do not always consistently meet our customers' expectations. To address this, we are streamlining the onboarding process and conducting deep dives in these areas to identify opportunities for improvement. Further work has been planned for this year across all of these areas, focusing on utilising customer insights to drive appropriate changes required to improve overall customer experience and satisfaction.

GB&M

The core internal metric used to assess the strength of our client relationships in GB&M is the Client Engagement Score (a composite measure made up of seven questions, covering satisfaction, advocacy, loyalty, trust, emotion, value and rapport) which is tracked over time. The measure provides a score out of 100 and is benchmarked against the competition (competitors are self-defined by respondents).

In 2018 the Client Engagement Score for HSBC in Continental Europe was 86, in line with competitor scores, and slightly above the HSBC global score of 85. Our staff are considered a real asset by clients, consistently scoring highly on their professional integrity.

In Greenwich Associates' 2018 Large Corporate Cash Management report, HSBC continues to be second in Market Penetration among Top-Tier European companies (companies with at least EUR 2bn turnover per annum). Account opening is an area that our clients have highlighted where their experience lags behind their expectation levels. We will continue to build on the improvements we have already made, with a focus on simplifying the documentation process and increasing the responsiveness and resolution of errors.The bank won a number of awards in Europe in 2018, including Most Innovative Bank for Western Europe (The Banker Awards 2018).

Economic background and outlook

UK

UK real GDP rose by 0.2% in the last quarter of 2018, a sharp slowdown from the Q3 growth rate of 0.6% quarter-on-quarter. The year-on-year GDP growth rate was 1.3%, the joint slowest pace since 2012. The unemployment rate was broadly steady over the second half of 2018 - in November it stood at 4.0%, the lowest since February 1975. Employment as a percentage of the population aged 16-64 was 75.8% in November, a series high. The annual rate of wage growth rose over the course of the year, increasing to a new ten-year high of 3.4% for the three months to November. The annual Consumer Price Index (CPI) inflation rate dropped to 1.8% in January, down from 3.0% a year earlier, due to lower energy prices and a waning inflationary impact of the drop in sterling in 2016. The Bank of England increased Bank Rate in August, from 0.50% to 0.75%.

HSBC Global Research forecasts assume that the UK avoids a departure from the EU without a Withdrawal Agreement and begins to move towards agreement on a multi-year transition period. Under this assumption, calendar year GDP growth is expected to edge up to 1.6% in 2019 and 2020, from 1.4% in 2018. The unemployment rate is forecast to remain low, at around the 4% mark. CPI inflation is expected to fall to around 1.5% by Q4 2019, driven by recent oil price falls and soft underlying price pressures. Given outstanding uncertainties, mainly relating to the UK's withdrawal from the EU, the central forecast is for no Bank Rate rises through 2019 and 2020. But if a Withdrawal Agreement can be approved smoothly and quickly, the Bank of England might be more minded to raise rates.

Eurozone

Eurozone economic growth slowed through the course of 2018. GDP increased by 0.2% in the fourth quarter of 2018, unchanged versus Q3. The annual growth rate slowed from 1.6% to 1.2%, the weakest since 2013. In terms of quarterly growth in the fourth quarter, Germany's economy stagnated following a 0.2% contraction in Q3. Italy's economy contracted for the second successive quarter (-0.2% quarter-on-quarter following -0.1% in Q3). France saw an expansion of 0.3% for the second quarter in a row, while the Spanish economy continued its robust expansion by growing 0.7%. Relative to strong growth seen in 2017, the 2018 slowdown was largely driven by a softening in net exports and investment. The labour market remained fairly robust, though. The unemployment rate fell to a ten-year low of 7.9% in November, while annual wage growth climbed to a ten-year high of 2.5% in the third quarter of 2018. The Harmonised Index of Consumer Prices (HICP) rate of inflation softened towards the end of year, dropping to 1.4% in January, reflecting the impact of lower oil prices.

Following GDP growth of 1.8% in 2018, HSBC Global Research forecasts GDP to grow by 1.4% in 2019 and 1.3% in 2020. In terms of the drivers of growth, net exports are expected to remain subdued, while household spending is expected to make relatively solid gains, as a result of further rises in household income growth. But, given this subdued rate of economic growth, inflationary pressure is unlikely to build very rapidly. As a result of oil price falls, the HICP inflation rate is expected to fall to just below 1% in the autumn of 2019, before recovering thereafter, reaching a (still subdued) rate of 1.6% in 2020. In light of this soft inflation backdrop, alongside risks to the growth outlook, the European Central Bank (ECB) is forecast to keep key policy rates on hold throughout this year and next.

Financial summary

Use of non-GAAP financial measures

Our reported results are prepared in accordance with IFRSs, as detailed in the Financial Statements starting on page 86. In measuring our performance, the financial measures that we use include those derived from our reported results in order to eliminate factors that distort year-on-year comparisons. These are considered non-GAAP financial measures.

Non-GAAP financial measures are described and reconciled to the closest reported financial measure when used.

The global business segmental results on pages 12 to 15 are presented on an adjusted basis in accordance with IFRS 8 'Operating Segments' as detailed in 'Basis of preparation'.

Adjusted performance

Adjusted performance is computed by adjusting reported results for the year-on-year effects of significant items that distort year-on-year comparisons.

We use 'significant items' to describe collectively the group of individual adjustments excluded from reported results when arriving at adjusted performance. These items are ones that management and investors would ordinarily identify and consider separately when assessing performance to understand better the underlying trends in the business.

We consider adjusted performance provides useful information for investors by aligning internal and external reporting, identifying and quantifying items management believes to be significant and providing insight into how management assesses year-on-year performance.

Basis of preparation

Global businesses are our reportable segments under IFRS 8.

The global business results are assessed by the chief operating decision maker on the basis of adjusted performance that removes the effects of significant items from reported results. We therefore present these results on an adjusted basis.

Reconciliations of reported and adjusted performance are presented on pages 12 to 15. Our operations are closely integrated and, accordingly, the presentation of data includes internal allocations of certain items of income and expense. These allocations include the costs of certain support services and global functions to the extent that they can be meaningfully attributed to operational business lines. While such allocations have been made on a systematic and consistent basis, they necessarily involve a degree of subjectivity. Costs which are not allocated to global businesses are included in Corporate Centre.

Where relevant, income and expense amounts presented include the results of inter-segment funding along with intercompany and inter-business line transactions. All such transactions are undertaken on arm's length terms. The intra-group elimination items are presented in the Corporate Centre.

A description of the Global businesses is provided in the Strategic Report, page 5

Changes to accounting from 1 January 2018

IFRS 9

The group adopted the requirements of IFRS 9 'Financial Instruments' on 1 January 2018, with the exception of the provisions relating to the presentation of gains and losses on financial liabilities designated at fair value, which were adopted on 1 January 2017. The impact of transitioning to IFRS 9 at 1 January 2018 on the consolidated financial statements of the group was a decrease in net assets of £532m, arising from:

- a decrease of £764m from additional impairment allowances;
- an increase of £58m from the remeasurement of financial assets and liabilities as a consequence of classification changes, mainly from revoking fair value accounting designations for certain subordinated debt instruments; and
- an increase in net deferred tax assets of £174m.

Refer to 'Standards adopted during the year ended 31 December 2018' on page 97 and Note 34 'Effects of reclassifications upon adoption of IFRS 9' for further details.

Changes in accounting policy

We have considered market practices for the presentation of certain financial liabilities which contain both deposit and derivative components and were previously included in 'Trading liabilities'. Such liabilities amounted to £17,958m at 31 December 2017. We have concluded that a change in accounting policy and presentation is appropriate, since it would better align with the presentation of similar financial instruments by peers and therefore provide more relevant information about the effect of these financial liabilities on our financial position and performance.

As a result, rather than being classified as held for trading, these liabilities are classified as 'Financial liabilities designated at fair value' from 1 January 2018. Comparative information has not been restated.

A further consequence of this change in presentation is that movements in fair value attributable to changes in own credit risk of these liabilities are presented in other comprehensive income with the remaining fair value movements presented in profit or loss in accordance with the accounting policy adopted in 2017. Previously, all fair value movements related to these liabilities were included in profit or loss. For 2017, a loss of £335m relating to changes in the credit risk of these liabilities was included in 'Net income from financial instruments held for trading or managed on a fair value basis' with a credit of £96m recognised in 'Tax expense'. If the change in accounting policy had been applied retrospectively, these amounts would have been recognised in other comprehensive income, thereby resulting in a net increase in profit after tax for 2017 of £239m.

Cash collateral, margin and settlement accounts included in 'Trading assets' (£26,447m), 'Loans and advances to banks' (£573m) and 'Loans and advances to customers' (£394m) at 31 December 2017 were reclassified to 'Prepayments, accrued income and other assets' at 1 January 2018 in accordance with IFRS 9. Cash collateral, margin and settlement accounts included in 'Trading liabilities' (£30,755m), 'Deposits by banks' (£570m) and 'Customer accounts' (£548m) at 31 December 2017 were reclassified to 'Accruals, deferred income and other liabilities' at 1 January 2018 as this presentation is considered to provide more relevant information, given the change in presentation for the financial assets. Comparative information has not been restated.

Refer to 'Standards adopted during the year ended 31 December 2018' on page 97 and Note 34 'Effects of reclassifications upon adoption of IFRS 9' for further details.

Income statement presentation

The classification and measurement requirements under IFRS 9, which was adopted from 1 January 2018, are based on an entity's assessment of both the business model for managing the assets and the contractual cash flow characteristics of the assets. The standard contains a classification for items measured mandatorily at fair value through profit or loss as a residual category. Given its residual nature, the presentation of the income statement has been updated to separately present items in this category which are of a dissimilar nature or function, in line with IAS 1 'Presentation of Financial Statements' requirements. Comparative information has been re-presented. There is no net impact on total operating income.

Prior to 2018, foreign exchange movements on some financial instruments designated at fair value were presented in the same line in the income statement as the underlying fair value movement on these instruments. In 2018, foreign exchange movements on these instruments and their economic hedges are presented together within 'Net income from financial instruments held for trading or managed on a fair value basis'. Comparative information has been re-presented. As a result, the amount reported in 'Changes in fair value of long-term debt and related derivatives' decreased by £402m for 2017. There is no net impact on total operating income.

Summary consolidated income statement for the year ended[1]

	Footnotes	2018 £m	2017 £m
Net interest income		**3,660**	6,181
Net fee income		**2,044**	2,989
Net income from financial instruments measured at fair value	2, 3	**2,645**	3,505
Gains less losses from financial investments		**12**	262
Net insurance premium income		**2,005**	1,809
Other operating income		**580**	796
Total operating income	4	**10,946**	15,542
- of which: Discontinued operations		***3,132***	*5,997*
Net insurance claims, benefits paid and movement in liabilities to policyholders		**(1,478)**	(2,490)
Net operating income before expected credit losses and other credit impairment charges		**9,468**	13,052
Change in expected credit losses and other credit impairment charges		**(159)**	N/A
Loan impairment charges and other credit risk provisions		**N/A**	(495)
Net operating income		**9,309**	12,557
- of which: Discontinued operations		***3,037***	*5,767*
Total operating expenses	4	**(7,351)**	(10,208)
- of which: Discontinued operations		***(1,894)***	*(4,635)*
Operating profit		**1,958**	2,349
Share of profit/(loss) in associates and joint ventures		**16**	21
Profit before tax	1,3	**1,974**	2,370
- of which: Discontinued operations		***1,143***	*1,132*
Tax expense		**(442)**	(528)
Profit/(loss) for the year		**1,532**	1,842
Profit/(loss) attributable to shareholders of the parent company		**1,506**	1,809
Profit attributable to non-controlling interests		**26**	33

1 *The group adopted IFRS 9 on 1 January 2018. Comparative information has not been restated, apart from the re-presentation of certain income statement line items. For further details, refer to 'Changes to accounting' on page 10, 'Standards adopted during the year ended 31 December 2018' on page 97, and Note 34 'Effects of reclassifications upon adoption of IFRS 9' on page 158.*

2 *On 1 July 2018, HSBC completed the ring-fencing of its UK retail banking activities transferring qualifying RBWM, CMB and GPB customers from the group to HSBC UK, HSBC's ring-fenced bank. This included the transfer of relevant retail banking subsidiaries. We have retained the non-qualifying components, primarily the UK GB&M business and the overseas branches and subsidiaries. Refer to 'Ring-fenced bank' on page 18 and Note 35 'Discontinued operations' on page 161 for further details.*

3 *We have considered market practices for the presentation of certain financial liabilities which contain both deposit and derivative components and were previously included in 'Trading liabilities'. Such liabilities amounted to £17,958m at 31 December 2017. These liabilities are classified as 'Financial liabilities designated at fair value' from 1 January 2018. Comparative information has not been restated. For 2017, a loss of £335m relating to changes in the credit risk of these liabilities was included in 'Net income from financial instruments held for trading or managed on a fair value basis' with a credit of £96m recognised in 'Tax expense'. If the change in accounting policy had been applied retrospectively, these amounts would have been recognised in other comprehensive income, thereby resulting in a net increase in profit for 2017 of £239m. Refer to 'Changes to accounting from 1 January 2018' on page 10 and Note 34 'Effects of reclassifications upon adoption of IFRS 9' for further details.*

4 *Total operating income and expenses include significant items as detailed on pages 12 to 15.*

Reported performance

Reported profit before tax was £1,974m, £396m lower than 2017.

Net interest income ('NII') decreased by £2,521m or 41%. Of this, £1,855m was due to the impact of discontinued operations. Excluding this, NII decreased in Corporate Centre in Balance Sheet Management ('BSM') due to the effect of de-risking activities undertaken in 2017 and due to higher funding costs driven by liquidity requirements resulting from the ring-fencing of the UK bank. In GB&M, NII decreased due to margin compression and lower client activity in Global Markets. In RBWM, income decreased due to the transfer of our operations in Turkey to HSBC Middle East Holdings B.V and HSBC Bank Middle East Limited in June 2017, and from adverse market valuation adjustments on insurance manufacturing in France.

Net fee income decreased by £945m or 32%. Of this, £798m was due to the impact of discontinued operations. Excluding this, net fee income decreased in GB&M due to lower Global Banking revenue reflecting lower volumes and fee compression, in particular across Debt Capital Markets, Equity Capital Markets and Advisory product lines. In RBWM, income decreased due to the transfer of our operations in Turkey to HSBC Middle East Holdings B.V and HSBC Bank Middle East Limited in June 2017.

Net income from financial instruments designated at fair value decreased by £860m or 25%. Of this, £34m was due to the impact of discontinued operations. Income also decreased in RBWM in the Insurance business primarily reflecting deteriorating equity market conditions in France, which impacted the value of equity and unit trust assets supporting insurance contracts. Corresponding movements were recorded in the liabilities to customers, reflecting the extent to which they participate in the investment performance of the associated assets. The offsetting movements are recorded in 'Net insurance claims and benefits paid and movement in liabilities to policyholders'. This was partly offset in GB&M reflecting net adverse movements in debit valuation adjustments on derivative contracts.

Gains less losses from financial investments decreased by £250m or 95%. Of this, £40m was due to the impact of discontinued operations. Excluding this, income decreased in GB&M due to lower disposal gains in Principal Investments. In Corporate Centre, income decreased, notably in the UK, due to losses in Legacy Credit following portfolio disposals, undertaken to run-down the legacy business to release capital for other purposes.

Net insurance premium income increased by £196m or 11%, primarily due to increased net insurance premium income in France driven by improved commercial performance.

Net insurance claims, benefits paid and movement in liabilities to policyholders decreased by £1,012m or 41%. This was primarily in the Insurance business largely reflecting lower returns on financial assets supporting contracts where the policyholder is subject to part or all of the investment risk. This reflected unfavourable equity market performance in France compared with favourable performance in 2017 as well as higher claims and benefits paid. These decreases were partly offset by the impact of higher new business in France. The gains or losses recognised on the financial assets measured at fair value through profit and loss that are held to support these insurance contract liabilities are reported in 'Net income from financial instruments designated at fair value'.

Other operating income decreased by £214m or 27%. Of this, £133m was due to discontinued operations. Excluding this, income decreased in Corporate Centre due mainly to lower recharges to other entities in the Group reflecting the transfer of

certain costs to ServCo in 2018. This was partly offset by increases in RBWM driven in part by favourable movements in the present value of in-force long-term insurance business ('PVIF') in 2018 compared with 2017, in GB&M from the recovery of costs relating to the foreign exchange business from other HSBC Group entities, and in CMB in part due to the non-repeat of prior year fair value losses on investment properties in Malta.

Changes in expected credit losses and other impairment charges ('ECL') were £159m in 2018. Of this, £94m related to discontinued operations. The remaining charge was mainly in GB&M in the construction and retail sectors, partly offset by releases of provisions in the retail and telecoms sectors. In Corporate Centre, there was a net ECL release following Legacy Credit portfolio disposals.

Loan impairment charges and other credit risk provisions ('LICs') were £495m in 2017. Of this, £229m was due to discontinued operations. The remaining charge was mainly in GB&M due to two large corporate exposures in the construction and retail sectors. This was partly offset in Corporate Centre by net releases in Legacy Credit following portfolio disposals.

Total operating expenses decreased by £2,857m or 28%. Of this, £2,742m was due to the impact of discontinued operations. The decrease also included the impact of a number of significant items including:

- a decrease in costs-to-achieve of £551m, comprising costs relating to the achievement of strategic actions following the completion of this programme at the end of 2017;
- lower UK customer redress costs of £19m; partly offset by
- net legal and regulatory provision releases of £70m in 2018, compared with releases in 2017 of £540m;
- higher costs of structural reform of £141m.

Excluding these items, operating expenses decreased in Corporate Centre, partly offset by higher costs in GB&M. Lower costs in Corporate Centre were mainly due to the transfer of certain costs to a service company ServCo in 2018. Since these costs had been recharged from the bank to other entities in the Group in 2017, there was an offsetting reduction in intercompany revenue. The costs moved to ServCo primarily related to premises and equipment, and electronic data processing. Higher costs in GB&M were driven by higher temporary staff costs relating to regulatory projects and higher indirect taxes.

For further details of significant items affecting revenue and costs, please refer to significant revenue/cost items by business segment on pages 12 and 13.

Tax expense totalled £442m in 2018 compared with £528m in 2017. The effective rate of 22.4% in 2018 was broadly in line with prior year.

Adjusted performance

Significant revenue items by business segment – (gains)/losses

Audited	RBWM	CMB	GB&M	GPB	Corporate Centre	Total
	£m	£m	£m	£m	£m	£m
31 Dec 2018						
Reported revenue	**2,580**	**2,479**	**4,249**	**249**	**(89)**	**9,468**
Significant revenue items	**—**	**(34)**	**(42)**	**—**	**2**	**(74)**
– UK customer redress programmes	**—**	**(34)**	**—**	**—**	**—**	**(34)**
– debit valuation adjustment on derivative contracts	**—**	**—**	**(42)**	**—**	**—**	**(42)**
– fair value movement on non-qualifying hedges	**—**	**—**	**—**	**—**	**2**	**2**
Adjusted revenue	**2,580**	**2,445**	**4,207**	**249**	**(87)**	**9,394**
31 Dec 2017						
Reported revenue	4,097	3,490	4,436	321	708	13,052
Significant revenue items	2	77	166	—	(65)	180
– UK customer redress programmes	—	73	2	—	—	75
– debit valuation adjustment on derivative contracts	—	—	164	—	—	164
– fair value movement on non-qualifying hedges	—	—	—	—	(4)	(4)
– provisions arising from on-going review of compliance with the CCA in the UK	2	4	—	—	—	6
– gain on disposal of HSBC's interest in VocaLink Holdings Limited	—	—	—	—	(61)	(61)
Adjusted revenue	4,099	3,567	4,602	321	643	13,232

Significant cost items by business segment – (recoveries)/charges

Audited

	RBWM	CMB	GB&M	GPB	Corporate Centre	Total
	£m	£m	£m	£m	£m	£m
31 Dec 2018						
Reported operating expenses	**(2,102)**	**(1,143)**	**(3,335)**	**(188)**	**(583)**	**(7,351)**
Significant cost items	**68**	**9**	**(56)**	**—**	**179**	**200**
– costs of structural reform[1]	**—**	**4**	**26**	**—**	**154**	**184**
– UK customer redress programmes	**68**	**5**	**(17)**	**—**	**—**	**56**
– restructuring and other related costs	**—**	**—**	**—**	**—**	**30**	**30**
– settlements and provisions in connection with legal and regulatory matters	**—**	**—**	**(65)**	**—**	**(5)**	**(70)**
Adjusted operating expenses	**(2,034)**	**(1,134)**	**(3,391)**	**(188)**	**(404)**	**(7,151)**
31 Dec 2017						
Reported operating expenses	(3,641)	(1,571)	(2,885)	(251)	(1,860)	(10,208)
Significant cost items	569	20	(396)	(1)	1,090	1,282
– costs to achieve	69	6	147	(1)	817	1,038
– costs to establish UK ring-fenced bank	5	1	—	—	251	257
– UK customer redress programmes	495	12	2	—	—	509
– settlements and provisions in connection with legal and regulatory matters	—	—	(551)	—	11	(540)
– costs associated with the UK's exit from the EU	—	1	6	—	11	18
Adjusted operating expenses	(3,072)	(1,551)	(3,281)	(252)	(770)	(8,926)

1 *The current year 'cost of structural reform' includes 'costs associated with the UK's exit from the EU' of £97m and 'costs to establish UK ring-fenced bank' of £87m.*

Net impact on profit before tax by business segment

Audited

	RBWM	CMB	GB&M	GPB	Corporate Centre	Total
	£m	£m	£m	£m	£m	£m
31 Dec 2018						
Reported profit/(loss) before tax	**375**	**1,310**	**804**	**62**	**(577)**	**1,974**
Net impact on reported profit and loss	**68**	**(25)**	**(98)**	**—**	**181**	**126**
– Significant revenue items	**—**	**(34)**	**(42)**	**—**	**2**	**(74)**
– Significant cost items	**68**	**9**	**(56)**	**—**	**179**	**200**
Adjusted profit/(loss) before tax	**443**	**1,285**	**706**	**62**	**(396)**	**2,100**
31 Dec 2017						
Reported profit/(loss) before tax	329	1,779	1,193	60	(991)	2,370
Net impact on reported profit and loss	571	97	(230)	(1)	1,025	1,462
– Significant revenue items	2	77	166	—	(65)	180
– Significant cost items	569	20	(396)	(1)	1,090	1,282
Adjusted profit/(loss) before tax	900	1,876	963	59	34	3,832

By operating segment:

Adjusted profit for the year

(Audited)

	2018					
	RBWM	CMB	GB&M	GPB	Corporate Centre	Total
	£m	£m	£m	£m	£m	£m
Net operating income before change in expected credit losses and other credit impairment charges[1]	**2,580**	**2,445**	**4,207**	**249**	**(87)**	**9,394**
– external	**2,530**	**2,252**	**4,554**	**248**	**(190)**	**9,394**
– inter-segment	**50**	**193**	**(347)**	**1**	**103**	**—**
Change in expected credit losses and other credit impairment charges	**(103)**	**(26)**	**(110)**	**1**	**79**	**(159)**
Net operating income	**2,477**	**2,419**	**4,097**	**250**	**(8)**	**9,235**
Total operating expenses	**(2,034)**	**(1,134)**	**(3,391)**	**(188)**	**(404)**	**(7,151)**
Operating profit	**443**	**1,285**	**706**	**62**	**(412)**	**2,084**
Share of profit/(loss) in associates and joint ventures	**—**	**—**	**—**	**—**	**16**	**16**
Adjusted profit before tax[2]	**443**	**1,285**	**706**	**62**	**(396)**	**2,100**
	%	**%**	**%**	**%**		**%**
Adjusted cost efficiency ratio	**78.8**	**46.4**	**80.6**	**75.5**		**76.1**
	2017					
Net interest income	3,185	2,323	856	175	(283)	6,256
Net fee income	963	1,138	762	117	9	2,989
Net trading income	13	40	2,368	9	113	2,543
Other income	(62)	66	616	20	804	1,444
Net operating income before loan impairment charges and other credit risk	4,099	3,567	4,602	321	643	13,232
– external	3,840	3,784	5,142	242	224	13,232
– inter-segment	259	(217)	(540)	79	419	—
Loan impairment charges and other credit risk provisions	(127)	(140)	(358)	(10)	140	(495)
Net operating income	3,972	3,427	4,244	311	783	12,737
Total operating expenses	(3,072)	(1,551)	(3,281)	(252)	(770)	(8,926)
– employee compensation and benefits	(973)	(507)	(1,014)	(82)	(41)	(2,617)
– general and administrative expenses	(2,084)	(1,027)	(2,262)	(168)	(212)	(5,753)
– depreciation and impairment of property, plant and equipment	(6)	(17)	(3)	(1)	(293)	(320)
– amortisation and impairment of intangible assets	(9)	—	(2)	(1)	(224)	(236)
Operating profit	900	1,876	963	59	13	3,811
Share of profit in associates and joint ventures	—	—	—	—	21	21
Adjusted profit before tax[2]	900	1,876	963	59	34	3,832
	%	%	%	%		%
Adjusted cost efficiency ratio	74.9	43.5	71.3	78.5		67.5

1 *Net operating income before change in expected credit losses and other credit impairment charges/Net operating income before loan impairment charges and other credit provisions also referred to as revenue.*

2 *The group adopted IFRS 9 on 1 January 2018. Comparative information has not been restated.*

Adjusted performance

Our adjusted profit before tax decreased by £1,732m or 45% compared with 2017. Adjusted profit before tax decreased due to the impact of discontinued operations and lower revenue, partly offset by lower ECL and operating expenses.

Adjusted revenue decreased by £3,838m or 29%. Of this, £2,912m was due to the impact of discontinued operations. Revenue was also lower in GB&M due to a decrease in Global Markets revenue, notably in Rates due to lower volumes and margin compression as a result of challenging market conditions and reduced client activity. Revenue was also lower in Global Banking due to lower volumes and fee compression across a number of product lines. In Corporate Centre, revenue decreased mainly due to lower recharges to other entities in the Group, offset by lower operating expenses. This reflected the transfer of certain costs to ServCo in 2018. This was partly offset by higher revenue in CMB, primarily driven by higher revenue in the UK achieved through collaboration between our global businesses.

Adjusted ECL/LICs were £336m or 68% lower. Of this, £136m was due to the impact of discontinued operations. In 2018, ECL net charges (excluding discontinued operations) were primarily in GB&M due to an increase in charges in Global Banking, notably in the construction and retail sectors in the UK and Italy. This was partly offset by provision releases in Corporate Centre in Legacy Credit following portfolio disposals. In 2017, net LICs (excluding discontinued operations) were primarily driven by a number of large exposures in GB&M in Global Banking in the retail and construction sectors in the UK. This was partly offset by provision releases in Corporate Centre following disposal of assets in Legacy Credit.

Adjusted operating expenses decreased by £1,775m or 20%. Of this, £1,629m was due to the impact of discontinued operations. The remaining decrease was in Corporate Centre, primarily driven by the transfer of costs to ServCo in 2018. Since these costs had previously been recharged to other entities in the Group in 2017, there was an offsetting reduction in intercompany revenue. This was partly offset by an increase in operating expenses in GB&M reflecting higher costs relating to temporary staff and higher indirect taxes.

Retail Banking and Wealth Management

Adjusted profit before tax of £443m was £457m or 51% lower than 2017. Of this, £454m was due to the impact of discontinued operations.

Revenue decreased by £1,519m or 37%. Of this, £1,506m was due to the impact of discontinued operations. Revenue also decreased due to the transfer of our operations in Turkey to HSBC Middle East Holdings B.V and HSBC Bank Middle East Limited in June 2017. In France revenue was lower reflecting margin compression on lending and deposits, partly offset in insurance manufacturing due to favourable movements in the present value of in-force long-term insurance business ('PVIF') in 2018 compared with 2017. Our revenue was higher in the Channel Islands reflecting growth in deposit balances and higher margins.

ECL/LICs decreased by £24m or 19%. In 2018, ECL of £103m included charges relating to discontinued operations of £101m as well as increased provisions in Malta driven by model changes. In

2017, LICs of £127m included charges relating to discontinued operations of £103m, charges in our Turkey operations of £10m, as well as individually assessed provisions in France and Greece.

Operating expenses decreased by £1,038m or 34%. Of this, £1,050m was due to the impact of discontinued operations. Operating expenses also decreased due to the transfer of our operations in Turkey to HSBC Middle East Holdings B.V and HSBC Bank Middle East Limited in June 2017. This was partly offset by an increase in operating expenses, mainly in France due to higher staff, marketing and training costs.

Commercial Banking

Adjusted profit before tax of £1,285m was £591m or 31% lower than 2017. Of this, £596m was due to the impact of discontinued operations.

Revenue decreased by £1,122m or 31%. Of this, £1,146m was due to the impact of discontinued operations. Excluding this, revenue increased, mainly in the UK through collaboration between our global businesses.

ECL/LICs decreased by £114m or 81%. In 2018, ECL of £26m included net releases relating to discontinued operations of £8m. There were also charges in the UK relating to exposures in Turkey. In 2017, LICs of £140m included charges relating to discontinued operations of £116m as well as provisions in Armenia and Germany, partly offset by releases in Greece and Spain.

Operating expenses decreased by £417m or 27%. Of this, £426m was due to the impact of discontinued operations. Excluding this, expenses increased due to higher IT costs in France.

Global Banking and Markets

Adjusted profit before tax of £706m was £257m or 27% lower, primarily reflecting lower revenue and higher operating expenses, partly offset by lower LICs/ECL.

Revenue decreased by £395m or 9%. Of this, £76m was due to the impact of discontinued operations. Revenue decreased mainly in Global Markets, notably in Rates due to lower volumes and margin compression as a result of challenging market conditions and reduced client activity. Revenue was also lower in Global Banking, particularly across Debt Capital Markets, Equity Capital Markets and Advisory product lines due to lower volumes and fee compression.

ECL/LICs decreased by £248m or 69%. In 2018, ECL of £109m were in the construction and retail sectors, partly offset by releases of provisions in the retail and telecommunications sectors. In 2017, LICs of £357m mainly comprised two large exposures in the construction and retail sectors.

Operating expenses increased by £110m or 3%. Operating expenses related to discontinued operations decreased by £79m. Excluding this, the increase in operating expenses was due to higher temporary staff costs relating to regulatory projects, higher indirect taxes, and a legal settlement in relation to a class action.

Global Private Banking

Adjusted profit before tax of £62m was £3m or 5% higher than 2017. Excluding discontinued operations, profit before tax increased by a further £7m from 2017.

Revenue decreased by £72m or 22%. Of this, £90m was due to the impact of discontinued operations. Excluding this, revenue increased in the Channel Islands from increased deposits and higher income on deposits due to the increase in interest rates.

ECL/LICs decreased by £11m. Of this, £10m was due to the impact of discontinued operations. ECL in 2018 were therefore broadly in line with LICs in 2017.

Operating expenses decreased by £64m or 25%. Of this, £73m was due to the impact of discontinued operations. Excluding this, operating expenses were higher, driven by increased costs in Channel Islands relating to collaboration services from HSBC UK.

Corporate Centre

Adjusted loss before tax of £396m was £430m lower than 2017. Of this, £93m was due to the impact of discontinued operations. Excluding this, profit before tax decreased due to lower revenue and higher ECL/LICs, partly offset by lower operating expenses.

Revenue decreased by £730m. Of this, £96m was due to the impact of discontinued operations. Excluding this, revenue decreased mainly due to lower recharges to other entities in the Group, offset by lower operating expenses. This reflected the transfer of certain costs to ServCo in 2018. Revenue was also lower due to increased losses on Legacy Credit portfolio disposals as we accelerated the run-down of this legacy business to release capital for other purposes.

ECL/LICs decreased by £61m or 43%, mainly driven by impairment provision releases in Legacy Credit in 2018 following asset portfolio disposals.

Operating expenses decreased by £366m or 47%, mainly due to the transfer of certain costs to ServCo in 2018. Since these costs had previously been recharged from the bank to other entities in the Group in 2017, there was an offsetting reduction in intercompany revenue. The costs moved to ServCo related to premises and equipment, and electronic data processing.

Dividends

The consolidated reported profit for the year attributable to the shareholders of the bank was £1,506m.

Interim dividends of £583m, in lieu of a final dividend in respect of the previous financial year, and £234m in respect of 2018 were paid on the ordinary share capital during the year.

A second interim dividend of £406m, in lieu of a final dividend in respect of the current year, was declared after 31 December 2018, payable on 26 February 2019.

In addition, a special dividend of £674m on the ordinary share capital of HSBC Bank plc in respect of the current year was declared after 31 December 2018, payable on 26 February 2019.

Further information about the results is given in the consolidated income statement on page 87.

Review of business position

Summary consolidated balance sheet at 31 Dec

	2018	2017
	£m	£m
Total assets[1,2]	**604,958**	818,868
Cash and balances at central banks	**52,013**	97,601
Trading assets[3]	**95,420**	145,725
Financial assets designated and otherwise mandatorily measured at fair value through profit or loss	**17,799**	N/A
Financial assets designated at fair value	**N/A**	9,266
Derivatives	**144,522**	143,335
Loans and advances to banks[3]	**13,628**	14,149
Loans and advances to customers[3]	**111,964**	280,402
Reverse repurchase agreements – non-trading	**80,102**	45,808
Financial investments	**47,272**	58,000
Other assets[3]	**42,238**	24,582
Total liabilities[1,2]	**577,549**	774,819
Deposits by banks[4]	**24,532**	29,349
Customer accounts[4]	**180,836**	381,546
Repurchase agreements – non-trading	**46,583**	37,775
Trading liabilities[4,5]	**49,514**	106,496
Financial liabilities designated at fair value[5]	**36,922**	18,249
Derivatives	**139,932**	140,070
Debt securities in issue	**22,721**	13,286
Liabilities under insurance contracts	**20,657**	21,033
Other liabilities[4]	**55,852**	27,015
Total equity[1,2]	**27,409**	44,049
Total shareholders' equity	**26,878**	43,462
Non-controlling interests	**531**	587

1 *The group adopted IFRS 9 together with voluntary changes to accounting policy and presentation on 1 January 2018. Comparative information has not been restated. For further details, refer to 'Changes to accounting from 1 January 2018' on page 10, 'Standards adopted during the year ended 31 December 2018' on page 97, and Note 34 'Effects of reclassifications upon adoption of IFRS 9' on page 158.*
2 *On 1 July 2018, HSBC completed the ring-fencing of its UK retail banking activities transferring qualifying RBWM, CMB and GPB customers from the group to HSBC UK. This included the transfer of relevant retail banking subsidiaries. We have retained the non-qualifying components, primarily the UK GB&M business and the overseas branches and subsidiaries. Refer to 'Ring-fenced bank' on page 18 and Note 35 'Discontinued operations' on page 161 for further details.*
3 *Cash collateral, margin and settlement accounts included in 'Trading assets' (£26,447m), 'Loans and advances to banks' (£573m) and 'Loans and advances to customers' (£394m) at 31 December 2017 were reclassified to 'Prepayments, accrued income and other assets' at 1 January 2018 in accordance with IFRS 9. Comparative information has not been restated. Refer to 'Changes to accounting from 1 January 2018' on page 10 and Note 34 'Effects of reclassifications upon adoption of IFRS 9' for further details.*
4 *Cash collateral, margin and settlement accounts included in 'Trading liabilities' (£30,755m), 'Deposits by banks' (£570m) and 'Customer accounts' (£548m) at 31 December 2017 were reclassified to 'Accruals, deferred income and other liabilities' at 1 January 2018 as this presentation is considered to provide more relevant information, given the change in presentation for the financial assets. Comparative information has not been restated. Refer to 'Changes to accounting from 1 January 2018' on page 10 and Note 34 'Effects of reclassifications upon adoption of IFRS 9' for further details.*
5 *We have considered market practices for the presentation of certain financial liabilities which contain both deposit and derivative components and were previously included in 'Trading liabilities'. Such liabilities amounted to £17,958m at 31 December 2017. These liabilities are classified as 'Financial liabilities designated at fair value' from 1 January 2018. Comparative information has not been restated. Refer to 'Changes to accounting from 1 January 2018' on page 10 and Note 34 'Effects of reclassifications upon adoption of IFRS 9' for further details.*

Balance sheet information by global business

(Audited)

	RBWM	CMB	GB&M	GPB	Corporate Centre	Total
	£m	£m	£m	£m	£m	£m
31 Dec 2018						
Loans and advances to customers	**21,924**	**29,021**	**56,464**	**3,541**	**1,014**	**111,964**
Customer accounts	**29,961**	**34,716**	**103,387**	**6,514**	**6,258**	**180,836**
31 Dec 2017						
Loans and advances to customers	117,933	84,947	63,379	7,372	6,771	280,402
Customer accounts	151,985	100,831	94,069	12,774	21,887	381,546

There are no reconciling items between the adjusted and reported view of the balance sheet for 2018 and 2017.

The group maintained a strong and liquid balance sheet with the ratio of customer advances to customer accounts of 61.9% compared with 73.5% at 31 December 2017.

The reduction in the ratio of customer advances to customer accounts, as well as the reduction in the overall balance sheet size is a result of ring-fencing. Notably this impacted:

Assets

- Loans and advances to customers, which decreased by 60%;
- Cash and balances at central banks, which decreased by 47%;
- Financial investments, which decreased by 18%;

Liabilities

- Customer accounts decreased by 53%;

Equity

- The equity balance decreased by 38% as a result of transfer to HSBC UK.

Trading assets and liabilities decreased by 35% and 54% respectively as a result of reclassifications upon adoption of IFRS 9 as well as a reduction in equities business.

Debt securities in issue increased by 71% due to funding initiatives driven by both internal and regulatory requirements.

Repurchase and reverse repurchase agreements (non-trading) increased by 23% and 75% respectively as a result of increased market activity.

Reported performance by country

Profit before tax – by country

	Footnotes	Retail Banking and Wealth Management	Commercial Banking	Global Banking and Markets	Global Private Banking	Corporate Centre	Total
		£m	£m	£m	£m	£m	£m
31 Dec 2018							
United Kingdom	1	**402**	**1,018**	**582**	**44**	**(535)**	**1,511**
France		**(42)**	**128**	**20**	**12**	**(75)**	**43**
Germany		**10**	**64**	**74**	**6**	**(3)**	**151**
Other		**5**	**100**	**128**	**–**	**36**	**269**
Profit before tax		**375**	**1,310**	**804**	**62**	**(577)**	**1,974**
31 Dec 2017							
United Kingdom		320	1,491	704	50	(950)	1,615
France		(8)	158	181	4	(121)	214
Germany		16	48	111	7	30	212
Turkey	2	(9)	8	19	—	2	20
Other		10	74	178	(1)	48	309
Profit before tax		329	1,779	1,193	60	(991)	2,370

1 *On 1 July 2018, HSBC completed the ring-fencing of its UK retail banking activities transferring qualifying RBWM, CMB and GPB customers from the group to HSBC UK. This included the transfer of relevant retail banking subsidiaries. We have retained the non-qualifying components, primarily the UK GB&M business and the overseas branches and subsidiaries. Refer to 'Ring-fenced bank' on page 18 and Note 35 Discontinued operations on page 161 for further details.*

2 *On 29 June 2017, the Turkish operations transferred to HSBC Middle East Holdings B.V. and HSBC Bank Middle East Limited.*

Net interest margin

Net interest margin is calculated by dividing net interest income as reported in the income statement by the average balance of interest-earning assets. Average balances are based on daily averages of the group's activities.

Net interest margin of 0.88% was 48 basis points ('bps') lower than in 2017, including the effects of significant items, foreign currency translation and impacted by the transfer of the UK businesses to HSBC UK.

Net interest income

	2018	2017
	£m	£m
Interest income	**7,422**	9,043
Interest expense	**(3,762)**	(2,862)
Net interest income	**3,660**	6,181
Average interest-earning assets	**417,569**	453,182
	%	%
Gross interest yield	**1.58**	1.84
Less: cost of funds	**(0.77)**	(0.53)
Net interest spread	**0.81**	1.31
Net interest margin[1]	**0.88**	1.36

1 *Net interest margin is net interest income expressed as an annualised percentage of average interest-earning assets.*

Summary of interest income by asset type

	2018			2017		
	Average balance	**Interest income**	**Yield[1]**	Average balance	Interest income	Yield[1]
	£m	**£m**	**%**	£m	£m	%
Short term funds and loans and advances to banks	**85,186**	**146**	**0.17**	78,133	53	0.07
Loans and advances to customers	**188,956**	**4,865**	**2.57**	266,491	7,136	2.68
Reverse repurchase agreements - non trading	**64,462**	**404**	**0.63**	44,739	186	0.42
Financial investments	**52,153**	**902**	**1.73**	63,462	943	1.49
Other interest-earning assets	**26,812**	**268**	**1.00**	357	18	5.04
Total interest-earning assets	**417,569**	**6,585**	**1.58**	453,182	8,336	1.84
Trading assets and financial assets designated or mandatorily measured at fair value[2]	**70,958**	**1,906**	**2.69**	N/A	N/A	N/A
Trading assets and financial assets designated at fair value[2]	**N/A**	**N/A**	**N/A**	82,765	1,685	2.04
Expected credit losses provision	**(2,051)**	**—**	**—**	N/A	N/A	N/A
Impairment allowance	**N/A**	**N/A**	**N/A**	(2,328)	—	—
Non-interest-earning assets	**263,691**	**—**	**—**	300,521	—	—
Total assets	**750,167**	**8,491**	**1.13**	834,140	10,021	1.20

1 *Yield calculations include negative interest on assets recognised as interest expense in the income statement.*
2 *Interest income arising from trading assets is included within 'Net trading income' in the income statement.*

Summary of interest expense by type of liability and equity

	2018			2017		
	Average balance	**Interest expense[1]**	**Cost**	Average balance	Interest expense[1]	Cost
	£m	**£m**	**%**	£m	£m	%
Deposits by banks	**21,716**	**109**	**0.50**	17,293	54	0.31
Financial liabilities designated at fair value – own debt issued	**16,178**	**187**	**1.16**	17,307	218	1.26
Customer accounts	**222,970**	**1,343**	**0.60**	308,944	1,279	0.41
Repurchase agreements - non trading	**49,523**	**389**	**0.79**	39,239	152	0.39
Debt securities in issue and subordinated debts	**34,969**	**600**	**1.72**	21,846	377	1.73
Other interest-bearing liabilities	**32,729**	**297**	**0.91**	1,114	75	6.73
Total interest-bearing liabilities	**378,085**	**2,925**	**0.77**	405,743	2,155	0.53
Trading liabilities and financial liabilities designated at fair value (excluding own debt issued)[2]	**65,768**	**1,617**	**2.46**	91,830	1,167	1.27
Non-interest-bearing current accounts	**53,741**	**—**	**—**	49,527	—	—
Total equity and other non-interest bearing liabilities	**252,573**	**—**	**—**	287,040	—	—
Total equity and liabilities	**750,167**	**4,542**	**0.61**	834,140	3,322	0.40

1 *Cost of funding calculations include negative interest on liabilities recognised as interest income in the income statement.*
2 *Interest expense arising from trading liabilities is included within 'Net trading income' in the income statement.*

Structural reform

UK exit from EU

The structural reform in preparation of the UK's withdrawal from the EU is described under Areas of special interest within the Risk section, page 23.

Ring-fenced bank

Policy background

The UK Financial Services (Banking Reform) Act 2013 and associated secondary legislation and regulatory rules required UK deposit-taking banks with more than £25bn of 'core deposits' (broadly from individuals and small to medium-sized businesses) to separate their UK retail banking activities from their other wholesale and investment banking activities by 1 January 2019. The resulting UK ring-fenced bank ('RFB') entities need to be legally distinct, operationally separate and economically independent from the non-ring-fenced bank entities.

Ring-fencing rules have been published by the Prudential Regulation Authority ('PRA') determining how ring-fenced banks are permitted to operate. Further rules published by the FCA set out the disclosures that non-ring-fenced banks are required to make to prospective customers who are individuals.

Ring-fencing implementation

HSBC completed the ring-fencing of its UK retail banking activities on 1 July 2018, six months in advance of the legal requirement coming into force, transferring circa 14.5 million qualifying RBWM, CMB and GPB customers from HSBC Bank plc to HSBC UK Bank plc ('HSBC UK'), HSBC's ring-fenced bank. This included the transfer of relevant retail banking subsidiaries. HSBC Bank plc, which is HSBC's non-ring-fenced bank, has retained the non-qualifying components, primarily the UK GB&M business and the overseas branches and subsidiaries. The two banking entities will operate alongside each other, supported by services received from HSBC Global Services (UK) Limited ('UK ServCo').

The primary means of transferring HSBC Bank plc's qualifying customers and subsidiaries to HSBC UK was through a court-approved ring-fencing transfer scheme ('RFTS') as provided for in Part VII, section 106 of the Financial Services and Markets Act 2000 (as amended) ('FSMA'). In addition to these transfers, certain items were transferred through other legal arrangements.

Establishment of HSBC UK Bank plc

The establishment of HSBC UK was accounted for as a group restructuring. HSBC's accounting policy for such transactions requires that assets and liabilities were recognised by HSBC UK at their existing carrying amounts in the financial statements of the group.

Risk overview

The group continuously identifies and monitors risks. This process, which is informed by its risk factors and the results of its stress testing programme, gives rise to the classification of certain principal risks. Changes in the assessment of principal risks may result in adjustments to the group's business strategy and, potentially, its risk appetite.

Our banking risks are credit risk, operational risk, market risk, liquidity and funding risk, compliance risk and reputational risk. We also incur insurance risk.

In addition to these banking risks, we have identified top and emerging risks with the potential to have a material impact on our financial results or reputation and the sustainability of our long-term business model.

The exposure to our risks and risk management of these are explained in more detail in the Risk section of the Report of the Directors on pages 20 to 35.

During 2018, a number of changes to our top and emerging risks have been made, to reflect the revised assessment of their effect on the group. Two risks have been removed, 'Turning of the Credit cycle'; this risk will be controlled in line with the group's approach to managing credit through the cycle and "Increasing Regulatory expectations"; this risk has been removed as specific high impact regulatory change initiatives have dedicated coverage (such as the HSBC programme to manage the impact of the UK's exit from the EU) and the associated implications of such change initiatives will be covered through Execution Risk.

A new risk 'IBOR (Inter Bank Offered Rate) transition' was added during 2018 and also includes LIBOR (London Inter Bank Offered Rate).

Risk		Mitigants
Externally driven		
UK exit from EU	▲	The UK is due to leave the EU in March 2019 and negotiations are ongoing. We will continue to work with regulators, governments and our customers to manage the risks of the UK's exit from the EU (and the current period of uncertainty) as they arise, particularly across those sectors most impacted.
Geopolitical risk	▲	We continually assess the impact of geopolitical events on our businesses and exposures across Europe and take steps to mitigate them, where required, to help ensure that we remain within risk appetite. We have also strengthened physical security at our premises where the risk of terrorism is heightened.
Cyber threat and unauthorised access to systems	▶	We continue to strengthen our cyber control framework, in line with the changing threat environment and improve our resilience and cybersecurity capabilities, including threat detection and analysis, access control, payment system controls, data protection, network controls and backup and recovery.
Regulatory focus on conduct of business	▶	We continue to enhance our management of conduct in a number of areas, including the treatment of potentially vulnerable customers, market surveillance, employee training and performance.
Financial Crime Compliance	▶	We have integrated the majority of the Global Standards programme financial crime risk core capabilities into our day-to-day operations during 2018, and expect to complete the transition to business and function management in the first half of 2019. We continue to take further steps to refine and strengthen our defences against financial crime by applying advanced analytics and artificial intelligence.
Market illiquidity and volatility	▶	We monitor risks closely and report regularly on illiquidity and concentration risks to the PRA.
IBOR transition	●	We are evaluating the impact on HSBC's products, services and processes as the industry accord evolves, with the intention of minimising disruption through appropriate mitigating actions.
Internally driven		
People risk	▶	We continue to increase our focus on resource planning and employee retention and to equip line managers with the skills to both manage change and support their employees.
IT systems infrastructure and resilience	▶	We continue to monitor and improve service resilience across our technology infrastructure, enhancing our problem diagnosis/resolution and change execution capabilities, reducing service disruption to our customers.
Execution risk	▶	We continue to strengthen our prioritisation and governance processes for significant strategic, regulatory and compliance projects.
Model risk	▲	We have enhanced our model risk governance framework by establishing an independent second line of defence Model Risk Management sub-function, and enhancing our existing policy and standards in order to address evolving regulatory, external and internal requirements.
Data management	▲	We continue to improve our insights, consistency of data aggregation, reporting and decisions through ongoing enhancement of our data governance, data quality, data privacy and architecture framework.

▲ Risk has heightened during 2018

▶ Risk remains at the same level as 2017

● New risk introduced in 2018

On behalf of the Board

J Fleurant, *Director*

19 February 2019

Registered number 14259

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Risk

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Our risk appetite

Throughout its history HSBC has maintained a risk profile that has developed in line with its strategy and business objectives.

The following principles guide the group's overarching risk appetite and determine how its businesses and risks are managed:

Financial position

- Strong capital position, defined by regulatory and internal ratios.
- Liquidity and funding management for each entity on a stand-alone basis.

Operating model

- Ambition to generate returns in line with our risk appetite and strong risk management capability.
- Ambition to deliver sustainable earnings and appropriate returns for shareholders.

Business practice

- Zero tolerance for knowingly engaging in any business, activity or association where foreseeable reputational risk or damage has not been considered and/or mitigated.
- No appetite for deliberately or knowingly causing detriment to consumers arising from our products and services or incurring a breach of the letter or spirit of regulatory requirements.
- No appetite for inappropriate market conduct by a member of staff or by any group business.

Enterprise-wide application

Our risk appetite encapsulates consideration of financial and non-financial risks and is expressed in both quantitative and qualitative terms. It is applied at the global business level, at the country level and to material European entities.

Top and emerging risks

Top and emerging risks are those that may impact on the financial results, reputation or business model of the bank. If these risks were to occur, they could have a material effect on the group. The exposure to these risks and our risk management approach are explained in more detail below.

Externally driven

Process of UK withdrawal from the European Union

Uncertainty regarding the terms of the UK's exit agreement and its future relationship (including trading) with both the EU and the rest of the world is expected to continue for the next few years at least. Market volatility will therefore persist as the UK continues its negotiations with the EU and its potential future trading partners around the world. Throughout this period, we will continually update our assessment of potential consequences for our customers, products and banking model and re-evaluate our mitigating actions accordingly.

The scale and nature of the impact on HSBC will depend on the precise terms on which HSBC and its customers will be able to conduct cross-border business following the UK's departure from the EU. Changes to the UK's current trade relationships could require changes to HSBC's banking model to ensure we continue to comply with law and regulation in meeting the needs of our customers and conducting our business. Such changes could, among other things, increase our operating costs and require us to relocate staff and businesses to other jurisdictions. In addition, any negative impact on the economy, demand for borrowing and capital flows as a result of the aforementioned uncertainty, volatility or result of UK negotiations could have a consequential negative impact on HSBC.

Mitigating actions

- We have undertaken a comprehensive impact assessment to understand the range of potential implications for our customers, our products and our business. We have identified actions to ensure we can continue to serve our customers across the UK and Europe, and have started implementing them.
- We actively monitor our portfolio to identify areas of stress, supported by stress testing analyses. Vulnerable sectors will be subject to management review to determine if any adjustments to risk policy or appetite are required. As part of our stress testing programme, in addition to the Bank of England regulatory stress test which incorporated assumptions of a UK departure from the EU without a Withdrawal Agreement, we have conducted additional specific stress tests incorporating a number of internal macroeconomic and event-driven scenarios to assess a range of risks and provide management with a wider view of possible scenarios and outcomes from the UK's EU departure.
- We will continue to work with regulators, governments and our clients in an effort to manage risks as they arise, particularly across the most impacted sectors.

We believe we are well placed to withstand these risks, but would nevertheless be affected by severe shocks. For further details, see 'Areas of special interest' section.

Geopolitical risk

Our operations and portfolios are exposed to risks associated with political instability, civil unrest and military conflict which could lead to disruption to our operations, physical risk to our staff and/or physical damage to our assets. In addition rising protectionism and the increased trend of using trade and investment policies as diplomatic tools may also adversely affect global trade flows. Geopolitical risk remained heightened throughout 2018.

The growing presence of populist parties means political systems across Europe are increasingly fragmented, volatile and less predictable. Political uncertainty remains high in the UK as its departure from the EU continues to dominate the political agenda. The persistent threat of terrorist attacks remains.

Mitigating actions

- We continually monitor the geopolitical outlook, in particular in countries where we have material exposures and/or a physical presence.
- We use internal stress tests and scenario analysis as well as regulatory stress test programmes, to adjust limits and exposures to reflect our risk appetite and mitigate risks as appropriate.
- We have taken steps to enhance physical security in those countries deemed to be at high risk from terrorism.

Cyber threat and unauthorised access to systems

HSBC and other public and private organisations continue to be the targets of increasingly sophisticated cyber attacks. Ransomware and distributed denial of service attacks appear to be an increasingly dominant threat to the financial industry, which may result in disruption to our operations and customer-facing websites, financial loss or loss of customer data.

Mitigating actions

- We continue to strengthen our capabilities to protect against increasingly sophisticated malware, denial of service attacks and loss of data, as well as enhancing our security event detection and incident response processes. As well as technological improvement there is an increasing awareness of the cyber threat within our business, supported by formal training and the implementation of a number of specific cyber related working groups leading to an improving control environment around the end user and third party environment.
- Cyber risk is a top priority of the Board and is regularly reported to ensure appropriate visibility, governance and executive support for our ongoing cybersecurity programme.
- We participate in intelligence sharing with both law enforcement and industry schemes to help improve our understanding of, and ability to respond to, the evolving threats faced by us and our peers.

Regulatory focus on conduct of business

Financial institutions remain under considerable scrutiny regarding conduct of business, particularly in relation to fair outcomes for customers and orderly and transparent operations in financial markets. Regulators, prosecutors, the media and the public all have heightened expectations as to the behaviour and conduct of financial institutions, and any shortcomings or failure to demonstrate adequate controls are in place to mitigate such risks could result in regulatory sanctions, fines or an increase in civil litigation.

In September 2017, HBSC Holdings and HSBC North America Holdings Inc. ('HNAH') consented to a civil money penalty order with the US Federal Reserve Board ('FRB') in connection with its investigation into HSBC's historical foreign exchange activities. Under the terms of the order, HSBC Holdings and HNAH agreed to undertake certain remedial steps and to pay a civil money penalty to the FRB. In January 2018, HSBC Holdings entered into a three-year deferred prosecution agreement with the Criminal Division of the US Department of Justice ('DoJ') relating to HSBC's historical foreign exchange sales and trading activities. Under the terms of the deferred prosecution agreement, HSBC agreed to undertake certain remedial steps; to provide annual reports to the DoJ and to pay a financial penalty and restitution. For further details, see Note 32 of the Financial Statements.

Mitigating actions

- We have continued to enhance our management of conduct in areas including the treatment of potentially vulnerable customers, market surveillance, employee training and performance management (see 'Regulatory compliance risk management' on page 31.

Financial crime compliance

Financial institutions remain under considerable regulatory scrutiny regarding their ability to prevent and detect financial crime. Financial crime threats continue to evolve, often in tandem with geopolitical developments. The highly speculative, volatile and opaque nature of virtual currencies as well as the pace of new currencies and associated technological developments creates challenges in effectively managing financial crime risks. The evolving regulatory environment continues to present execution challenge. An increasing trend towards greater data privacy requirements may affect our ability to effectively manage financial crime risks.

In December 2012, among other agreements, HSBC Holdings plc ('HSBC Holdings') consented to a cease-and-desist order with the US Federal Reserve Board ('FRB') and agreed to an undertaking with the UK Financial Conduct Authority ('FCA') to comply with certain forward-looking AML and sanctions-related obligations. HSBC Holdings also agreed to retain an independent compliance monitor - who is for FCA purposes a 'Skilled Person' under section 166 of the Financial Services and Markets Act, and for FRB purposes an 'Independent Consultant - to produce annual assessments of the Group's AML and sanctions compliance programme. HSBC Holdings entered into an agreement with the Office of Foreign Assets Control ('OFAC') regarding historical transactions involving parties subject to OFAC sanctions. The Skilled Person/Independent Consultant will continue to conduct country reviews and provide periodic reports for a period of time at the FCA's and FRB's discretion. The role of the Skilled Person/ Independent Consultant is discussed on page 33.

Mitigating actions

- HSBC continues to enhance financial crime risk management capabilities; investing in the next generation of tools to fight financial crime by applying advanced analytics and artificial intelligence.
- HSBC are developing procedures and controls to manage the risks associated with direct and indirect exposure to virtual currencies.
- HSBC continues to work with jurisdictions and relevant bodies to address data privacy challenges through international standards, guidance and legislation to enable effective management of financial crime risk.
- We continue to ensure that the reforms we have put in place are both effective and sustainable over the long term.

Market illiquidity and volatility

Market liquidity, as defined by the ability to trade the desired volume of a financial security in a timely manner, continues to be sporadic. Liquidity remains challenging due to multiple factors: regulatory demands such as increased capital requirements constraining the overall balance sheet size of financial institutions, the implementation of the Volcker rule, which prohibits certain trading activities, and the impact of revised collateral requirements.

This is a market-wide issue, where HSBC may suffer losses or incur lower revenue.

Mitigating actions

- We continually monitor our illiquid positions and concentration risks, adjusting our market risk limits and risk appetite where appropriate.

IBOR transition

Interbank Offered Rates ('IBORs') including LIBOR (London Interbank Offered Rate) are used to set interest rates on hundreds of trillions of US dollars' worth of different types of financial transactions and are used extensively for valuation purposes, risk measurement and performance benchmarking.

Following the recommendations of the Financial Stability Board, a fundamental review and reform of the major interest rates benchmarks, including IBORs, are underway across the world's largest financial markets. In some cases, the reform will include replacing interest rate benchmarks with alternative Risk Free Rates ('RFRs'). This replacement process is at different stages, and is progressing at different speeds, across several major currencies.

There is therefore uncertainty as to the basis, method and timing of transition and their implications on the participants in the financial markets.

HSBC has identified a number of potential prudential, conduct and systemic risks associated with the transition.

Mitigating actions

- The Group has established a Global Programme across all of our Global Businesses to coordinate HSBC's transition activities and to assess the potential risks and impacts of any transition.
- The Group will continue to engage with industry participants and the official sector to support an orderly transition.
- We will continue to contribute to the ongoing Global Programme work to determine the volume and value of customer exposures potentially impacted by the transition from IBORs.

Internally driven

People risk

Our people are critical to our success and it is important that we identify, manage and mitigate any risks that might have an impact on our people feeling empowered and able to thrive in their careers, as well as being able to support our customers and the communities they serve. We aim to foster a culture that proactively promotes the right colleague behaviours and conduct, and that we have the right number of people with the right skills, knowledge and capabilities to be able to do the right thing for our customers. We have processes in place to identify where this might not be the case and to mitigate the risk accordingly.

We continually assess the impact of geopolitical events on our businesses and exposures. Some events, such as the UK's exit from the EU, result in increased people risks to be assessed in the UK and across a number of European sites, and for steps to be taken to mitigate such risks, where required.

Our success in delivering the Group's strategic priorities, as well as proactively managing the regulatory environment, depends on the continuous development and retention of our leadership and high performing employees. The ability to continue to attract, train, motivate and retain highly qualified professionals in an employment market where expertise is often mobile and in short supply is critical, particularly as our business lines execute their strategic business outlooks.

Mitigating actions

- We have plans in place to manage the potential impacts resulting from the UK exit from the EU.
- HSBC University is focused on developing opportunities and tools for now, next and future skills, personal skills to 'learn, adapt and evolve' and leaders to create an environment for success.
- HSBC is building the healthiest human system where colleagues can thrive. A number of initiatives to improve our 'Ways of Working' (e.g. simplifying processes and governance, adopting new behaviours) and encourage an open and positive culture have been launched. We also promote a diverse and inclusive workforce and provide active support across a wide range of health and wellbeing activities.

IT systems infrastructure and resilience

HSBC continues to invest in the reliability and resilience of the group's IT systems and crucial services, which could result in reputational and regulatory damage.

Mitigating actions

- Strategic initiatives are transforming how technology is developed, delivered and maintained, with a particular focus on providing high quality, stable and secure services. As part of this, we are concentrating on materially improving system resilience and service continuity testing. In addition we have enhanced the security of our development lifecycle and improved our testing processes and tools.
- During 2018, we continued to monitor and upgrade our IT systems, simplifying our service provision and replacing older IT infrastructure and applications.

Execution risk

In order to deliver our strategic objectives and meet mandatory regulatory requirements, it is important for HSBC to maintain a strong focus on execution risk. This requires robust management of significant resource-intensive and time-sensitive programmes. Risks arising from the magnitude and complexity of change may include regulatory censure, reputational damage or financial losses. Current major initiatives include managing the operational implications of updating our business model following the UK's vote to leave the EU.

Mitigating actions

- Our prioritisation and governance processes for significant projects are monitored by the group's Executive Committee.
- In 2018, we continued to manage execution risks through closely monitoring the punctual delivery of critical initiatives, internal and external dependencies, and key risks, to allow better portfolio management across the group.

Model risk

We use models for a range of purposes in managing our business, including regulatory capital calculations, stress testing, credit approvals, financial crime risk management and financial reporting. Evolving regulatory requirements have had a significant impact on our approach to model risk management, which poses execution challenges. The adoption of more sophisticated modelling approaches and technology across the industry could also lead to increased model risk.

Mitigating actions

- We established a model risk management sub-function in the second line of defence to strengthen governance and oversight of this risk type.
- We enhanced our model risk governance framework while partnering with the business in order to enable more effective management of model risk in a commercial context. As we adopt new modelling technologies, we are updating our model risk management framework and governance standards to help drive the evolution of the overall governance framework to ensure best practice.

Data management

The group currently uses a large number of systems and applications to support key business processes and operations. As a result, we often need to reconcile multiple data sources to reduce the risk of error. HSBC, along with other organisations, also needs to respond to the increasing external and regulatory expectations regarding data privacy and protection capabilities across our customer data systems.

Mitigating actions

- We continue to improve data quality across a large number of systems globally. Our data management, aggregation and oversight continues to strengthen and enhance the effectiveness of internal systems and processes. We are implementing data controls for critical processes in the 'front-office' systems to improve our data capture at the point of entry. HSBC has achieved its objective of meeting a "largely compliant" rating in support of the Basel Committee for Banking Supervision (BCBS 239) principles.
- Through the Group's Global Data Management Framework, we have embedded governance processes to proactively monitor the quality of critical customer, product and transaction data and resolving associated data issues in a timely manner. We have also implemented data controls in order to improve the reliability of data used by our customers and staff.
- To address global data privacy and protection regulations, HSBC is leveraging outcomes from the Global Data Protection Regulations (GDPR) initiative to roll-out and implement a global

- and consistent data privacy framework, while tailoring it to address any country specific regulations where required.
- We have also initiated efforts to modernize our data architecture and infrastructure through adoption of big data, cloud, machine learning, advanced analytics and visualization technologies.

Areas of special interest

Process of UK withdrawal from the European Union

The UK is due to formally leave the EU on 29 March 2019. The UK's withdrawal from the EU may adversely affect our operating model and financial results. Before 29 March, the UK and the EU are seeking to finalise the Article 50 Withdrawal Agreement, which will need to be approved by their respective parliaments. A comprehensive trade deal will not be concluded within this time frame. A period of transition until 31 December 2020 has been agreed between the UK and the EU. However, there will be no legal certainty until this is enshrined in the Withdrawal Agreement.

The modalities of the UK's exit from the European Union will likely to have a significant impact on general economic conditions in the UK and the European Union. The UK's future relationship with the EU and its trading relationships with the rest of the world will likely take a number of years to resolve. This may result in a prolonged period of uncertainty, unstable economic conditions and market volatility, including currency fluctuations. Throughout this period of uncertainty, our priority is to support our clients and continue to service them, independent of the outcome of negotiations.

To ensure continuity of service, independent of the outcome of negotiations, our robust contingency plan is based on a scenario whereby the UK leaves the EU without the existing passporting or regulatory equivalence framework that supports cross-border business. HSBC's programme to manage the impact of the UK leaving the EU was set up in 2017 and now has in excess of 1,000 employees covering all businesses and functions. It focuses on four main components: legal entity restructuring, platform build, clients and employees.

Legal entity restructuring

On 1 January 2018, the activities of HSBC Bank plc's branch in Greece were transferred to a new branch of HSBC France ('HBFR') in Greece.

On 1 August 2018, the group transferred two wholly owned subsidiaries, HSBC Bank Polska S.A. and HSBC Institutional Trust Services (Ireland) DAC to its subsidiary, HBFR.

The group currently has branches in seven European Economic Area ('EEA') countries (Belgium, the Netherlands, Luxembourg, Spain, Italy, Ireland and Czech Republic) which rely on passporting out of the UK. Following regulatory approval in 2018, and on the assumption that the UK leaves the EU without the existing passporting or regulatory equivalence framework that supports cross-border business, the branch network is in the process of transferring to HBFR, as HSBC's primary banking entity authorised in the EU.

The transfer of branches is happening in several steps:

- establishment of new branches of HBFR
- business transfer to the newly established branches
- de-registration of the group's branches.

We are on track to complete the business transfer in the first quarter of 2019 and good progress is being made on the operational integration with HBFR of its branches in Belgium, Czech Republic, Luxembourg, the Netherlands, Ireland, Italy and Spain.

Platform build

To accommodate customer migrations and new business after the UK's EU departure, we are expanding and enhancing our product offering and building new capabilities across Europe, where we already have a strong foundation, with a focus on France, the Netherlands and Ireland. Euro clearing capabilities are now available in HBFR and further product launches are planned during the first quarter of 2019.

Potential outcomes arising from the UK's departure from the EU will impact our clients and our employees. Our focus is on mitigating this impact and providing support and guidance throughout the withdrawal process.

Clients

The UK's departure from the EU is likely to have an impact on our clients' operating models including their working capital requirements, investment decisions and financial markets infrastructure access. Our priority is to provide our clients continuity of service and our intention is to minimise the level of change for our customers. However, some of our EEA-incorporated customers will no longer be able to be serviced out of the UK under the scenario planned for and will need to be migrated from the UK to HBFR (or another EEA entity). Relationship Managers are in active dialogue with affected clients and are working with them on an appropriate migration plan, including the timely execution of legal documentation. To provide clients with a better understanding of these implications, we are organising client events and communications.

Employees

The migration of EEA-incorporated clients will require us to strengthen our local teams in Continental Europe, and France in particular. We expect the majority of roles to be filled through hires and we have started a recruitment process. Throughout, our objective is to minimise the level of change for our people and to ensure any transition is as smooth as possible.

Given the scale and capabilities of our existing business in France, which already has more than 8,000 employees, a strong balance sheet and extensive product capabilities, we are well prepared to handle the transfer of activities.

Beyond the transfer of roles to Continental Europe, we are also providing support to our UK employees resident in EEA countries and EEA employees resident in the UK, for example on settlement applications.

Nevertheless, London will continue to be an important global financial centre and the best location for our global headquarters. At 31 December 2018, HSBC employed approximately 39,000 people in the UK.

Across the programme, we have made good progress in terms of ensuring we are prepared for the UK leaving the EU in the first quarter of 2019 under the terms described above, but there remain execution risks, many of them linked to the uncertain outcome of negotiations and potentially tight timelines to implement significant changes to our UK and European operating models.

If these risks materialise, HSBC's clients and employees are likely to be affected. The exact impact on our clients will depend on their individual circumstances and, in a worst case scenario, could include disruption to the provision of products and services.

We have carried out detailed reviews of our credit portfolios to determine those sectors and customers most vulnerable to the UK's exit from the EU. For further details please see 'Impact of UK economic uncertainty on ECL' on page 44.

Risk management

As a provider of banking and financial services, the group actively manages risk as a core part of its day-to-day activities. It continues to maintain a strong liquidity position and is well positioned for the evolving regulatory landscape.

Our risk management framework

An established risk governance framework and ownership structure ensures oversight of, and accountability for, the effective management of risk. The group's risk management framework fosters the continuous monitoring of the risk environment and an

integrated evaluation of risks and their interactions. Integral to the group's risk management framework are risk appetite, stress testing and the identification of emerging risks.

The bank's Risk Committee focuses on risk governance and provides a forward-looking view of risks and their mitigation. The Risk Committee is a committee of the Board and has responsibility for oversight and advice to the Board on, *inter alia*, the bank's risk appetite, tolerance and strategy, systems of risk management, internal control and compliance. Additionally, members of the Risk Committee attend meetings of the Chairman's Nominations and Remuneration Committee at which the alignment of the reward structures to risk appetite is considered.

In carrying out its responsibilities, the Risk Committee is closely supported by the Chief Risk Officer, the Chief Financial Officer, the Head of Internal Audit and the Heads of Compliance, together with other business functions on risks within their respective areas of responsibility.

Three lines of defence

To create a robust control environment to manage risks, we use an activity-based three lines of defence model, whereby the activity a member of staff undertakes drives which line they reside within. This model delineates management accountabilities and responsibilities for risk management and the control environment.

The model underpins our approach to risk management by clarifying responsibility, encouraging collaboration and enabling efficient coordination of risk and control activities. The three lines are summarised below:

- The first line of defence owns the risks and is responsible for identifying, recording, reporting and managing them, and ensuring that the right controls and assessments are in place to mitigate them.
- The second line of defence sets the policy and guidelines for managing specific risk areas, provides advice and guidance in relation to the risk, and challenges the first line of defence on effective risk management.
- The third line of defence is our Internal Audit function, which provides independent and objective assurance of the adequacy of the design and operational effectiveness of the group's risk management framework and control governance process.

Our risk culture

Risk culture refers to HSBC's norms, attitudes and behaviours related to risk awareness, risk taking and risk management.

HSBC has long recognised the importance of a strong risk culture, the fostering of which is a key responsibility of senior executives. Our risk culture is reinforced by the HSBC Values and our Global Standards programme. It is instrumental in aligning the behaviours of individuals with our attitude to assuming and managing risk, which helps to ensure that our risk profile remains in line with our risk appetite.

We use clear and consistent employee communication on risk to convey strategic messages and set the tone from senior management and the Board. We also deploy mandatory training on risk and compliance topics to embed skills and understanding in order to strengthen our risk culture and reinforce the attitude to risk in the behaviour expected of employees, as described in our risk policies.

The risk culture is reinforced by HSBC Group's approach to remuneration. Individual awards, including those for senior executives, are based on compliance with the HSBC Values and the achievement of both financial and non-financial objectives, that are aligned to our risk appetite and global strategy.

Whistleblowing

We operate a global whistleblowing standard, HSBC Confidential, allowing staff to report matters of concern confidentially. We also maintain an external email address for concerns about accounting and internal financial controls or auditing matters (accountingdisclosures@hsbc.com).

For further details, see page 6 of the How we do Business section.

Risk appetite

The group's Risk Appetite Statement describes the types and levels of risk that the group is prepared to accept in executing its strategy. Quantitative and qualitative metrics are assigned to 14 key categories, including: earnings, capital (including leverage measures), liquidity and funding, interest rate risk in the banking book, credit risk, traded risk, operational risk, model risk and regulatory compliance.

Measurement against the metrics:

- guides underlying business activity;
- informs risk-adjusted remuneration;
- enables the key underlying assumptions to be monitored and, where necessary, adjusted through subsequent business planning cycles; and
- promptly identifies business decisions needed to mitigate risk.

The Risk Appetite Statement is approved by the Board following advice from the Risk Committee. It is part of the annual planning process, in which global businesses, geographical regions and functions are required to articulate their individual risk appetite statements. These are aligned with the group strategy, and provide a risk profile of each global business, region or function in the context of the individual risk categories.

Stress testing

Stress testing is an important tool for banks and regulators to assess vulnerabilities in individual banks and/or the financial banking sector under hypothetical adverse scenarios. The results of stress testing are used to assess banks' resilience to a range of adverse shocks and to assess their capital adequacy.

HSBC Bank plc is subject to regulatory stress testing in several jurisdictions. These requirements are increasing in frequency and granularity. They include the programmes of the Bank of England ('BoE'), Prudential Regulation Authority ('PRA') and the European Banking Authority ('EBA'). Assessment by regulators is on both a quantitative and qualitative basis, the latter focusing on our portfolio quality, data provision, stress testing capability and capital planning processes.

A number of internal macroeconomic and event-driven scenarios specific to the European region were considered and reported to senior management during the course of the year, focusing in particular on the ramifications of various potential scenarios relating to the UK exit from the EU, before and after the successful completion of the ring-fencing of HSBC UK at 1 July 2018. We have worked closely with Group Stress Testing and France to ensure that the impact of the various planned transfers of branches and customers to France, as part of our preparation for the UK's exit from the EU, can be appropriately reflected and modelled in our internal and regulatory stress testing exercises. The group also conducts Reverse Stress Testing. This exercise requires a firm to assess scenarios and circumstances that would render its business model unviable, thereby identifying potential business vulnerabilities.

In 2018, the Group participated in the successful completion of the annual BoE concurrent stress testing exercise. The Annual Cyclical Scenario was materially unchanged from 2017, incorporating a synchronised global downturn affecting Asia and the UK in particular. Financial markets come under severe stress with a reduction in global risk appetite and reductions in market liquidity. The UK experiences a slowdown driven by the downturn in its trading partners, fall in confidence, and a sharp sterling depreciation leading to inflationary pressure on imports. In response monetary policy tightening leads to a steep rise in market and lending interest rates in the UK while global yield curves remain flat.

The BoE published the results of the 2018 Concurrent Stress Test in December 2018, confirming that these tests did not reveal any capital inadequacies for the HSBC Group. At the European level, the results of the EBA 2018 exercise were published in November 2018 and likewise demonstrated HSBC's continuing capital strength.

Our material banking and insurance risks

The material risk types associated with our banking and insurance manufacturing operations are described in the following tables.

Description of risks – banking operations

Risks	Arising from	Measurement, monitoring and management of risk
Credit risk (see page 26) The risk of financial loss if a customer or counterparty fails to meet an obligation under a contract.	Credit risk arises principally from direct lending, trade finance and leasing business, but also from certain other products such as guarantees and derivatives.	Credit risk is: • measured as the amount that could be lost if a customer or counterparty fails to make repayments; • monitored using various internal risk management measures and within limits approved by individuals within a framework of delegated authorities; and • managed through a robust risk control framework that outlines clear and consistent policies, principles and guidance for risk managers.
Liquidity and funding risk (see page 28) The risk that we do not have sufficient financial resources to meet our obligations as they fall due or that we can only do so at an excessive cost. Funding Risk is the risk that funding considered to be sustainable, and therefore used to fund assets, is not sustainable over time.	Liquidity risk arises from mismatches in the timing of cash flows. Funding risk arises when illiquid asset positions cannot be funded at the expected terms and when required.	Liquidity and funding risk is: • measured using a range of different metrics including the liquidity coverage ratio and net stable funding ratio; • assessed through the internal liquidity adequacy assessment process ('ILAAP'); • monitored against the group's liquidity and funding risk framework; and • managed on a stand-alone basis with no reliance on any group entity (unless pre-committed) or central bank unless this represents routine established business-as-usual market practice.
Market risk (see page 28) The risk that movements in market factors such as foreign exchange rates, interest rates, credit spreads, equity prices and commodity prices will reduce our income or the value of our portfolios.	Exposure to market risk is separated into two portfolios: • trading portfolios; and • non-trading portfolios. Market risk exposures arising from our insurance operations are discussed on page 65.	Market risk is: • measured using sensitivities, value at risk ('VaR') and stress testing, giving a detailed picture of potential gains and losses for a range of market movements and scenarios, as well as tail risks over specified time horizons; • monitored using VaR, stress testing and other measures, including the sensitivity of net interest income and the sensitivity of structural foreign exchange; and • managed using risk limits approved by the risk management meeting ('RMM') and the RMM in various global businesses.
Operational risk (see page 31) The risk to achieving our strategy or objectives as a result of inadequate or failed internal processes, people and systems or from external events.	Operational risk arises from day-to-day operations or external events, and is relevant to every aspect of our business. Regulatory compliance risk and financial crime compliance risk are discussed below.	Operational risk is: • measured using the risk and control assessment process, which assesses the level of risk and effectiveness of controls, and is also measured for economic capital management using risk event losses and scenario analysis; • monitored using key indicators and other internal control activities; and • managed primarily by global business and functional managers that identify and assess risks, implement controls to manage them and monitor the effectiveness of these controls utilising the operational risk management framework.
Regulatory compliance risk (see page 31) The risk that we fail to observe the letter and spirit of all relevant laws, codes, rules, regulations and standards of good market practice, and incur fines and penalties and suffer damage to our business as a consequence.	Regulatory compliance risk is part of operational risk, and arises from the risks associated with breaching our duty to customers and other counterparties, inappropriate market conduct and breaching other regulatory standards.	Regulatory compliance risk is: • measured by reference to identified metrics, incident assessments, regulatory feedback and the judgement and assessment of our Regulatory Compliance teams; • monitored against the first line of defence risk and control assessments, the results of the monitoring and control activities of the second line of defence functions, and the results of internal and external audits and regulatory inspections; and • managed by establishing and communicating appropriate policies and procedures, training employees in them, and monitoring activity to assure their observance. Proactive risk control and/or remediation work is undertaken where required.
Financial crime compliance risk (see page 32) The risk that we knowingly or unknowingly help parties to commit or to further potentially illegal activity through the group.	Financial crime compliance risk is part of operational risk and arises from day-to-day banking operations.	Financial crime compliance risk is: • measured by reference to identified metrics, incident assessments, regulatory feedback and the judgement and assessment of our Financial Crime Compliance teams; • monitored against our financial crime compliance risk appetite statement and metrics, the results of the monitoring and control activities of the second line of defence functions, and the results of internal and external audits and regulatory inspections; and • managed by establishing and communicating appropriate policies and procedures, training employees in them, and monitoring activity to ensure their observance. Proactive risk control and/or remediation work is undertaken where required.

Other material risk

Risks	Arising from	Measurement, monitoring and management of risk
Reputational risk (see page 34)		
The risk of failure to meet stakeholder expectations as a result of any event, behaviour, action or inaction, either by the group itself, our employees or those with whom we are associated.	Primary reputational risks arise directly from an action or inaction by HSBC, its employees or associated parties that are not the consequence of another type of risk. Secondary reputational risks are those arising indirectly and are a result of a failure to control any other risks.	Reputational risk is: • measured by reference to our reputation as indicated by our dealings with all relevant stakeholders, including media, regulators, customers and employees; • monitored through a reputational risk management framework that is integrated into the group's broader risk management framework; and • managed by every member of staff, and covered by a number of policies and guidelines. There is a clear structure of committees and individuals charged with mitigating reputational risk.
Pension risk (see page 34)		
The risk of increased costs to the group from offering post-employment benefit plans to its employees.	Pension risk arises from investments delivering an inadequate return, adverse changes in interest rates or inflation, or members living longer than expected. Pension risk also includes the operational and reputational risk of sponsoring pension plans.	Pension risk is: • measured in terms of the schemes' ability to generate sufficient funds to meet the cost of their accrued benefits; • monitored through the specific risk appetite that has been developed at HSBC Group and Regional levels; and • managed locally through the Pensions Oversight Forum and ultimately through the RMM.

Our insurance manufacturing subsidiaries are regulated separately from our banking operations. Risks in our insurance entities are managed using methodologies and processes that are subject to Group oversight. Our insurance operations are also subject to some of the same risks as our banking operations, which are covered by the group's risk management processes.

Description of risks – insurance manufacturing operations

Risks	Arising from	Measurement, monitoring and management of risk
Financial risk (see page 65)		
Our ability to effectively match liabilities arising under insurance contracts with the asset portfolios that back them is contingent on the management of financial risks and the extent to which these are borne by policyholders.	Exposure to financial risks arises from: • market risk affecting the fair values of financial assets or their future cash flows; • credit risk; and • liquidity risk of entities not being able to make payments to policyholders as they fall due.	Financial risk is: • measured (i) for credit risk, in terms of economic capital and the amount that could be lost if a counterparty fails to make repayments; (ii) for market risk, in terms of economic capital, internal metrics and fluctuations in key financial variables; and (iii) for liquidity risk, in terms of internal metrics, including stressed operational cash flow projections; • monitored through a framework of approved limits and delegated authorities; and • managed through a robust risk control framework that outlines clear and consistent policies, principles and guidance. This includes using product design and asset liability matching and bonus rates.
Insurance risk (see page 68)		
The risk that, over time, the cost of the contract, including claims and benefits may exceed the total amount of premiums and investment income received.	The cost of claims and benefits can be influenced by many factors, including mortality and morbidity experience, as well as lapse and surrender rates.	Insurance risk is: • measured in terms of life insurance liabilities and economic capital allocated to insurance underwriting risk; • monitored though a framework of approved limits and delegated authorities; and • managed through a robust risk control framework that outlines clear and consistent policies, principles and guidance. This includes using product design, underwriting, reinsurance and claims-handling procedures.

Credit risk management

(Audited)

Of the risks in which we engage, credit risk generates the largest regulatory capital requirements.

The principal objectives of our credit risk management are:

- to maintain across the group a strong culture of responsible lending and a robust risk policy and control framework;
- to both partner and challenge Global Businesses in defining, implementing and continually re-evaluating our risk appetite under actual and scenario conditions; and
- to ensure there is independent, expert scrutiny of credit risks, their costs and mitigation.

Within the bank, the Credit Risk function is headed by the European Chief Risk Officer who reports to the Chief Executive Officer, with a functional reporting line to HSBC Group Chief Risk Officer. Its responsibilities are:

- to formulate credit policy. Compliance, subject to approved dispensations, is mandatory for all operating companies which must develop local credit policies consistent with group policies that very closely reflect Group policy;
- to guide operating companies on the group's appetite for credit risk exposure to specified market sectors, activities and banking products and controlling exposures to certain higher-risk sectors;
- to undertake an independent review and objective assessment of risk. Credit risk assesses all credit facilities and exposures over designated limits, prior to the facilities being committed to customers or transactions being undertaken;
- to monitor the performance and management of portfolios across the group;
- to control exposure to sovereign entities, banks and other financial institutions, as well as debt securities which are not held solely for the purpose of trading;
- to set policy on large credit exposures, ensuring that concentrations of exposure by counterparty, sector or geography do not become excessive in relation to the group's capital base, and remain within internal and regulatory limits;

- to maintain and develop the risk rating framework and systems through Model Oversight Committees (MOCs). MOCs are in place to oversee risk rating governance for the wholesale and retail models that are used within the group;
- to report on retail portfolio performance, high risk portfolios, risk concentrations, large impaired accounts, impairment allowances and stress testing results and recommendations to the group's Risk Management Meeting, the group's Risk Committee and the Board; and
- to act on behalf of the group as the primary interface for credit-related issues, with the BoE, the PRA, local regulators, rating agencies, analysts and counterparts in major banks and non-bank financial institutions.

Concentration of credit risk exposure

(Audited)

Concentrations of credit risk arise when a number of counterparties or exposures have comparable economic characteristics, or are engaged in similar activities, or operate in the same geographical areas/industry sectors, so that their collective ability to meet contractual obligations is uniformly affected by changes in economic, political or other conditions. The group uses a number of controls and measures to minimise undue concentration of exposure in the group's portfolios across industry, country and customer groups. These include portfolio and counterparty limits, approval and review controls, and stress testing.

Wrong-way risk occurs when a counterparty's exposures are adversely correlated with its credit quality. There are two types of wrong-way risk:

- general wrong-way risk occurs when the probability of counterparty default is positively correlated with general risk factors such as where the counterparty is resident and/or incorporated in a higher-risk country and seeks to sell a non-domestic currency in exchange for its home currency; and
- specific wrong-way risk occurs in self-referencing transactions. These are transactions in which exposure is driven by capital or financing instruments issued by the counterparty and occurs where exposure from HSBC's perspective materially increases as the value of the counterparty's capital or financing instruments referenced in the contract decreases. It is HSBC policy that specific wrong-way risk transactions are approved on a case-by-case basis.

We use a range of procedures to monitor and control wrong-way risk, including requiring entities to obtain prior approval before undertaking wrong-way risk transactions outside pre-agreed guidelines.

Credit quality of financial instruments

(Audited)

Our credit risk rating systems and processes differentiate exposures in order to highlight those with greater risk factors and higher potential severity of loss. In the case of individually significant accounts, risk ratings are reviewed regularly and any amendments are implemented promptly. Within the group's retail business, risk is assessed and managed using a wide range of risk and pricing models to generate portfolio data.

Our risk rating system facilitates the internal ratings-based approach under the Basel framework adopted by HSBC Group to support calculation of the minimum credit regulatory capital requirement.

Special attention is paid to problem exposures in order to accelerate remedial action. Where appropriate, operating companies use specialist units to provide customers with support to help them avoid default returning to sound trading wherever possible.

The Credit Review and Risk Identification team reviews the robustness and effectiveness of key management, monitoring and control activities.

Risk rating scales

The Customer Risk Rating ('CRR') 10-grade scale summarises a more granular underlying 23-grade scale of obligor probability of default ('PD'). All distinct HSBC customers are rated using one of these two PD scales, depending on the degree of sophistication of the Basel II approach adopted for the exposure.

Each CRR band is associated with an external rating grade by reference to long-run default rates for that grade, represented by the average of issuer-weighted historical default rates. This mapping between internal and external ratings is an indication only and may vary over time.

The Expected Loss ('EL') 10-grade scale for retail business summarises a more granular underlying EL scale for these customer segments; this combines obligor and facility/product risk factors in a composite measure. For debt securities and certain other financial instruments, external ratings have been aligned to the five quality classifications based upon the mapping of related CRR to external credit grades.

For the purpose of the following disclosure, retail loans which are past due up to 89 days and are not otherwise classified as EL 9 or EL 10, are not disclosed within the EL grade to which they relate, but are separately classified as past due but not impaired. The following tables set out the group's distribution of financial instruments by measures of credit quality.

The five credit quality classifications defined each encompasses a range of granular internal credit rating grades assigned to wholesale and retail lending businesses and the external ratings attributed by external agencies to debt securities.

For debt securities and certain other financial instruments, external ratings have been aligned to the five quality classifications based upon the mapping of related CRR to external credit ratings. The mapping is reviewed on a regular basis and the most recent review resulted in sovereign BBB+ and BBB exposures previously mapped to Credit Quality band 'Good' being mapped to Credit Quality band 'Strong'. Sovereign BB+ and BB exposures previously mapped to Credit Quality band 'Satisfactory' were mapped to Credit Quality band 'Good'. This represents a change in disclosure mapping unrelated to changes in counterparty creditworthiness.

Credit quality classification

	Sovereign debt securities and bills	Other debt securities and bills	Wholesale lending and derivatives		Retail lending	
	External credit rating	External credit rating	Internal credit rating	12-month probability of default %	Internal credit rating	Expected loss %
Quality classification						
Strong	**BBB and above**	**A- and above**	**CRR1 to CRR2[1]**	**0 – 0.169**	**EL1 to EL2[2]**	**0 – 0.999**
Good	**BB to BBB-**	**BBB+ to BBB-**	**CRR3**	**0.170 – 0.740**	**EL3**	**1.000 – 4.999**
Satisfactory	**BB- to B and unrated**	**BB+ to B and unrated**	**CRR4 to CRR5**	**0.741 – 4.914**	**EL4 to EL5**	**5.000 – 19.999**
Sub–standard	**B- to C**	**B- to C**	**CRR6 to CRR8**	**4.915 – 99.999**	**EL6 to EL8**	**20.000 – 99.999**
Credit impaired	**Default**	**Default**	**CRR9 to CRR10**	**100**	**EL9 to EL10**	**100+ or defaulted[3]**

1 *Customer risk rating ('CRR').*
2 *Expected loss ('EL').*
3 *The EL percentage is derived through a combination of Probability of Default ('PD') and Loss Given Default ('LGD') and may exceed 100% in circumstances where the LGD is above 100% reflecting the cost of recoveries.*

Quality classification definitions

- 'Strong': Exposures demonstrate a strong capacity to meet financial commitments, with negligible or low probability of default and/or low levels of expected loss.
- 'Good': Exposures require closer monitoring and demonstrate a good capacity to meet financial commitments, with low default risk.
- 'Satisfactory': Exposures require closer monitoring and demonstrate an average to fair capacity to meet financial commitments, with moderate default risk.
- 'Sub-standard': Exposures require varying degrees of special attention and default risk is of greater concern.
- 'Credit-impaired': Exposures have been assessed as described in Note 1.2(i) in the Financial Statements.

Renegotiated loans and forbearance

A range of forbearance strategies are employed to improve the management of customer relationships, maximise collection opportunities and, if possible, avoid default, foreclosure or repossession. They include extended payment terms, a reduction in interest or principal repayments, approved external debt management plans, debt consolidations, the deferral of foreclosures and other forms of loan modifications and re-ageing.

The group's policies and practices are based on criteria which enable local management to judge whether repayment is likely to continue. These typically provide a customer with terms and conditions that are more favourable than those provided initially. Loan forbearance is only granted in situations where the customer has showed a willingness to repay their loan and is expected to be able to meet the revised obligations.

Refinance risk

Personal lending

Interest-only mortgages lending incorporate bullet payments at the point of final maturity. To reduce refinance risk, an initial on-boarding assessment of customers' affordability is made on a capital repayment basis and every customer has a credible defined repayment strategy. Additionally the customer is contacted at least once during the mortgage term to check the status of the repayment strategy. In situations where it is identified that a borrower is expected not to be able either to repay a bullet/balloon payment then the customer will either default on the repayment or it is likely that the bank may need to apply forbearance to the loan. In either circumstance this gives rise to a loss event and an impairment allowance will be considered where appropriate.

Wholesale lending

Many types of wholesale lending incorporate bullet/balloon payments at the point of final maturity; often, the intention or assumption is that the borrower will take out a new loan to settle the existing debt. Where this is true the term refinance risk refers generally to the possibility that, at the point that such a repayment is due, a borrower cannot refinance by borrowing to repay existing debt. In situations where it is identified that a borrower is expected not to be able either to repay a bullet/balloon payment or to be capable of refinancing their existing debt on commercial terms then the customer will either default on the repayment or it is likely that the bank may need to refinance the loan on terms it would not normally offer in the ordinary course of business. In either circumstance this gives rise to a loss event and an impairment allowance will be considered.

Impairment assessment

(Audited)

For details of our impairment policies on loans and advances and financial investments see Note 1.2(i) on the Financial Statements.

Write-off of loans and advances

(Audited)

For details of our accounting policy on the write-off of loans and advances, see Note 1.2(i) on the Financial Statements.

Personal lending

Property collateral for residential mortgages is repossessed and sold on behalf of the borrower only when all normal debt recovery procedures have been unsuccessful. Any portion of the balance not covered following the realisation of security is written-off.

Unsecured personal lending products are normally written off, when there is no realistic prospect of recovery, usually when they reached 180 days past due.

In case of some products, e.g. credit cards, it is common for accounts to be written off at the end of the month in which they fall six months past due. Examples of events which may result in early write-off include bankruptcy, deceased customers, fraud and facilities with small balances.

Wholesale lending

Wholesale loans and advances are written off where normal collection procedures have been unsuccessful to the extent that there appears no realistic prospect of repayment. These procedures may include a referral of the business relationship to a debt recovery company. Debt reorganisation will be considered at all times and may involve, in exceptional circumstances and in the absence of any viable alternative, a partial write-off in exchange for a commitment to repay the remaining balance.

In the event of bankruptcy or analogous proceedings, write-off for both personal and wholesale lending may occur earlier than at the periods stated above. Collections procedures may continue after write-off.

Liquidity and funding risk management

Details of HSBC's Liquidity and Funding Risk Management Framework ('LFRF') can be found in the group's Pillar 3 document.

HSBC requires all operating entities to comply with HSBC Group's LFRF on a stand–alone basis and to meet regulatory and internal minimum requirements at all times. The liquidity coverage ratio ('LCR') and net stable funding ratio ('NSFR') are key components of the LFRF.

The elements of the LFRF are underpinned by a robust governance framework, the two major elements of which are:

- Group, regional and entity level asset and liability management committees ('ALCOs'); and
- Annual individual liquidity adequacy assessment process ('ILAAP') used to validate risk tolerance and set risk appetite.

The Group's operating entities are predominantly defined on a country basis to reflect the local management of liquidity and funding. However, where appropriate, this definition may be expanded to cover a consolidated group of legal entities or narrowed to a principal office (branch) of a wider legal entity to reflect the management under internal or regulatory definitions.

The RMM reviews and agrees annually the list of entities it directly oversees and the composition of these entities.

Market risk management

Where appropriate, we apply similar risk management policies and measurement techniques to both trading and non-trading portfolios. Our objective is to manage and control market risk exposures to optimise return on risk while maintaining a market profile consistent with our status as one of the world's largest banking and financial services organisations.

The nature of the hedging and risk mitigation strategies performed across the group corresponds to the market risk management instruments available within each operating jurisdiction. These strategies range from the use of traditional market instruments, such as interest rate swaps, to more sophisticated hedging strategies to address a combination of risk factors arising at portfolio level.

Market risk governance

(Audited)

Market risk is managed and controlled through limits approved by the RMM of HSBC Group Management Board ('GMB') for HSBC Holdings and the global businesses. These limits are allocated across business lines and agreed with HSBC Group's legal entities, including HSBC Bank plc.

The management of market risk is principally undertaken in Markets using risk limits allocated from the risk appetite, which is subject to HSBC Bank plc RMM ratification. Limits are set for portfolios, products and risk types, with market liquidity being a primary factor in determining the level of limits set.

Global Risk is responsible for setting market risk management policies and measurement techniques. Each major operating entity has an independent market risk management and control function which is responsible for measuring market risk exposures in accordance with the policies defined by Global Risk, and monitoring and reporting these exposures against the prescribed limits on a daily basis.

Each operating entity is required to assess the market risks arising on each product in its business and to transfer them to either its local Markets unit for management, to Balance Sheet management books or to separate books managed under the supervision of the local ALCO.

The aim is to ensure that all market risks are consolidated within operations which have the necessary skills, tools, management and governance to manage them professionally. In certain cases where the market risks cannot be fully transferred, the group identifies the impact of varying scenarios on valuations or on net interest income resulting from any residual risk positions.

Model risk is governed through Model Oversight Committees ('MOCs') at the regional and global Wholesale Credit and Market Risk levels. They have direct oversight and approval responsibility for all traded risk models utilised for risk measurement and management and stress testing. The MOCs prioritise the development of models, methodologies and practices used for traded risk management within HSBC Group and ensure that they remain within our risk appetite and business plans. The Markets MOC reports into HSBC Group MOC, which oversees all model risk types at Group level. Group MOC informs HSBC Group RMM about material issues at least on a bi-annual basis. The RMM is HSBC Group's 'Designated Committee' according to regulatory rules and has delegated day-to-day governance of all traded risk models to the Markets MOC.

The control of market risk in the trading and non-trading portfolios is based on a policy restricting individual operations to trading within a list of permissible instruments authorised for each site by Global Risk, enforcing new product approval procedures, and restricting trading in the more complex derivative products only to offices with appropriate levels of product expertise and robust control systems.

Market risk measures

Monitoring and limiting market risk exposures

Our objective is to manage and control market risk exposures while maintaining a market profile consistent with the group's risk appetite.

We use a range of tools to monitor and limit market risk exposures including sensitivity analysis, value at risk ('VaR'), and stress testing.

Sensitivity analysis

Sensitivity analysis measures the impact of individual market factor movements on specific instruments or portfolios, including interest rates, foreign exchange rates, credit spreads and equity prices, such as the effect of a one basis point change in yield. We use sensitivity measures to monitor the market risk positions within each risk type. Sensitivity limits are set for portfolios, products and risk types, with the depth of the market being one of the principal factors in determining the level of limits set.

Value at risk

VaR is a technique that estimates the potential losses on risk positions as a result of movements in market rates and prices over a specified time horizon and to a given level of confidence. The use of VaR is integrated into market risk management and is calculated for all trading positions regardless of how the group capitalises those exposures. Where there is not an approved internal model, the group uses the appropriate local rules to capitalise exposures.

In addition, the group calculates VaR for non-trading portfolios in order to have a complete picture of risk. The models are predominantly based on historical simulation. VaR is calculated at a 99% confidence level for a one-day holding period. Where we do not calculate VaR explicitly, we use alternative tools as summarised in the Market Risk Stress testing section.

The VaR models used by us are based predominantly on historical simulation. These models derive plausible future scenarios from past series of recorded market rates and prices, taking into account inter-relationships between different markets and rates such as interest rates and foreign exchange rates. The models also incorporate the effect of option features on the underlying exposures.

The historical simulation models used incorporate the following features:

- historical market rates and prices are calculated with reference to foreign exchange rates and commodity prices, interest rates, equity prices and the associated volatilities;
- potential market movements utilised for VaR are calculated with reference to data from the past two years; and
- VaR measures are calculated to a 99% confidence level and use a one-day holding period.

The nature of the VaR models means that an increase in observed market volatility will most likely lead to an increase in VaR without any changes in the underlying positions.

VaR model limitations

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

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

Risk not in VaR framework

Other basis risks which are not completely covered in VaR, such as the Libor tenor basis, are complemented by our risk not in VaR ('RNIV') calculations, and are integrated into our capital framework.

Risk factors are reviewed on a regular basis and either incorporated directly in the VaR models, where possible, or quantified through the VaR-based RNIV approach or a stress test approach within the RNIV framework. The outcome of the VaR-based RNIV is included in the VaR calculation and back-testing; a stressed VaR RNIV is also computed for the risk factors considered in the VaR-based RNIV approach.

Stress-type RNIVs include a gap risk exposure measure to capture risk on non-recourse margin loans and a de-peg risk measure to capture risk to pegged and heavily managed currencies.

Stress testing

Stress testing is an important procedure that is integrated into our market risk management tool to evaluate the potential impact on portfolio values of more extreme, although plausible, events or movements in a set of financial variables. In such scenarios, losses can be much greater than those predicted by VaR modelling.

Stress testing is implemented at legal entity, regional and overall Group levels. A standard set of scenarios is utilised consistently across all regions within HSBC Group. Scenarios are tailored to capture the relevant events or market movements at each level. The risk appetite around potential stress losses for the group is set and monitored against referral limits.

Market risk reverse stress tests are undertaken on the premise that there is a fixed loss. The stress testing process identifies which scenarios lead to this loss. The rationale behind the reverse stress test is to understand scenarios which are beyond normal business settings that could have contagion and systemic implications.

Stressed VaR and stress testing, together with reverse stress testing and the management of gap risk, provide management with insights regarding the 'tail risk' beyond VaR for which the group's appetite is limited.

Trading portfolios

Back-testing

We routinely validate the accuracy of our VaR models by back-testing them against both actual and hypothetical profit and loss against the corresponding VaR numbers. Hypothetical profit and loss excludes non-modelled items such as fees, commissions and revenues of intra-day transactions.

We would expect on average to see two or three profits in excess of the VaR at 1% confidence level and two or three losses in excess of VaR at the 99% confidence level over a one-year period. The actual number of profits or losses in excess of VaR over this period can therefore be used to gauge how well the models are performing.

We back-test our VaR at various levels which reflect a full legal entity scope of HSBC, including entities that do not have local permission to use VaR for regulatory purposes.

Non-trading portfolios

Non-trading VaR of HSBC Bank plc includes the interest rate risk of non-trading financial instruments held by the global businesses and transferred into portfolios managed by BSM or ALCM functions. In measuring, monitoring and managing risk in our non-trading portfolios, VaR is just one of the tools used. The management of interest rate risk in the banking book is described further in 'Non-trading interest rate risk' below, including the role of BSM. The group's and HSBC Bank plc's control of market risk in the non-trading portfolios is based on transferring the assessed market risk of non-trading assets and liabilities created outside BSM or Markets, to the books managed by BSM, provided the market risk can be neutralised. The net exposure is typically managed by BSM through the use of fixed rate government bonds (liquid asset held in held-to-collect-and-sale (HTCS books)) and interest rate swaps. The interest rate risk arising from fixed rate government bonds held within HTCS portfolios is reflected within the group's non-traded VaR. Interest rate swaps used by BSM are typically classified as either a fair value hedge or a cash flow hedge and included within the group's non-traded VaR. Any market risk that cannot be neutralised in the market is managed by HSBC Bank plc ALCM in segregated ALCO books.

Structural foreign exchange exposure

Structural foreign exchange exposures represent the group's net investments in subsidiaries, branches and associates, the functional currencies of which are currencies other than sterling. An entity's functional currency is that of the primary economic environment in which the entity operates.

Unrealised gains or losses due to revaluations of structured foreign exchange exposures are recognised in other comprehensive income, whereas other unrealised gains or losses arising from revaluations of foreign exchange positions are reflected in the income statement.

The group's structural foreign exchange exposures are managed with the primary objective of ensuring, where practical, that the group's consolidated capital ratios and the capital ratios of individual banking subsidiaries are largely protected from the effect of changes in exchange rates. We hedge structural foreign exchange exposures only in limited circumstances.

Interest rate risk in the banking book

Overview

Interest Rate Risk in the Banking Book ('IRRBB') is the risk of an adverse impact to earnings or capital due to changes in market interest rates. IRRBB is generated by our non-traded assets and liabilities. The Asset, Liability and Capital Management ('ALCM') function is responsible for measuring and controlling IRRBB under the supervision of the RMM who approve risk limits used in the management of interest rate risk. IRRBB is transferred to and managed by BSM, who are overseen by Wholesale Market Risk and Product Control functions.

Key risk drivers

The bank's IRRBB can be segregated into the following drivers:

- Managed rate risk – the risk that the pricing of products, which are dependent upon business line decisions, do not correlate to movements in market interest rates.
- Re-investment risk – risk arising due to change in rates when behaviouralised balances are reinvested as per the transfer pricing policy.
- Basis risk – the risk arising from assets and liabilities that are priced referencing different market indices creating a repricing mismatch.
- Prepayment risk – the risk that the actual customer prepayment in different interest rate scenarios does not match the profile used to hedge the interest rate risk.
- Duration risk – the risk that there are changes in the maturities of assets and liabilities due to changes in interest rate, which create or exacerbate a mismatch.

Governance and structure

ALCM monitors and control non-traded interest rate risk as well as reviewing and challenging the business prior to the release of new products and proposed behavioural assumptions used for hedging activities. ALCM is also responsible for maintaining and updating the transfer pricing framework, informing ALCO of the group's overall banking book interest rate risk exposure and managing the balance sheet in conjunction with BSM.

The internal transfer pricing framework is constructed to ensure that structural interest rate risk, arising due to differences in the repricing timing of assets and liabilities, is transferred to BSM and business lines are correctly allocated income and expense based on the products they write, inclusive of activities to mitigate this risk. Contractual principal repayments, payment schedules, expected prepayments, contractual rate indices used for repricing and interest rate reset dates are examples of elements transferred for risk management by BSM.

The internal transfer pricing framework is governed by ALCO whose responsibility it is to define each operating entity's transfer pricing curve as well as to review and approve the transfer pricing policy, including behaviouralisation assumptions used for products where there is either no defined maturity or where customer optionality exists. ALCO is also responsible for monitoring and reviewing the overall structural interest rate risk position. Interest rate behaviouralisation policies have to be formulated in line with HSBC Group's behaviouralisation policies and approved at least annually by local ALCOs.

Non-traded assets and liabilities are transferred to BSM based on their repricing and maturity characteristics. For assets and liabilities with no defined maturity or repricing characteristics behaviouralisation is used to assess the interest rate risk profile.

BSM manages the banking book interest rate positions transferred to it within the Markets Risk limits approved by RMM. Effective governance across BSM is supported by the dual reporting lines it has to the Chief Executive Officer of GB&M and to the HSBC Group Treasurer. BSM will only receive non-trading assets and liabilities as long as they can economically hedge the risk they receive. Hedging is generally managed through vanilla interest rate derivatives or fixed rate government bonds. Any interest rate risk which BSM cannot economically hedge is not transferred and will remain within the business line where the risk is originated.

Measurement of interest rate risk in the banking book

The following measures are used by ALCM to monitor and control interest rate risk in the banking book including:

- non-traded VaR;
- net Interest Income ('NII') sensitivity; and
- economic value of equity ('EVE').

Non-traded VaR uses the same models as those used in the trading book but for banking book balances.

NII sensitivity reflects the group’s sensitivity of earnings to changes in market interest rates. Entities forecast both one year and five year NII sensitivities across a range of interest rate scenarios based on a static balance sheet assumption. Sites include business line rate pass-on assumptions, re-investment of maturing assets and liabilities at market rates per shock scenario and prepayment risk. BSM is modelled based on no management actions i.e. the risk profile at the month end is assumed to remain constant throughout the forecast horizon.

Net interest income sensitivity

A principal part of our management of non-traded interest rate risk is to monitor the sensitivity of expected NII under varying interest rate scenarios (simulation modelling), where all other economic variables are held constant. This monitoring is undertaken by ALCO.

The group applies a combination of scenarios and assumptions relevant to the businesses as well as applying standard scenarios that are required throughout HSBC Group.

Economic value of equity

EVE represents the present value of the future banking book cash flows that could be distributed to equity providers under a managed run-off scenario, i.e. the current book value of equity plus the present value of future net interest income in this scenario. EVE sensitivity is the extent to which the EVE value will change due to a pre-specified movement in interest rates, where all other economic variables are held constant.

Defined benefit pension scheme

Market risk also arises within the group’s defined benefit pension schemes to the extent that the obligations of the schemes are not fully matched by assets with determinable cash flows. Refer to Pension risk section on page 34 for additional information.

Operational risk management

Details of our operational risk profile in 2018 can be found on page 65, in ‘Operational risk in 2018’.

Overview

The objective of our operational risk management is to manage and control operational risk in a cost-effective manner within targeted levels of operational risk consistent with our risk appetite.

Key developments in 2018

During 2018 we continued to strengthen our approach to managing operational risk as set out in the operational risk management framework (‘ORMF’). The approach sets out governance, appetite and provides an end-to-end view of non-financial risks, enhancing focus on the risks that matter most and associated controls. It incorporates a risk management system to enable active risk management.

Activity to strengthen our risk culture and better embed the approach, particularly the three lines of defence model, continued to be a key focus in 2018. The framework sets out our roles and responsibilities for managing operational risk on a daily basis.

Data relating to HSBC UK Bank plc in the risk management system was separated from HSBC Bank plc in advance of the UK ring-fenced bank going live on 1 July 2018.

In accordance with preparations for the UK's withdrawal from the EU, a number of branches within the European Economic Area have been moved under HSBC France in the risk management system, replicating the proposed legal structure of the bank.

Further information on the three lines of defence model can be found in the ‘Our risk management framework’ section on page 23.

Governance and structure

The ORMF defines minimum standards and processes, and the governance structure for the management of operational risk and internal control. The ORMF has been codified in a high-level standards manual, supplemented with detailed policies, which describes our approach to identifying, assessing, monitoring and controlling operational risk and gives guidance on mitigating action to be taken when weaknesses are identified.

We have a dedicated Operational Risk sub-function within our Risk function. It is responsible for leading the embedding of the ORMF, and assuring adherence to associated policies and processes across the first and second lines of defence.

Operational Risk reviews the level of implementation of the ORMF and provides updates on progress to the RMM.

Key risk management processes

Business managers throughout HSBC Group are responsible for maintaining an acceptable level of internal control commensurate with the scale and nature of operations, and for identifying and assessing risks, designing controls and monitoring the effectiveness of these controls. The ORMF helps managers to fulfil these responsibilities by defining a standard risk assessment methodology and providing a tool for the systematic reporting of operational loss data.

A Group-wide risk management system is used to record the results of the operational risk management process. Operational risk and control self-assessments, along with issues and action plans, are entered and maintained by business units. Business and functional management monitor the progress of documented action plans to address shortcomings. To help ensure that operational risk losses are consistently reported and monitored at Group level, all Group companies are required to report individual losses when the net loss is expected to exceed $10,000, and to aggregate all other operational risk losses under $10,000. Losses are entered into the Group-wide risk management system and reported to governance on a monthly basis.

Continuity of business operations

The Operational Risk function undertakes business continuity management, which incorporates the development of a plan including a business impact analysis assessing risk when business disruption occurs.

The group maintains a number of dedicated work area recovery sites globally. Regular testing of these facilities is carried out with representation from each business and support function, to ensure business continuity plans remain accurate, relevant and fit for purpose. Where possible, the group has ensured that its critical business systems are not co-located with business system users, thereby reducing concentration risk.

Regulatory compliance risk management

Overview

The Regulatory Compliance sub-function (‘RC’) provides independent, objective oversight and challenge, and promotes a compliance-orientated culture that supports the business in

delivering fair outcomes for customers, maintaining the integrity of financial markets and achieving HSBC's strategic objectives.

Key developments in 2018

There were no material changes to the policies and practices for the management of RC risk in 2018, except for the following:

- The HBEU Board maintains oversight of conduct matters following the demise of the Conduct & Values Committee in 2018.
- We implemented a number of initiatives to raise our standards in relation to the conduct of our business, as described below under 'Conduct of business'.
- The reporting line of the Global Head of Regulatory Compliance was changed from reporting to the Group Chief Risk Officer to reporting to the Group Chief Compliance Officer from 1 November 2018.

Governance and structure

The Europe Head of RC reports into the Global head of RC. Regulatory Compliance and Financial Crime Risk were integrated into a new Compliance function from 1 November, which is headed by the Group Chief Compliance Officer. RC continues to be structured as a global sub function with regional and country RC teams, which support and advise each global business and global function.

Key risk management processes

We regularly review our policies and procedures. Global policies and procedures require the prompt identification and escalation of any actual or potential regulatory breach to RC. Reportable events are escalated to the bank's RMM and Risk Committee, as appropriate. Matters relating to the Group's regulatory conduct of business are reported to the Group Risk Committee.

Conduct of business

In 2018, we have continued to highlight conduct requirements, as a global principle and elsewhere within the risk management framework, reflecting the individual responsibility and accountability we have for delivery of good conduct outcomes for customers and market integrity. Other key activities in 2018 included:

- the inclusion of an annual conduct objective in performance management scorecards for executive Directors, Group Managing Directors, Group General Managers and Country CEOs across all regions, business lines, global functions and HSBC Operations Services and Technology. Executive Directors are also now subject to a new separate conduct-focused 'long term incentive' measure;
- further development of digital products and supporting processes to ensure our digital offerings deliver fair outcomes for customers. Governance and controls continue to be strengthened to ensure they remain fit for purpose as new technology is introduced;
- enhanced global policy requirements helping customers who are, or may become, vulnerable. Business line-led initiatives in specific markets have addressed support for appointed representatives of vulnerable customers, customers in financial distress, financial inclusion, and a pilot programme of training to help customers with or affected by cancer or dementia; and
- the delivery of our fourth annual global mandatory training course on conduct for all employees. This is complemented by an ongoing programme of newsletter, intranet and live-streamed communications, internal surveys of staff sentiment regarding progress in delivering good conduct, and conduct awareness campaigns.

Further information on our conduct is provided in the Strategic Report on page 6 and www.hsbc.com/conduct, and for conduct-related costs relating to significant items, see page 13.

Financial crime risk management

Overview

HSBC continues to embed a sustainable financial crime risk management capability. We are making good progress with our financial crime control framework enhancements including the three-year programme to further strengthen the bank's anti-bribery and corruption risk management capability. We have made good progress on completing the actions arising from the 2017 country-by-country assessment of our framework. We also continue to take further steps to refine and strengthen our defences against financial crime by applying advanced analytics and artificial intelligence to improve our ability to identify financial crime risk in our customer population.

Key developments in 2018

During 2018, the group continued to increase its efforts to keep financial crime out of the financial system. We have integrated the majority of the Global Standards programme financial crime risk core capabilities into our day-to-day operations during 2018, and expect to complete the closure of the programme infrastructure in 2019.

We have commenced several initiatives to define the next phase of financial crime risk management and to improve effectiveness through the use of artificial intelligence and applying advanced analytics techniques to achieve an intelligence-led financial crime risk management framework for the future.

Working in partnership is vital to managing financial crime risk. HSBC is a strong proponent of public-private partnerships and information-sharing initiatives. During 2018, FCR created new partnerships in HK and Singapore and continues to mature existing partnerships which include UK Joint Money Laundering Intelligence Task Force, US AML Consortium, Australia and Canada in order to bring further benefit to the bank by enhancing the understanding of financial crime risks.

We have delivered a number of enhancements to our control framework around correspondent banking; developed our operating model to address the move of EEA branches to HSBC France; and strengthened the dedicated Financial Crime Risk sub-function.

Key Risk management processes

During 2018 we embedded a robust financial crime risk management governance framework, mandating Financial Crime Risk Management Committees with a standardised agenda and management information at country, region and global business line levels.

During 2018, we also deployed anti-tax evasion controls and established an AB&C Transformation programme to further enhance the policies and controls around identifying and managing the risks of bribery and corruption across our business. We have delivered improvements to our capabilities to manage AB&C risk in our portfolio of third party service providers by undertaking a data quality remediation of existing relationships and providing targeted training to those managing higher risk relationships. For the longer term we established improved AB&C requirements for the strategic third party relationship management system. We have introduced a Fraud transformation programme to strengthen the anti-fraud capabilities. As of January 2019, the Fraud Risk stewards will become a part of FCC and a Risk and Control Framework review is planned.

We are ensuring we retain a strong link between the bank and HSBC UK Bank plc wherever there is commonality of risk or cross reliance for controls between the entities. We have maintained a single investigation function and continue to share issues of relevance between both the First and Second Line including reviews of the respective entities' governance papers and changes to relevant financial crime policies and procedures.

We are investing in the next generation of capabilities to fight financial crime by applying advanced analytics and artificial intelligence. Our commitment to enhance our risk assessment

capabilities remains, aiming to deliver more proactive risk management and improve the customer experience.

The Skilled Person

Following expiration in December 2017 of the AML Deferred Prosecution Agreement entered into with the US Department of Justice ('DoJ'), the then Monitor has continued to work under the Direction issued by the UK Financial Conduct Authority ('FCA') in 2012 in his capacity as a Skilled Person under section 166 of the Financial Services and Markets Act. He has also continued to work in his capacity as an Independent Consultant under the 2012 Cease and Desist Order issued by the US Federal Reserve Board ('FRB'). The Skilled Person and the Independent Consultant will continue working for a period of time at the FCA's and FRB's discretion.

The Skilled Person has assessed HSBC's progress towards being able to effectively manage its financial risk on a business as usual basis. The Skilled Person has issued five country reports and two quarterly reports in 2018. The Skilled Person has noted that HSBC continues to make material progress towards its financial crime risk target end state in terms of key systems, processes and people. Nonetheless, the Skilled Person has identified some areas that require further work before HSBC reaches a business as usual state. The Skilled Person has not highlighted potential instances of financial crime.

The Independent Consultant completed his fifth annual assessment. The Independent Consultant concluded that HSBC continues to make significant strides toward establishing an effective sanctions compliance programme, commending HSBC on a largely successful affiliates remediation exercise. He has, however, determined that that certain areas within HSBC's sanctions compliance programme require further work and, as such, HSBC's sanctions programme does not yet operate in a business-as-usual state. The Independent Consultant has commenced his sixth annual assessment which is due to conclude in March 2019.

Throughout 2018, the Financial System Vulnerabilities Committee ('FSVC') received regular reports on HSBC's relationship with the Skilled Person and Independent Consultant. The FSVC received regular updates on the Skilled Person's and Independent Consultant's reviews and has received the Skilled Person's country and quarterly reports and the Independent Consultant's fifth annual assessment report.

Insurance manufacturing operations risk management

Details of changes in our insurance manufacturing operations risk profile in 2018 can be found on page 65 in 'Insurance manufacturing operations risk in 2018'.

There were no material changes to our policies and practices for the management of risks arising in our insurance manufacturing operations in 2018.

Governance

(Audited)

Insurance risks are managed to a defined risk appetite, which is aligned to the bank's risk appetite and risk management framework, including the three lines of defence model. For details on the governance framework, see page 23. The Group Insurance Risk Management Meeting oversees the control framework globally and is accountable to the RBWM Risk Management Meeting on risk matters relating to the insurance business.

The monitoring of the risks within the insurance operations is carried out by insurance risk teams. Specific risk functions, including Wholesale Credit & Market Risk, Operational Risk, Information Security Risk and Financial Crime Risk, support Insurance Risk teams in their respective areas of expertise.

Stress and scenario testing

(Audited)

Stress testing forms a key part of the risk management framework for the insurance business. We participate in local and group-wide regulatory stress tests, including the Bank of England stress test of the banking system, the European Insurance and Occupational Pensions Authority stress test, and individual country insurance regulatory stress tests.

These have highlighted that a key risk scenario for the insurance business is a prolonged low interest rate environment. In order to mitigate the impact of this scenario, the insurance operations are taking a number of actions including repricing some products to reflect lower interest rates, launching less capital intensive products, investing in more capital efficient assets and developing investment strategies to optimise the expected returns against the cost of economic capital.

Management and mitigation of key risk types

Market risk

All our insurance manufacturing subsidiaries have market risk mandates which specify the investment instruments in which they are permitted to invest and the maximum quantum of market risk which they may retain. They manage market risk by using, among others, some or all of the techniques listed below, depending on the nature of the contracts written:

- For products with discretionary participating features ('DPF'), adjusting bonus rates to manage the liabilities to policyholders. The effect is that a significant portion of the market risk is borne by the policyholder.
- Asset and liability matching where asset portfolios are structured to meet projected liability cash flows. The group manages its assets using an approach that considers asset quality, diversification, cash flows matching, liquidity, volatility and target investment return. It is not always possible to match asset and liability durations due to uncertainty over the receipt of all future premiums and the timing of claims, and also because the forecast payment dates of liabilities may exceed the duration of the longest-dated investments available. We use models to assess the effect of a range of future scenarios on the values of assets and associated liabilities, and local ALCOs employ the outcomes in determining how to best structure asset holdings to support liabilities.
- Using derivatives to protect against adverse market movements or better match liability cash flows.
- For new products with investment guarantees, considering the cost when determining the level of premiums or the price structure.
- Periodically reviewing products identified as higher risk, which contain investment guarantees and embedded optionality features linked to savings and investment products, for active management.
- Designing new products to mitigate market risk, such as changing the investment return sharing between policyholders and the shareholder.
- Exiting, to the extent possible, investment portfolios whose risk is considered unacceptable.
- Repricing premiums charged to policyholders.

Credit risk

Our insurance manufacturing subsidiaries are responsible for the credit risk, quality and performance of their investment portfolios. Our assessment of the creditworthiness of issuers and counterparties is based primarily upon internationally recognised credit ratings and other publicly available information.

Investment credit exposures are monitored against limits by our insurance manufacturing subsidiaries, and are aggregated and reported to HSBC Group Insurance Credit Risk and Group Credit Risk functions. Stress testing is performed on the investment credit exposures using credit spread sensitivities and default probabilities.

We use a number of tools to manage and monitor credit risk. These include a credit report which contains a watch-list of investments with current credit concerns, primarily investments

that may be at risk of future impairment or where high concentrations to counterparties are present in the investment portfolio. The report is circulated monthly to senior management in Group Insurance and the individual country chief risk officers to identify investments which may be at risk of future impairment.

Liquidity risk

Risk is managed by cash flow matching and maintaining sufficient cash resources, investing in high credit-quality investments with deep and liquid markets, monitoring investment concentrations and restricting them where appropriate, and establishing committed contingency borrowing facilities.

Insurance manufacturing subsidiaries are required to complete quarterly liquidity risk reports for HSBC Group Insurance Risk function and an annual review of the liquidity risks to which it is exposed.

Insurance risk

The bank primarily uses the following techniques to manage and mitigate insurance risk:

- product design, pricing and overall proposition management (for example, management of lapses by introducing surrender charges);
- underwriting policy;
- claims management processes; and
- reinsurance which cedes risks above our acceptable thresholds to an external reinsurer thereby limiting our exposure.

Other material risks

Reputational risk management

Overview

Reputational risk is the risk of failing to meet stakeholder expectations as a result of any event, behaviour, action or inaction, either by HSBC, our employees or those with whom we are associated. Any material lapse in standards of integrity, compliance, customer service or operating efficiency may represent a potential reputational risk. Stakeholder expectations constantly evolve, and so reputational risk is dynamic and varies between geographical regions, groups and individuals. We have an unwavering commitment to operate at the high standards we set for ourselves in every jurisdiction.

Key developments in 2018

In the second half of 2018, as part of a revised enterprise risk management framework, it was agreed that reputational risk would be classified as a 'transverse' risk, which spans both financial and non-financial risk categories. It was also agreed that the overall risk stewardship for reputational risk would be transferred to a single risk steward, the Group Chief Risk Officer. As a result, the reputational risk policy will be revised and updated in 2019. The governance structure, however, remains unchanged.

Governance and structure

The development of policies and an effective control environment for the identification, assessment, management and mitigation of reputational risk, are considered by the Group Reputational Risk Committee which is chaired by the Group Chief Risk Officer. The focus of the Group Reputational Risk Committee is to consider matters arising from clients or transactions that either present a serious potential reputational risk to the Group or merit a Group-led decision to ensure a consistent risk management approach across the regions, global businesses and global functions. Within HBEU, matters arising from clients, transactions and third parties that present a material reputational risk are considered by the Line Of Business Reputational Risk Client Selection Committees. These committees are responsible for keeping the RMMs apprised of areas and activities presenting significant reputational risk and, where appropriate, for making recommendations to the RMM to mitigate such risk.

Key risk management processes

Our Reputational Risk and Client Selection team oversees the identification, management and control of significant reputational risks across the Region. It is responsible for informing on policies to guide HBEU reputational risk management, devising strategies to protect against reputational risk, and advising the regional businesses and regional functions to help them identify, assess and mitigate such risks, where possible. It is supported by Reputational Risk and CSEM teams in each of the businesses. Each global business has an established reputational risk management governance process. The global functions manage and escalate reputational risks within established operational risk frameworks.

Our policies set out our risk appetite and operational procedures for all areas of reputational risk, including financial crime prevention, regulatory compliance, conduct-related concerns, environmental impacts, human rights matters and employee relations.

For further details of our financial crime risk management and regulatory compliance risk management, see 'Financial crime risk management' on page 32 and 'Regulatory compliance risk management' on page 31 respectively.

Further details can be found on www.hsbc.com.

Pension risk management

There were no material changes to our policies and practices for the management of pension risk in 2018.

Governance and structure

A global pension risk framework and accompanying global policies on the management of risks related to defined benefit and defined contribution plans are in place. Pension risk is managed by a network of local and regional pension risk forums. The group's Europe Pension Oversight Forum is responsible for the governance and oversight of pension plans sponsored by HSBC within its European operations.

Key risk management processes

HSBC provides future pension benefits on a defined contribution basis from many of its European operations. However there remain future defined benefit pensions provided in the region.

In defined contribution pension plans, the contributions that HSBC is required to make are known, while the ultimate pension benefit will vary, typically with investment returns achieved by investment choices made by the employee. While the market risk to HSBC of defined contribution plans is low, the bank is still exposed to operational and reputational risk.

In defined benefit pension plans, the level of pension benefit is known. Therefore, the level of contributions required by HSBC will vary due to a number of risks, including:

- investments delivering a return below that required to provide the projected plan benefits;
- the prevailing economic environment leading to corporate failures, thus triggering write-downs in asset values (both equity and debt);
- a change in either interest rates or inflation, causing an increase in the value of the plan liabilities; and
- plan members living longer than expected (known as longevity risk).

Pension risk is assessed using an economic capital model that takes into account potential variations in these factors. The impact of these variations on both pension assets and pension liabilities is assessed using a one-in-200 year stress test. Scenario analysis and other stress tests are also used to support pension risk management.

To fund the benefits associated with defined benefit plans, sponsoring Group companies, and in some instances employees, make regular contributions in accordance with advice from actuaries and in consultation with the plan's trustees where relevant. These contributions are normally set to ensure that there

are sufficient funds to meet the cost of the accruing benefits for the future service of active members. However, higher contributions are required when plan assets are considered insufficient to cover the existing pension liabilities. Contribution rates are typically revised annually or once every three years, depending on the plan.

The defined benefit plans invest contributions in a range of investments designed to limit the risk of assets failing to meet a plan's liabilities. Any changes in expected returns from the investments may also change future contribution requirements. In pursuit of these long-term objectives, an overall target allocation of the defined benefit plan assets between asset classes is established. In addition, each permitted asset class has its own benchmarks, such as stock market or property valuation indices. The benchmarks are reviewed at least once every three to five years and more frequently if required by local legislation or circumstances. The process generally involves an extensive asset and liability review.

Key developments and risk profile

Key developments in 2018

- We continued to strengthen our operational risks controls, as described on page 65 under 'Operational risk in 2018'.
- We have integrated the majority of the Global Standards programme financial crime risk core capabilities into our day-to-day operations during 2018, and expect to complete the transition to business and function management in the first half of 2019. We continue to take further steps to refine and strengthen our defences against financial crime by applying advanced analytics and artificial intelligence.
- IFRS 9 introduced new concepts and measures such as significant increase in credit risk and lifetime expected credit losses ('ECL'). Existing stress testing and regulatory models, skills and expertise were adapted in order to meet IFRS 9 requirements. Data from various client, finance and risk systems has been integrated and validated. As a result of IFRS 9 adoption, management has additional insight and measures not previously utilised which, over time, may influence our risk appetite and risk management processes.

Credit risk in 2018

Credit risk is the risk of financial loss if a customer or counterparty fails to meet an obligation under a contract. Credit risk arises principally from direct lending, trade finance and leasing business, but also from certain other products, such as guarantees and derivatives.

1 January 2018 comparative credit disclosures reflecting the adoption of IFRS 9 have been included where available. 31 December 2017 comparative credit tables, which do not reflect the adoption of IFRS 9, have been disclosed separately on pages 55 to 61, as they are not directly comparable.

Refer to 'Standards applied during the year ended 31 December 2018 on page 97 and Note 34 'Effects of reclassifications upon adoption' of IFRS 9 for further details.

There were no material changes to the policies and practices for the management of credit risk in 2018. A summary of our current policies and practices for the management of credit risk is set out in 'Credit risk management' on page 26.

Gross loans and advances to customers of £113bn, as defined by IFRS9, have decreased from £277bn at 1 January 2018, predominantly due to the separation of the ring-fenced bank. Loans and advances to banks of £14bn have increased from £13bn at 1 January 2018; Wholesale and personal lending movements are disclosed on pages 49 to 56.

The change in ECL, as it appears in the income statement, for the period was £159m.

Our maximum exposure to credit risk is presented on page 41 and credit quality on page 46. While credit risk arises across most of our balance sheet, losses have typically been incurred on loans and advances and securitisation exposures and other structured products. As a result, our disclosures focus primarily on these two areas.

Summary of credit risk

The disclosure below presents the gross carrying/nominal amount of financial instruments to which the impairment requirements in IFRS 9 are applied and the associated allowance for ECL. Due to the forward-looking nature of IFRS 9, the scope of financial instruments on which ECL is recognised is greater than the scope of IAS 39.

The following tables analyse loans by industry sector and the extent in which they are exposed to credit risks.

The allowance for ECL at 31 December 2018 comprised of £1,347m in respect of assets held at amortised cost, £83m in respect of loan commitments and financial guarantees, and £45m in respect of debt instruments measured at fair value through other comprehensive income ('FVOCI').

Summary of financial instruments to which the impairment requirements in IFRS 9 are applied

(Audited)

	31 Dec 2018		At 1 Jan 2018	
	Gross carrying/ nominal amount	**Allowance for ECL[1]**	Gross carrying/ nominal amount	Allowance for ECL[1]
The group	**£m**	**£m**	£m	£m
Loans and advances to customers at amortised cost	**113,306**	**(1,342)**	276,852	(2,893)
– personal	**23,903**	**(206)**	120,277	(685)
– corporate and commercial	**74,058**	**(1,106)**	133,742	(2,093)
– non-bank financial institutions	**15,345**	**(30)**	22,833	(115)
Loans and advances to banks at amortised cost	**13,631**	**(3)**	13,227	(8)
Other financial assets measured at amortised cost	**165,525**	**(2)**	179,750	(2)
– cash and balances at central banks	**52,014**	**(1)**	97,601	(1)
– items in the course of collection from other banks	**839**	**—**	2,023	—
– reverse repurchase agreements – non trading	**80,102**	**—**	45,808	—
– financial investments	**13**	**—**	6	—
– prepayments, accrued income and other assets[2]	**32,557**	**(1)**	34,312	(1)
Total gross carrying amount on balance sheet	**292,462**	**(1,347)**	469,829	(2,903)
Loans and other credit related commitments	**141,620**	**(66)**	167,349	(108)
– personal	**2,062**	**—**	39,462	—
– corporate and commercial	**69,119**	**(65)**	81,323	(105)
– financial[3]	**70,439**	**(1)**	46,564	(3)
Financial guarantees [4]	**6,054**	**(17)**	8,301	(32)
– personal	**43**	**—**	70	—
– corporate and commercial	**4,429**	**(16)**	5,972	(32)
– financial	**1,582**	**(1)**	2,259	—
Total nominal amount off balance sheet[5]	**147,674**	**(83)**	175,650	(140)
	440,136	**(1,430)**	645,479	(3,043)

	Fair value	**Memorandum allowance for ECL[6]**	Fair value	Memorandum allowance for ECL[6]
	£m	**£m**	£m	£m
Debt instruments measured at fair value through other comprehensive income ('FVOCI')	**47,172**	**(45)**	55,045	(166)

1 *The total ECL is recognised in the loss allowance for the financial asset unless the total ECL exceeds the gross carrying amount of the financial asset, in which case the ECL is recognised as a provision.*
2 *Includes only those financial instruments which are subject to the impairment requirements of IFRS 9. 'Prepayments, accrued income and other assets' as presented within the consolidated balance sheet on page 89 includes both financial and non-financial assets.*
3 *31 December 2017 balances have been restated to include £32.5bn of loan commitments (unsettled reverse repurchase agreements) not previously identified for disclosure.*
4 *Excludes performance guarantee contracts to which the impairment requirements in IFRS 9 are not applied.*
5 *Represents the maximum amount at risk should the contracts be fully drawn upon and clients default.*
6 *Debt instruments measured at FVOCI continue to be measured at fair value with the allowance for ECL as a memorandum item. Change in ECL is recognised in 'Change in expected credit losses and other credit impairment charges' in the income statement.*

Summary of financial instruments to which the impairment requirements in IFRS 9 are applied

(Audited)

The bank	31 Dec 2018 Gross carrying/ nominal amount £m	Allowance for ECL[1] £m
Loans and advances to customers at amortised cost	59,527	(744)
– personal	3,249	(9)
– corporate and commercial	39,256	(685)
– non-bank financial institutions	17,022	(50)
Loans and advances to banks at amortised cost	12,689	(3)
Other financial assets measured at amortised cost	124,544	(1)
– cash and balances at central banks	40,657	–
– items in the course of collection from other banks	442	–
– reverse repurchase agreements – non trading	56,495	–
– financial investments	–	–
– prepayments, accrued income and other assets[2]	26,950	(1)
Total gross carrying amount on balance sheet	196,760	(748)
Loans and other credit related commitments	61,196	(50)
– personal	305	–
– corporate and commercial	33,291	(49)
– financial	27,600	(1)
Financial guarantees[3]	5,578	(14)
– personal	3	–
– corporate and commercial	1,846	(13)
– financial	3,729	(1)
Total nominal amount off balance sheet[4]	66,774	(64)
	263,534	(812)

	Fair value £m	Memorandum allowance for ECL[5] £m
Debt instruments measured at fair value through other comprehensive income ('FVOCI')	26,646	(6)

1 *The total ECL is recognised in the loss allowance for the financial asset unless the total ECL exceeds the gross carrying amount of the financial asset, in which case the ECL is recognised as a provision.*
2 *Includes only those financial instruments which are subject to the impairment requirements of IFRS 9. 'Prepayments, accrued income and other assets' as presented within the consolidated balance sheet on page 89 includes both financial and non-financial assets.*
3 *Excludes performance guarantee contracts to which the impairment requirements in IFRS 9 are not applied.*
4 *Represents the maximum amount at risk should the contracts be fully drawn upon and clients default.*
5 *Debt instruments measured at FVOCI continue to be measured at fair value with the allowance for ECL as a memorandum item. Change in ECL is recognised in 'Change in expected credit losses and other credit impairment charges' in the income statement.*

The following table provides an overview of the banks and group's credit risk by stage and industry, and the associated ECL coverage. The financial assets recorded in each stage have the following characteristics:

- stage 1: unimpaired and without significant increase in credit risk on which a 12-month allowance for ECL is recognised.
- stage 2: a significant increase in credit risk has been experienced since initial recognition on which a lifetime ECL is recognised.
- stage 3: objective evidence of impairment, and are therefore considered to be in default or otherwise credit-impaired on which a lifetime ECL is recognised.
- purchased or originated credit-impaired ('POCI'): Purchased or originated at a deep discount that reflects the incurred credit losses on which a lifetime ECL is recognised.

Summary of credit risk (excluding debt instruments measured at FVOCI) by stage distribution and ECL coverage by industry sector at 31 December 2018

(Audited)

	Gross carrying/nominal amount[2]					Allowance for ECL					ECL coverage %				
	Stage 1	Stage 2	Stage 3	POCI[3]	Total	Stage 1	Stage 2	Stage 3	POCI[3]	Total	Stage 1	Stage 2	Stage 3	POCI[3]	Total
The group	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	%	%	%	%	%
Loans and advances to customers at amortised cost	102,129	8,816	2,244	117	113,306	(121)	(171)	(972)	(78)	(1,342)	0.1	1.9	43.3	66.7	1.2
– personal	22,170	1,206	527	–	23,903	(9)	(27)	(170)	–	(206)	–	2.2	32.3	–	0.9
– corporate and commercial	64,822	7,476	1,643	117	74,058	(99)	(132)	(797)	(78)	(1,106)	0.2	1.8	48.5	66.7	1.5
– non-bank financial institutions	15,137	134	74	–	15,345	(13)	(12)	(5)	–	(30)	0.1	9.0	6.8	–	0.2
Loans and advances to banks at amortised cost	13,565	66	–	–	13,631	(2)	(1)	–	–	(3)	–	1.5	–	–	–
Other financial assets measured at amortised	165,496	24	5	–	165,525	(1)	–	(1)	–	(2)	–	–	20.0	–	–
Loan and other credit-related commitments	136,539	4,827	249	5	141,620	(27)	(26)	(13)	–	(66)	–	0.5	5.2	–	–
– personal	2,005	54	3	–	2,062	–	–	–	–	–	–	–	–	–	–
– corporate and commercial	64,428	4,441	245	5	69,119	(26)	(26)	(13)	–	(65)	–	0.6	5.3	–	0.1
– financial	70,106	332	1	–	70,439	(1)	–	–	–	(1)	–	–	–	–	–
Financial guarantees[1]	5,423	565	64	2	6,054	(4)	(9)	(4)	–	(17)	0.1	1.6	6.3	–	0.3
– personal	42	–	1	–	43	–	–	–	–	–	–	–	–	–	–
– corporate and commercial	3,866	499	62	2	4,429	(4)	(8)	(4)	–	(16)	0.1	1.6	6.5	–	0.4
– financial	1,515	66	1	–	1,582	–	(1)	–	–	(1)	–	1.5	–	–	0.1
At 31 Dec	423,152	14,298	2,562	124	440,136	(155)	(207)	(990)	(78)	(1,430)	–	1.4	38.6	62.9	0.3

1 *Excludes performance guarantee contracts to which the impairment requirements in IFRS 9 are not applied.*
2 *Represents the maximum amount at risk should the contracts be fully drawn upon and clients default.*
3 *Purchased or originated credit-impaired ('POCI').*

Unless identified at an earlier stage, all financial assets are deemed to have suffered a significant increase in credit risk when they are 30 days past due and are transferred from stage 1 to stage 2. The following disclosure presents the ageing of stage 2 financial assets. It distinguishes those assets that are classified as stage 2 when they are less than 30 days past due (1-29 DPD) from those that are more than 30 DPD (30 and > DPD). Past due financial instruments are those loans where customers have failed to make payments in accordance with the contractual terms of their facilities.

Stage 2 days past due analysis at 31 December 2018

(Audited)

	Gross carrying amount			Allowance for ECL			ECL coverage %		
		Of which:			Of which:			Of which:	
	Stage 2	1 to 29 DPD[1]	30 and > DPD[1]	Stage 2	1 to 29 DPD[1]	30 and > DPD[1]	Stage 2	1 to 29 DPD[1]	30 and > DPD[1]
The group	£m	£m	£m	£m	£m	£m	£m	£m	£m
Loans and advances to customers at amortised cost:	8,816	117	178	(171)	(3)	(6)	1.9	2.6	3.4
– Personal	1,206	80	83	(27)	(2)	(4)	2.2	2.5	4.8
– Corporate and commercial	7,476	37	95	(132)	(1)	(2)	1.8	2.7	2.1
– Non-bank financial institutions	134	–	–	(12)	–	–	9.0	–	–
Loans and advances to banks at amortised cost	66	5	–	(1)	–	–	1.5	–	–
Other financial assets measured at amortised cost	24	–	–	–	–	–	–	–	–

1 *Days past due ('DPD') Up-to-date accounts in stage 2 are not shown in amounts presented above.*

Summary of credit risk (excluding debt instruments measured at FVOCI) by stage distribution and ECL coverage by industry sector at 1 January 2018

	Gross carrying/nominal amount[3]					Allowance for ECL					ECL coverage %				
	Stage 1	Stage 2	Stage 3	POCI[4]	Total	Stage 1	Stage 2	Stage 3	POCI[4]	Total	Stage 1	Stage 2	Stage 3	POCI[4]	Total
The group	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	%	%	%	%	%
Loans and advances to customers at amortised cost	256,850	14,526	5,063	413	276,852	(401)	(566)	(1,852)	(74)	(2,893)	0.2	3.9	36.6	17.9	1.0
– personal	115,877	3,153	1,247	—	120,277	(129)	(195)	(361)	—	(685)	0.1	6.2	28.9	—	0.6
– corporate and commercial	118,985	10,699	3,645	413	133,742	(267)	(368)	(1,384)	(74)	(2,093)	0.2	3.4	38.0	17.9	1.6
– non-bank financial institutions	21,988	674	171	—	22,833	(5)	(3)	(107)	—	(115)	—	0.4	62.6	—	0.5
Loans and advances to banks at amortised cost	12,966	250	11	—	13,227	(5)	(2)	(1)	—	(8)	—	0.8	9.1	—	0.1
Other financial assets measured at amortised cost	179,519	225	4	2	179,750	(2)	—	—	—	(2)	—	—	—	—	—
Loan and other credit related commitments	163,726	3,364	225	34	167,349	(42)	(49)	(17)	—	(108)	—	1.5	7.6	—	0.1
– personal	39,300	112	50	—	39,462	—	—	—	—	—	—	—	—	—	—
– corporate and commercial	77,932	3,182	175	34	81,323	(40)	(48)	(17)	—	(105)	0.1	1.5	9.7	—	0.1
– financial[1]	46,494	70	—	—	46,564	(2)	(1)	—	—	(3)	—	1.4	—	—	—
Financial guarantees[2]	7,595	647	43	16	8,301	(4)	(1)	(27)	—	(32)	0.1	0.2	62.8	—	0.4
– personal	69	—	1	—	70	—	—	—	—	—	—	—	—	—	—
– corporate and commercial	5,353	561	42	16	5,972	(4)	(1)	(27)	—	(32)	0.1	0.2	64.3	—	0.5
– financial	2,173	86	—	—	2,259	—	—	—	—	—	—	—	—	—	—
At 1 Jan 2018	620,656	19,012	5,346	465	645,479	(454)	(618)	(1,897)	(74)	(3,043)	0.1	3.3	35.5	15.9	0.5

1 *31 December 2017 balances have been restated to include £32.5bn of loan commitments (unsettled reverse repurchase agreements) not previously identified for disclosure.*
2 *Excludes performance guarantee contracts to which the impairment requirements in IFRS 9 are not applied.*
3 *Represents the maximum amount at risk should the contracts be fully drawn upon and clients default.*
4 *Purchased or originated credit-impaired ('POCI').*

Stage 2 days past due analysis at 1 January 2018

	Gross carrying amount			Allowance for ECL			ECL coverage %		
		Of which:			Of which:			Of which:	
	Stage 2	1 to 29 DPD[1]	30 and > DPD[1]	Stage 2	1 to 29 DPD[1]	30 and > DPD[1]	Stage 2	1 to 29 DPD[1]	30 and > DPD[1]
The group	£m	£m	£m	£m	£m	£m	%	%	%
Loans and advances to customers at amortised cost	14,526	477	590	(566)	(49)	(50)	3.9	10.3	8.5
– personal	3,153	411	183	(195)	(36)	(36)	6.2	8.8	19.7
– corporate and commercial	10,699	66	405	(368)	(13)	(14)	3.4	19.7	3.5
– non-bank financial institutions	674	—	2	(3)	—	—	0.4	—	—
Loans and advances to banks at amortised cost	250	1	2	(2)	(2)	—	0.8	200.0	—
Other financial assets measured at amortised cost	225	1	16	—	—	—	—	—	—

1 *Days past due ('DPD') Up-to-date accounts in stage 2 are not shown in amounts presented above.*

Summary of credit risk (excluding debt instruments measured at FVOCI) by stage distribution and ECL coverage by industry sector at 31 December 2018

(Audited)

	Gross carrying/nominal amount[2]					Allowance for ECL					ECL coverage %				
	Stage 1	Stage 2	Stage 3	POCI[3]	Total	Stage 1	Stage 2	Stage 3	POCI[3]	Total	Stage 1	Stage 2	Stage 3	POCI[3]	Total
The bank	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	%	%	%	%	%
Loans and advances to customers at amortised cost	52,962	5,477	985	103	59,527	(86)	(122)	(461)	(75)	(744)	0.2	2.2	46.8	72.8	1.2
– personal	3,134	91	24	–	3,249	(1)	(3)	(5)	–	(9)	–	3.3	20.8	–	0.3
– corporate and commercial	32,966	5,292	895	103	39,256	(72)	(108)	(430)	(75)	(685)	0.2	2.0	48.0	72.8	1.7
– non-bank financial institutions	16,862	94	66	–	17,022	(13)	(11)	(26)	–	(50)	0.1	11.7	39.4	–	0.3
Loans and advances to banks at amortised cost	12,629	60	–	–	12,689	(2)	(1)	–	–	(3)	–	1.7	–	–	–
Other financial assets measured at amortised cost	124,521	19	4	–	124,544	–	–	(1)	–	(1)	–	–	25.0	–	–
Loan and other credit-related commitments	58,162	2,889	141	5	61,197	(24)	(24)	(2)	–	(50)	–	0.8	1.4	–	0.1
– personal	302	3	–	–	305	–	–	–	–	–	–	–	–	–	–
– corporate and commercial	30,549	2,597	141	5	33,292	(23)	(24)	(2)	–	(49)	0.1	0.9	1.4	–	0.1
– financial	27,311	289	–	–	27,600	(1)	–	–	–	(1)	–	–	–	–	–
Financial guarantees[1]	5,248	277	53	–	5,578	(3)	(7)	(4)	–	(14)	0.1	2.5	7.5	–	0.3
– personal	3	–	–	–	3	–	–	–	–	–	–	–	–	–	–
– corporate and commercial	1,567	227	52	–	1,846	(3)	(6)	(4)	–	(13)	0.2	2.6	7.7	–	0.7
– financial	3,678	50	1	–	3,729	–	(1)	–	–	(1)	–	2.0	–	–	–
At 31 Dec 2018	**253,522**	**8,722**	**1,183**	**108**	**263,535**	**(115)**	**(154)**	**(468)**	**(75)**	**(812)**	**–**	**1.8**	**39.6**	**69.4**	**0.3**

1 Excludes performance guarantee contracts to which the impairment requirements in IFRS 9 are not applied.
2 Represents the maximum amount at risk should the contracts be fully drawn upon and clients default.
3 Purchased or originated credit-impaired ('POCI').

Unless identified at an earlier stage, all financial assets are deemed to have suffered a significant increase in credit risk when they are 30 days past due and are transferred from stage 1 to stage 2. The following disclosure presents the ageing of stage 2 financial assets. It distinguishes those assets that are classified as stage 2 when they are less than 30 days past due (1-29 DPD) from those that are more than 30 DPD (30 and > DPD). Past due financial instruments are those loans where customers have failed to make payments in accordance with the contractual terms of their facilities.

Stage 2 days past due analysis at 31 December 2018

(Audited)

	Gross carrying amount			Allowance for ECL			ECL coverage %		
		Of which:			Of which:			Of which:	
	Stage 2	1 to 29 DPD[1]	30 and > DPD[1]	Stage 2	1 to 29 DPD[1]	30 and > DPD[1]	Stage 2	1 to 29 DPD[1]	30 and > DPD[1]
The bank	£m	£m	£m	£m	£m	£m	£m	£m	£m
Loans and advances to customers at amortised cost:	5,477	20	5	(122)	–	–	2.2	–	–
– Personal	91	20	5	(3)	–	–	3.3	–	–
– Corporate and commercial	5,292	–	–	(108)	–	–	2.0	–	–
– Non-bank financial institutions	94	–	–	(11)	–	–	11.7	–	–
Loans and advances to banks at amortised cost	60	–	–	(1)	–	–	1.7	–	–
Other financial assets measured at amortised cost	19	–	–	–	–	–	–	–	–

1 Days past due ('DPD') Up-to-date accounts in stage 2 are not shown in amounts presented above.

Credit exposure

Maximum exposure to credit risk

(Audited)

The following table provides information on balance sheet items, offsets, and loan and other credit-related commitments.

The offset on derivatives remains in line with the movements in maximum exposure amounts.

'Maximum exposure to credit risk' table

The following table presents our maximum exposure before taking account of any collateral held or other credit enhancements (unless such enhancements meet accounting offsetting requirements). The table excludes financial instruments whose carrying amount best represents the net exposure to credit risk and it excludes equity securities as they are not subject to credit risk. For the financial assets recognised on the balance sheet, the maximum exposure to credit risk equals their carrying amount; for financial guarantees and other guarantees granted, it is the maximum amount that we would have to pay if the guarantees were called upon. For loan commitments and other credit-related commitments, it is generally the full amount of the committed facilities.

The offset in the table relates to amounts where there is a legally enforceable right of offset in the event of counterparty default and where, as a result, there is a net exposure for credit risk purposes. However, as there is no intention to settle these balances on a net basis under normal circumstances, they do not qualify for net presentation for accounting purposes. No offset has been applied to off-balance sheet collateral. In the case of derivatives the offset column also includes collateral received in cash and other financial assets.

Other credit risk mitigants

While not disclosed as an offset in the following 'Maximum exposure to credit risk' table, other arrangements are in place which reduce our maximum exposure to credit risk. These include a charge over collateral on borrowers' specific assets such as residential properties, collateral held in the form of financial instruments that are not held on balance sheet and short positions in securities. In addition, for financial assets held as part of linked insurance/investment contracts the risk is predominantly borne by the policyholder. See Note 28 on the Financial Statements for further details of collateral in respect of certain loans and advances and derivatives.

Maximum exposure to credit risk

(Audited)

	Maximum exposure	Offset	Net
The group	**£m**	**£m**	**£m**
Loans and advances to customers held at amortised cost	111,964	(12,579)	99,385
– personal	23,697	–	23,697
– corporate and commercial	72,952	(10,610)	62,342
– non-bank financial institutions	15,315	(1,969)	13,346
Loans and advances to banks at amortised cost	13,628	(12)	13,616
Other financial assets held at amortised cost	165,793	(17,065)	148,728
– cash and balances at central banks	52,013	–	52,013
– items in the course of collection from other banks	839	–	839
– reverse repurchase agreements – non trading	80,102	(17,065)	63,037
– financial investments	13	–	13
– prepayments, accrued income and other assets	32,826	–	32,826
Derivatives	144,522	(140,644)	3,878
Total on balance sheet exposure to credit risk	435,907	(170,300)	265,607
Total off-balance sheet	172,073	–	172,073
– financial and other guarantees[1]	23,244	–	23,244
– loan and other credit-related commitments	148,829	–	148,829
31 Dec 2018	607,980	(170,300)	437,680

The bank	**£m**	**£m**	**£m**
Loans and advances to customers held at amortised cost	58,783	(20,045)	38,738
– personal	3,240	–	3,240
– corporate and commercial	38,571	(10,610)	27,961
– non-bank financial institutions	16,972	(9,435)	7,537
Loans and advances to banks at amortised cost	12,686	(22)	12,664
Other financial assets held at amortised cost	124,815	(13,401)	111,414
– cash and balances at central banks	40,657	–	40,657
– items in the course of collection from other banks	442	–	442
– reverse repurchase agreements – non trading	56,495	(13,401)	43,094
– financial investments	–	–	–
– prepayments, accrued income and other assets	27,221	–	27,221
Derivatives	139,229	(137,504)	1,725
Total on balance sheet exposure to credit risk	335,513	(170,972)	164,541
Total off-balance sheet	81,748	–	81,748
– financial and other guarantees[1]	15,860	–	15,860
– loan and other credit-related commitments	65,888	–	65,888
31 Dec 2018	417,261	(170,972)	246,289

1 *'Financial and other guarantees' represents 'Financial guarantees' and 'Performance and other guarantees' as disclosed in Note 30.*

Concentration of exposure

The geographical diversification of our lending portfolio, and our broad range of global businesses and products, ensured that we did not overly depend on a few markets or businesses to generate growth in 2018.

For an analysis of:

- financial investments, see Note 15 on the Financial Statements;
- trading assets, see Note 10 on the Financial Statements;
- derivatives, see page 52 and Note 14 on the Financial Statements; and
- loans and advances by industry sector and by the location of the principal operations of the lending subsidiary or by the location of the lending branch, see page 50 for wholesale lending and page 52 for personal lending.

Credit deterioration of financial instruments

(Audited)

A summary of our current policies and practices regarding the identification, treatment and measurement of stage 1, stage 2 and stage 3 (credit impaired) and POCI financial instruments can be found in note 1.2 of the financial statements.

Measurement uncertainty and sensitivity analysis of ECL estimates

Expected credit loss impairment allowances recognised in the financial statements reflect the effect of a range of possible economic outcomes, calculated on a probability-weighted basis, based on the economic scenarios described below. The recognition and measurement of expected credit losses ('ECL') involves the use of significant judgement and estimation. It is necessary to formulate multiple forward-looking economic forecasts and incorporate them into the ECL estimates. HSBC uses a standard framework to form economic scenarios to reflect assumptions about future economic conditions, supplemented with the use of management judgement, which may result in using alternative or additional economic scenarios and/or management adjustments.

Methodology

HSBC has adopted the use of three scenarios, representative of our view of forecast economic conditions, sufficient to calculate unbiased expected loss in most economic environments. They represent a 'most likely outcome' (the Central scenario), and two, less likely 'outer' scenarios, referred to as the Upside and Downside scenarios. Each outer scenario is consistent with a probability of 10%, while the Central scenario is assigned the remaining 80%, according to the decision of HSBC's senior management. This weighting scheme is deemed appropriate for the unbiased estimation of ECL in most circumstances. Key scenario assumptions are set using the average of forecasts of external economists, helping to ensure that the IFRS 9 scenarios are unbiased and maximise the use of independent information. The Central, Upside and Downside scenarios selected with reference to external forecast distributions using the above approach are termed the 'consensus economic scenarios'.

For the Central scenario, HSBC sets key assumptions such as GDP growth, inflation, unemployment and policy interest rates, using either the average of external forecasts (commonly referred to as consensus forecasts) for most economies, or market prices. An external provider's global macro model, conditioned to follow the consensus forecasts, projects the other paths required as inputs to credit models. This external provider is subject to HSBC's risk governance framework, with oversight by a specialist internal unit.

The Upside and Downside scenarios are designed to be cyclical, in that GDP growth, inflation and unemployment usually revert back to the Central scenario after the first three years for major economies. We determine the maximum divergence of GDP growth from the Central scenario using the 10th and the 90th percentile of the entire distribution of forecast outcomes for major economies. While key economic variables are set with reference to external distributional forecasts, we also align the overall narrative of the scenarios to the macroeconomic risks described in HSBC's 'Top and emerging risks' on 20. This ensures that scenarios remain consistent with the more qualitative assessment of these risks. We project additional variable paths using the external provider's global macro model.

We apply the following steps to generate the three economic scenarios:

- Economic risk assessment: We develop a shortlist of the upside and downside economic and political risks most relevant to HSBC and the IFRS 9 measurement objective.
- Scenario generation: For the Central scenario, we obtain a pre-defined set of economic paths from the average taken from the consensus survey of professional forecasters. Paths for the two outer scenarios are benchmarked to the Central scenario and reflect the economic risk assessment. We select scenarios that in management's judgement are representative of the probability weighting scheme, informed by the current economic outlook, data analysis of past recessions, and transitions in and out of recession. The key assumptions made, and the accompanying paths, represent our "best estimate" of a scenario at a specified probability. Suitable narratives are developed for the Central scenario and the paths of the two outer scenarios.
- Variable enrichment: We expand each scenario through enrichment of variables. This includes the production of more than 400 variables that are required to calculate ECL. The external provider expands these scenarios by using as inputs the agreed scenario narratives and the variables aligned to these narratives. Scenarios, once expanded, continue to be benchmarked to latest events and information. Late breaking events could lead to revision of scenarios to reflect management judgement.

The Upside and Downside scenarios are generated at year-end and are only updated during the year if economic conditions change significantly. The Central scenario is generated every quarter. In quarters where only the Central scenario is updated, outer scenarios for use in Wholesale are adjusted such that the relationship between the Central scenario and outer scenarios in the quarter is consistent with that observed at the last full scenario generation. In Retail, three scenarios are run annually to establish the effect of multiple scenarios for each portfolio. This effect is then applied in each quarter with the understanding that the non-linearity of response to economic conditions should not change, unless a significant change in economic conditions occurs.

HSBC recognises that the consensus economic scenario approach, using three scenarios, will be insufficient in certain economic environments. Additional analysis may be requested at management's discretion. This may result in a change in the weighting scheme assigned to the three scenarios or the inclusion of extra scenarios. We anticipate that there will be only limited instances when the standard approach will not apply. We invoked this additional step on 1 January 2018, due to the specific uncertainties facing the UK economy at that time, resulting in the recognition of additional ECL through a management adjustment for economic uncertainty. During 2018 we maintained additional ECL impairment allowances for the UK.

Description of Consensus Central Scenarios

The Consensus Central Scenario

HSBC's central scenario is one of moderate growth over the forecast period 2019-2023. Global GDP growth is expected to be 2.9% on average over the period, which is marginally higher than the average growth rate over the period 2013-2017. Across the key markets, we note that:

- Expected average rates of GDP growth over the 2019-2023 period are lower than average growth rates achieved over the 2013-2017 period for the UK which reflects expectations that the long-term impact of current economic uncertainty will be moderately adverse.
- The average unemployment rate over the projection horizon is expected to remain at or below the averages observed in the 2013 -2017 period across all of our major markets.
- Inflation is expected to be stable despite steady GDP growth and strong labour markets and will remain close to central bank targets in our core markets over the forecast period.
- Major central banks are expected to gradually raise their main policy interest rate.
- The West Texas Intermediate oil price is forecast to average $63 per barrel over the projection period.

The following table describes key macroeconomic variables and the probabilities assigned in the Consensus Central scenario.

Consensus Central scenario (average 2019–2023)

	UK	France
GDP growth rate (%)	1.7	1.5
Inflation (%)	2.1	1.7
Unemployment (%)	4.5	7.8
Short Term Interest rate (%)	1.2	0.2
10 year Treasury bond yields (%)	2.6	2.0
House price growth (%)	2.9	1.7
Equity price growth (%)	3.2	3.1
Probability (%)	50.0	80.0

The Consensus Upside scenario

The economic forecast distribution of risks (as captured by consensus probability distributions of GDP growth) has shown a marginal increase in upside risks for the eurozone, but a decrease of the same for the UK over the course of 2018. Globally, real GDP growth rises in the first two years of the Upside scenario before converging to the Central scenario. Increased confidence, de-escalation of trade tensions and removal of trade barriers, expansionary fiscal policy, positive resolution of economic uncertainty in the UK, stronger oil prices as well as calming of geopolitical tensions are the risk themes that support the 2018 year-end upside scenario.

The following table describes key macroeconomic variables and the probabilities assigned in the Consensus Upside scenario.

Consensus Upside scenario (average 2019–2023)

	UK	France
GDP growth rate (%)	2.2	1.9
Inflation (%)	2.3	2.0
Unemployment (%)	4.2	7.4
Short term interest rate (%)	1.3	0.2
10-year treasury bond yields (%)	2.7	2.0
House price growth (%)	4.1	2.3
Equity price growth (%)	6.0	7.3
Probability (%)	10.0	10.0

The Consensus Downside scenario

The distribution of risks (as captured by consensus probability distributions of GDP growth) were broadly stable for the eurozone and the UK (but see discussion on UK economic uncertainty below). Globally, real GDP growth declines for two years in the Downside scenario before recovering to the Central scenario. House price growth either stalls or contracts and equity markets correct abruptly in our major markets. The global slowdown in demand drives commodity prices lower and results in an accompanying fall in inflation. Central Banks remain accommodative. This is consistent with the key risk themes of the downside, such as an intensification of global protectionism and trade barriers, faster than expected tightening of the Fed policy rate, a worsening of economic uncertainty in the UK, China choosing to rebalance with stringent measures, and weaker commodity prices.

The following table describes key macroeconomic variables and the probabilities assigned in the Consensus Downside scenario.

Consensus Downside scenario (average 2019–2023)

	UK	France
GDP growth rate (%)	1.1	1.1
Inflation (%)	1.7	1.3
Unemployment (%)	4.8	8.2
Short Term Interest rate (%)	0.3	(0.3)
10 year Treasury bond yields (%)	1.6	0.9
House price growth (%)	1.0	(1.3)
Equity price growth (%)	(0.2)	(2.4)
Probability (%)	–	10.0

Alternative Downside scenarios

UK economic uncertainty

A number of events occurred over the course of 2018 that led management to re-evaluate the shape of the consensus distribution for the UK. Given the challenges facing economic forecasters in this environment, management was concerned that this distribution did not adequately represent downside risks for the UK. The high level of economic uncertainty that prevailed at the end of 2018, including the lack of progress in agreeing a clear plan for an exit from the EU and the uncertain performance of the UK economy after an exit, was a key factor in this consideration. In management's view, the extent of this uncertainty justifies the use of the following Alternative Downside scenarios, used in place of the consensus downside, with the assigned probabilities:

Alternative Downside scenario 1 (AD1): Economic uncertainty could have a large impact on the UK economy resulting in a long lasting recession with a weak recovery. This scenario reflects the consequences of such a recession with an initial risk-premium shock and weaker long-run productivity growth. This scenario has been used with a 30% weighting.

Alternative Downside scenario 2 (AD2): This scenario reflects the possibility that economic uncertainty could result in a deep cyclical shock triggering a steep depreciation in sterling, a sharp increase in inflation and an associated monetary policy response. This represents a tail risk and has been assigned a 5% weighting.

Alternative Downside scenario 3 (AD3): This scenario reflects the possibility that the adverse impact associated with economic uncertainty currently in the UK could manifest over a far longer period of time with the worst effects occurring later than in the above two scenarios. This scenario is also considered a tail risk and has been assigned a 5% weighting.

The table below describes key macroeconomic variables and the probabilities for each of the Alternative Downside scenarios:

Average 2019–2023

	Alternative Downside scenario 1	Alternative Downside scenario 2	Alternative Downside scenario 3
GDP growth rate (%)	0.5	(0.1)	(0.7)
Inflation (%)	2.2	2.4	2.7
Unemployment (%)	6.5	8.0	7.7
Short term interest rate (%)	0.4	2.5	2.5
10-year treasury bond yields (%)	1.8	4.0	4.0
House price growth (%)	(1.5)	(3.3)	(4.8)
Equity price growth (%)	(0.9)	(2.3)	(7.5)
Probability (%)	30.0	5.0	5.0

The conditions which resulted in departure from the consensus economic forecasts will be reviewed regularly as economic conditions change in future to determine whether this adjustment continues to be necessary.

How economic scenarios are reflected in the wholesale calculation of ECL

HSBC has developed a globally consistent methodology for the application of economic scenarios into the calculation of ECL by incorporating those scenarios into the estimation of the term structure of probability of default ('PD') and loss given default ('LGD'). For PDs, we consider the correlation of economic guidance to default rates for a particular industry in a country. For LGD calculations we consider the correlation of economic guidance to collateral values and realisation rates for a particular country and industry. PDs and LGDs are estimated for the entire term structure of each instrument.

For impaired loans, LGD estimates take into account independent recovery valuations provided by external consultants where available, or internal forecasts corresponding to anticipated economic conditions and individual company conditions. In estimating the ECL on impaired loans that are individually considered not to be significant, HSBC incorporates economic

scenarios proportionate to the probability-weighted outcome and the central scenario outcome for non-stage 3 populations.

How economic scenarios are reflected in the retail calculation of ECL

HSBC has developed and implemented a globally consistent methodology for incorporating forecasts of economic conditions into ECL estimates. The impact of economic scenarios on PD is modelled at a portfolio level. Historical relationships between observed default rates and macroeconomic variables are integrated into IFRS 9 ECL estimates by leveraging economic response models. The impact of these scenarios on PD is modelled over a period equal to the remaining maturity of underlying asset or assets. The impact on LGD is modelled for mortgage portfolios by forecasting future loan-to-value ('LTV') profiles for the remaining maturity of the asset by leveraging national level forecasts of the house price index ('HPI') and applying the corresponding LGD expectation.

Impact of UK economic uncertainty on ECL

In light of UK economic uncertainty at 31 December 2018, management made an adjustment that increased ECL allowances in the UK by £64m, of which £62m was attributed to GB&M and £2m to CMB. The adjustment represents incremental ECL based on a probability-weighted distribution of the upside (10%), consensus (50%) and alternative downside scenarios (40% combined).

In its assessment of events after the balance sheet date, HSBC considered, among others, the events related to the process of the UK's withdrawal from the European Union that occurred between 31 December 2018 and the date when the financial statements were authorised for issue, and concluded that no adjustments to the financial statements were required.

Economic scenarios sensitivity analysis of ECL estimates

The ECL outcome is sensitive to judgement and estimations made with regards to the formulation and incorporation of multiple forward-looking economic forecasts described above. As a result, management assessed and considered the sensitivity of the ECL outcome against the forward-looking economic conditions as part of the ECL governance process by recalculating the ECL under each scenario described above for selected portfolios, applying a 100% weighting to each scenario in turn. The weighting is reflected in both the determination of significant increase in credit risk as well as the measurement of the resulting ECL. The ECL relating to Wholesale defaulted obligors reflects a combination of anticipated economic conditions, independent recovery valuations and factors specific to the defaulted corporate. For wholesale credit risk exposures, the sensitivity analysis excludes ECL and financial instruments related to defaulted obligors because the measurement of ECL is relatively more sensitive to credit factors specific to the obligor than future economic scenarios.

The economic scenarios are generated to capture HSBC's view of a range of possible forecast economic conditions that is sufficient for the calculation of unbiased and probability-weighted ECL. Therefore, the ECL calculated for each of the scenarios represent a range of possible outcomes that have been evaluated to estimate ECL. As a result, the ECL calculated for the Upside and Downside scenarios should not be taken to represent the upper and lower limits of possible actual ECL outcomes. There is a high degree of estimation uncertainty in numbers representing tail risk scenarios when assigned a 100% weighting, and an indicative range is provided for the UK tail risk sensitivity analysis. A wider range of possible ECL outcomes reflects uncertainty about the distribution of economic conditions and does not necessarily mean that credit risk on the associated loans is higher than for loans where the distribution of possible future economic conditions is narrower. The recalculated ECL for each of the scenarios should be read in the context of the sensitivity analysis as a whole and in conjunction with the narrative disclosures provided below.

ECL under each scenario is given in dollar terms and as a percentage of the gross carrying amount (and, for wholesale lending, the nominal amount for related loan commitments and financial guarantees).

Wholesale analysis

IFRS 9 ECL sensitivity to future economic conditions[1]

	UK	France
ECL Coverage of Loans and Advances to Customers at 31 December 2018		
Reported ECL (£m)	**218**	**36**
Gross carrying/nominal amount (£m)	**98,450**	**49,725**
Reported ECL Coverage (%)	**0.22**	**0.07**
Coverage Ratios by Scenario (%):		
Consensus central scenario	**0.16**	**0.07**
Consensus upside scenario	**0.14**	**0.07**
Consensus downside scenario	**0.18**	**0.1**
Coverage ratios for alternative scenarios		
UK AD 1	**0.22**	
UK AD 2	**0.39**	
UK AD 3	**0.35**	
Alternative scenarios ECL		
AD1	**213**	
Tail risk scenarios (UK AD 2-3)	**384 - 341**	

1 Excludes ECL and Drawn Amounts related to defaulted obligors

ECL coverage rates reflect the underlying observed credit defaults, the sensitivity to economic environment, extent of security and the effective maturity of the book. The additional scenarios for UK economic uncertainty could, if they occurred, increase ECL coverage by between 13 to 17 basis points compared with reported ECL for loans and advances to customers including loan commitments and financial guarantees, and represents the elasticity between macro economic factors such as gross domestic product and the risk of default.

Retail analysis

IFRS 9 ECL sensitivity to future economic conditions[1]

	UK	France
ECL Coverage of Loans and Advances to Customers at 31 December 2018		
Reported ECL (£m)	**6**	**116**
Drawn Amount (£m)	**1,899**	**16,760**
Reported ECL Coverage (%)	**0.33**	**0.69**
Coverage Ratios by scenario (%):		
Consensus central scenario	**0.33**	**0.69**
Consensus upside scenario	**0.29**	**0.69**
Consensus downside scenario	**0.37**	**0.7**

1 ECL sensitivities exclude portfolios utilising less complex modelling approaches

Under certain economic conditions, economic factors can influence ECL in counter-intuitive ways (for example an increase in GDP growth accompanied by rising interest rates resulting in an increase in PDs) and it may be necessary to apply management judgement to the output which, following management review of the calculated ECL sensitivities, may require modelled output adjustments. An example of this is in France, where the ECL sensitivity results have been adjusted to more accurately reflect management's views of ECL sensitivity under an upside and downside scenario by inverting the Upside and Downside ECL sensitivity.

For all the above sensitivity analyses, as the level of uncertainty, economic forecasts, historical economic variable correlations or credit quality changes, corresponding changes in the ECL sensitivity would occur.

Reconciliation of changes in gross carrying/nominal amount and allowances for loans and advances to banks and customers including loan commitments and financial guarantees

The following disclosure provides a reconciliation of the Group's gross carrying/nominal amount and allowances for loans and advances to banks and customers including loan commitments and financial guarantees.

The transfers of financial instruments represents the impact of stage transfers upon the gross carrying/nominal amount and associated allowance for ECL. The net remeasurement of ECL arising from stage transfers represents the increase or decrease due to these transfers, for example, moving from a 12-month (stage 1) to a lifetime (stage 2) ECL measurement basis. Net remeasurement excludes the underlying CRR/PD movements of the financial instruments transferring stage. This is captured, along with other credit quality movements in the 'changes in risk parameters – credit quality' line item.

The 'Net new and further lending/repayments' represent the gross carrying/nominal amount and associated allowance ECL impact from volume movements within the Group's lending portfolio.

Reconciliation of changes in gross carrying/nominal amount and allowances for loans and advances to banks and customers including loan commitments and financial guarantees[1]

(Audited)

	Non credit – impaired				Credit – impaired				Total	
	Stage 1		Stage 2		Stage 3		POCI			
	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL
The group	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
At 1 Jan 2018	408,167	(452)	18,702	(618)	5,342	(1,897)	463	(74)	432,674	(3,041)
Transfers to HSBC UK and its subsidiaries	(216,026)	288	(9,502)	453	(2,711)	663	–	–	(228,239)	1,404
Transfers of financial instruments:	(5,852)	(120)	4,637	176	1,215	(56)	–	–	–	–
– Transfers from Stage 1 to Stage 2	(15,141)	38	15,141	(38)	–	–	–	–	–	–
– Transfers from Stage 2 to Stage 1	9,955	(154)	(9,955)	154	–	–	–	–	–	–
– Transfers to Stage 3	(754)	11	(941)	79	1,695	(90)	–	–	–	–
– Transfers from Stage 3	88	(15)	392	(19)	(480)	34	–	–	–	–
Net remeasurement of ECL arising from transfer of stage	–	99	–	(114)	–	(7)	–	–	–	(22)
Net new and further lending / (repayments)	19,080	(143)	(421)	239	(769)	76	(330)	11	17,560	183
Changes to risk parameters -credit quality		138		(324)		(240)		(22)		(448)
Assets written off	–	–	–	–	(456)	456	–	–	(456)	456
Foreign exchange	779	(2)	86	–	14	(8)	(1)	–	878	(10)
Others	1,597	38	772	(19)	(78)	24	(8)	7	2,283	50
At 31 Dec 2018	207,745	(154)	14,274	(207)	2,557	(989)	124	(78)	224,700	(1,428)
ECL release/(charge) for the period		94		(199)		(171)		(11)		(287)
Recoveries										71
Others										(10)
Total change in ECL for the period										(226)

	At 31 Dec 2018		12 months ended 31 Dec 2018
	Gross carrying/nominal amount	Allowance for ECL	ECL charge
	£m	£m	£m
As above	224,700	(1,428)	(226)
Other financial assets measured at amortised cost	165,525	(2)	–
Non-trading reverse purchase agreement commitments	49,911	–	–
Summary of financial instruments to which the impairment requirements in IFRS 9 are applied/Summary consolidated income statement	440,136	(1,430)	(226)
Debt instruments measured at FVOCI	47,172	(45)	79
Total allowance for ECL/total income statement ECL charge for the period	487,308	(1,475)	(147)

1 *Excludes performance guarantee contracts to which the impairment requirements in IFRS 9 are not applied.*

Credit quality

Credit quality of financial instruments

(Audited)

We assess the credit quality of all financial instruments that are subject to credit risk. The credit quality of financial instruments is a point-in-time assessment of the probability of default of financial instruments, whereas IFRS 9 stages 1 and 2 are determined based on relative deterioration of credit quality since initial recognition. Accordingly, for non-credit-impaired financial instruments, there is no direct relationship between the credit quality assessment and IFRS 9 stages 1 and 2, though typically the lower credit quality bands exhibit a higher proportion in stage 2.

The five credit quality classifications each encompass a range of granular internal credit rating grades assigned to wholesale and personal lending businesses and the external ratings attributed by external agencies to debt securities, as shown in the table on page 27. Under IAS 39, personal lending credit quality was disclosed based on expected-loss percentages. Under IFRS 9, personal lending credit quality is now disclosed based on a 12-month point-in-time PD adjusted for multiple economic scenarios. The credit quality classifications for wholesale lending are unchanged and are based on internal credit risk ratings.

Distribution of financial instruments by credit quality

(Audited)

	Gross carrying/notional amount							
	Strong	Good	Satisfactory	Sub-standard	Credit impaired	Total	Allowance for ECL	Net
The group	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
In-scope for IFRS 9								
Loans and advances to customers held at amortised cost	45,870	31,451	30,141	3,483	2,361	113,306	(1,342)	111,964
– personal	15,579	5,266	2,346	185	527	23,903	(206)	23,697
– corporate and commercial	20,868	23,016	25,342	3,072	1,760	74,058	(1,106)	72,952
– non-bank financial institutions	9,423	3,169	2,453	226	74	15,345	(30)	15,315
Loans and advances to banks held at amortised cost	11,735	1,536	355	5	–	13,631	(3)	13,628
Cash and balances at central banks	51,965	–	35	14	–	52,014	(1)	52,013
Items in the course of collection from other banks	839	–	–	–	–	839	–	839
Reverse repurchase agreements – non-trading	67,748	8,017	4,337	–	–	80,102	–	80,102
Financial investments	5	–	8	–	–	13	–	13
Prepayments, accrued income and other assets	31,885	486	444	7	5	32,827	(1)	32,826
– endorsements and acceptances	93	14	7	–	1	115	(1)	114
– accrued income and other	31,792	472	437	7	4	32,712	–	32,712
Debt instruments measured at fair value through other comprehensive income[1]	42,363	2,084	606	597	9	45,659	(45)	45,614
Out-of-scope for IFRS 9								
Trading assets	42,274	9,924	7,088	876	–	60,162	–	60,162
Other financial assets designated and otherwise mandatorily measured at fair value through profit or loss	2,633	1,362	4,136	2	–	8,133	–	8,133
Derivatives	122,695	17,115	4,229	451	32	144,522	–	144,522
Total gross carrying amount on balance sheet	420,012	71,975	51,379	5,435	2,407	551,208	(1,392)	549,816
Percentage of total credit quality	78%	15%	6%	1%	–	100%		
Loan and other credit-related commitments	96,522	31,393	12,821	630	254	141,620	(66)	141,554
Financial guarantees	3,390	1,456	948	194	66	6,054	(17)	6,037
In-scope: Irrevocable loan commitments and financial guarantees	99,912	32,849	13,769	824	320	147,674	(83)	147,591
Loan and other credit-related commitments[2]	7,275	–	–	–	–	7,275	–	7,275
Performance and other guarantees	8,631	5,236	2,682	592	103	17,244	(37)	17,207
Out-of-scope: Revocable loan commitments and non-financial guarantees	15,906	5,236	2,682	592	103	24,519	(37)	24,482

1 For the purposes of this disclosure gross carrying value is defined as the amortised cost of a financial asset, before adjusting for any loss allowance. As such the gross carrying value of debt instruments at FVOCI as presented above will not reconcile to the balance sheet as it excludes fair value gains and losses.

2 Revocable loan and other commitments of £7.3bn which are out-of-scope of IFRS 9 are presented within the strong credit quality classification.

Distribution of financial instruments by credit quality

(Audited)

The bank	Gross carrying/notional amount Strong £m	Good £m	Satisfactory £m	Sub-standard £m	Credit impaired £m	Total £m	Allowance for ECL £m	Net £m
In-scope for IFRS 9								
Loans and advances to customers held at amortised cost	23,923	17,828	15,123	1,586	1,067	59,527	(744)	58,783
– personal	1,782	695	734	14	24	3,249	(9)	3,240
– corporate and commercial	9,441	14,695	12,764	1,358	998	39,256	(685)	38,571
– non-bank financial institutions	12,700	2,438	1,625	214	45	17,022	(50)	16,972
Loans and advances to banks held at amortised cost	11,225	1,356	107	1	—	12,689	(3)	12,686
Cash and balances at central banks	40,657	—	—	—	—	40,657	–	40,657
Items in the course of collection from other banks	442	—	—	—	—	442	–	442
Reverse repurchase agreements – non-trading	48,220	6,668	1,607	—	—	56,495	–	56,495
Financial investments	—	—	—	—	—	—	–	—
Prepayments, accrued income and other assets	26,653	170	122	1	4	26,950	(1)	26,949
– endorsements and acceptances	67	14	—	—	1	82	(1)	81
– accrued income and other	26,586	156	122	1	3	26,868	–	26,868
Debt instruments measured at fair value through other comprehensive income[1]	26,272	40	12	2	3	26,329	(6)	26,323
Out-of-scope for IFRS 9								
Trading assets	28,973	7,379	6,873	845	—	44,070	–	44,070
Other financial assets designated and otherwise mandatorily measured at fair value through profit or loss	303	939	3,800	2	—	5,044	–	5,044
Derivatives	120,848	14,240	3,684	427	30	139,229	–	139,229
Total gross carrying amount on balance sheet	327,516	48,620	31,328	2,864	1,104	411,432	(754)	410,678
Percentage of total credit quality	79%	12%	8%	1%	—	100%		
Loan and other credit-related commitments	37,245	14,927	8,499	379	146	61,196	(50)	61,146
Financial guarantees	4,448	598	383	96	53	5,578	(14)	5,564
In-scope: Irrevocable loan commitments and financial guarantees	41,693	15,525	8,882	475	199	66,774	(64)	66,710
Loan and other credit-related commitments[2]	4,742	—	—	—	—	4,742	—	4,742
Performance and other guarantees	5,231	2,458	2,193	374	67	10,323	(27)	10,296
Out-of-scope: Revocable loan commitments and non-financial guarantees	9,973	2,458	2,193	374	67	15,065	(27)	15,038

1 *For the purposes of this disclosure gross carrying value is defined as the amortised cost of a financial asset, before adjusting for any loss allowance. As such the gross carrying value of debt instruments at FVOCI as presented above will not reconcile to the balance sheet as it excludes fair value gains and losses.*
2 *Revocable loan and other commitments of £4.7bn which are out-of-scope of IFRS 9 are presented within the strong credit quality classification.*

Distribution of financial instruments to which the impairment requirements in IFRS 9 are applied, by credit quality and stage distribution

(Audited)

	Gross carrying/notional amount							
	Strong	Good	Satisfactory	Sub-standard	Credit impaired	Total	Allowance for ECL	Net
The group	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Loans and advances to customers at amortised cost	**45,870**	**31,451**	**30,141**	**3,483**	**2,361**	**113,306**	**(1,342)**	**111,964**
– stage 1	45,858	29,662	24,835	1,774	–	102,129	(121)	102,008
– stage 2	12	1,789	5,306	1,709	–	8,816	(171)	8,645
– stage 3	–	–	–	–	2,244	2,244	(972)	1,272
– POCI	–	–	–	–	117	117	(78)	39
Loans and advances to banks at amortised cost	**11,735**	**1,536**	**355**	**5**	**–**	**13,631**	**(3)**	**13,628**
– stage 1	11,727	1,483	350	5	–	13,565	(2)	13,563
– stage 2	8	53	5	–	–	66	(1)	65
– stage 3	–	–	–	–	–	–	–	–
– POCI	–	–	–	–	–	–	–	–
Other financial assets measured at amortised cost	**152,293**	**8,491**	**4,717**	**19**	**5**	**165,525**	**(2)**	**165,523**
– stage 1	152,293	8,477	4,710	16	–	165,496	(1)	165,495
– stage 2	–	14	7	3	–	24	–	24
– stage 3	–	–	–	–	5	5	(1)	4
– POCI	–	–	–	–	–	–	–	–
Loan and other credit-related commitments	**96,522**	**31,393**	**12,821**	**630**	**254**	**141,620**	**(66)**	**141,554**
– stage 1	96,507	30,452	9,515	65	–	136,539	(27)	136,512
– stage 2	15	941	3,306	565	–	4,827	(26)	4,801
– stage 3	–	–	–	–	249	249	(13)	236
– POCI	–	–	–	–	5	5	–	5
Financial guarantees[1]	**3,390**	**1,456**	**948**	**194**	**66**	**6,054**	**(17)**	**6,037**
– stage 1	3,354	1,431	604	34	–	5,423	(4)	5,419
– stage 2	36	25	344	160	–	565	(9)	556
– stage 3	–	–	–	–	64	64	(4)	60
– POCI	–	–	–	–	2	2	–	2
At 31 Dec 2018	**309,810**	**74,327**	**48,982**	**4,331**	**2,686**	**440,136**	**(1,430)**	**438,706**
Debt instruments at FVOCI[2]								
– stage 1	42,356	2,008	329	331	–	45,024	(8)	45,016
– stage 2	7	76	277	266	–	626	(36)	590
– stage 3	–	–	–	–	6	6	(1)	5
– POCI	–	–	–	–	3	3	–	3
At 31 Dec 2018	**42,363**	**2,084**	**606**	**597**	**9**	**45,659**	**(45)**	**45,614**

1 *Excludes performance guarantee contracts to which the impairment requirements in IFRS 9 are not applied.*
2 *For the purposes of this disclosure gross carrying value is defined as the amortised cost of a financial asset, before adjusting for any loss allowance. As such the gross carrying value of debt instruments at FVOCI as presented above will not reconcile to the balance sheet as it excludes fair value gains and losses.*

Credit-impaired loans

(Audited)

The Group determines that a financial instrument is credit impaired and in stage 3 by considering relevant objective evidence, primarily whether:

- contractual payments of either principal or interest are past due for more than 90 days;
- there are other indications that the borrower is unlikely to pay such as that a concession has been granted to the borrower for economic or legal reasons relating to the borrower's financial condition; and
- the loan is otherwise considered to be in default. If such unlikeliness to pay is not identified at an earlier stage, it is deemed to occur when an exposure is 90 days past due, even where regulatory rules permit default to be defined based on 180 days past due. Therefore the definitions of credit-impaired and default are aligned as far as possible so that stage 3 represents all loans which are considered defaulted or otherwise credit-impaired.

Renegotiated loans and forbearance

The following table shows the gross carrying amounts of the group's holdings of renegotiated loans and advances to customers by industry sector and by stages. Wholesale renegotiated loans are classified as stage 3 until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, observed over a minimum one-year period, and there are no other indicators of impairment. Personal renegotiated loans are deemed to remain credit-impaired until repayment or derecognition.

Renegotiated loans and advances to customers at amortised costs by stage allocation

The group	Stage 1 £m	Stage 2 £m	Stage 3 £m	POCI £m	Total £m
Gross carrying amount					
Personal	–	–	75	–	75
– first lien residential mortgages	–	–	56	–	56
– other personal lending	–	–	19	–	19
Wholesale	394	429	568	117	1,508
– corporate and commercial	394	429	567	117	1,507
– non-bank financial institutions	–	–	1	–	1
At 31 Dec 2018	394	429	643	117	1,583
Allowance for ECL					
Personal	–	–	(14)	–	(14)
– first lien residential mortgages	–	–	(9)	–	(9)
– other personal lending	–	–	(5)	–	(5)
Wholesale	(4)	(10)	(169)	(78)	(261)
– corporate and commercial	(4)	(10)	(169)	(78)	(261)
– non-bank financial institutions	–	–	–	–	–
At 31 Dec 2018	(4)	(10)	(183)	(78)	(275)

Wholesale lending

This section provides further details on the countries and industries comprising wholesale loans and advances to customers and banks. Industry granularity is also provided by stage with geographical data presented for loans and advances to customers and banks, loan and other credit-related commitments and financial guarantees.

Total wholesale lending for loans and advances to banks and customers by stage distribution

	Gross carrying amount					Allowance for ECL				
	Stage 1	Stage 2	Stage 3	POCI	Total	Stage 1	Stage 2	Stage 3	POCI	Total
The group	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Corporate and commercial	64,822	7,476	1,643	117	74,058	(99)	(132)	(797)	(78)	(1,106)
– agriculture, forestry and fishing	187	5	10	–	202	–	–	(4)	–	(4)
– mining and quarrying	1,368	107	19	–	1,494	(4)	(3)	(2)	–	(9)
– manufacture	12,364	1,379	245	53	14,041	(23)	(19)	(100)	(33)	(175)
– electricity, gas, steam and air-conditioning supply	2,232	332	6	47	2,617	(3)	(19)	(2)	(43)	(67)
– water supply, sewerage, waste management and remediation	465	2	–	–	467	–	–	–	–	–
– construction	1,267	179	305	–	1,751	(2)	(18)	(141)	–	(161)
– wholesale and retail trade, repair of motor vehicles and motorcycles	9,331	2,654	291	11	12,287	(8)	(11)	(156)	–	(175)
– transportation and storage	5,232	563	148	–	5,943	(14)	(19)	(23)	–	(56)
– accommodation and food	1,170	28	23	2	1,223	(1)	(1)	(12)	(1)	(15)
– publishing, audiovisual and broadcasting	3,849	310	30	–	4,189	(8)	(4)	(8)	–	(20)
– real estate	7,274	410	398	1	8,083	(8)	(7)	(252)	–	(267)
– professional, scientific and technical activities	5,570	175	38	–	5,783	(3)	–	(8)	–	(11)
– administrative and support services	7,757	703	86	3	8,549	(8)	(16)	(64)	(1)	(89)
– public administration and defence, compulsory social security	562	21	–	–	583	–	(2)	–	–	(2)
– education	109	3	1	–	113	(2)	–	(1)	–	(3)
– health and care	425	29	10	–	464	(1)	(1)	(7)	–	(9)
– arts, entertainment and recreation	1,367	446	12	–	1,825	(2)	(1)	(8)	–	(11)
– other services	3,114	55	16	–	3,185	(12)	(1)	(8)	–	(21)
– activities of households	6	–	–	–	6	–	–	–	–	–
– extra-territorial organisations and bodies activities	15	–	5	–	20	–	–	(1)	–	(1)
– government	1,157	63	–	–	1,220	–	–	–	–	–
– asset-backed securities	1	12	–	–	13	–	(10)	–	–	(10)
Non-bank financial institutions	15,137	134	74	–	15,345	(13)	(12)	(5)	–	(30)
Loans and advances to banks	13,565	66	–	–	13,631	(2)	(1)	–	–	(3)
At 31 Dec 2018	93,524	7,676	1,717	117	103,034	(114)	(145)	(802)	(78)	(1,139)
By country										
UK	54,481	4,776	716	6	59,979	(69)	(100)	(354)	–	(523)
France	26,555	1,549	408	10	28,522	(18)	(16)	(298)	(3)	(335)
Germany	9,071	472	220	–	9,763	(1)	(2)	(25)	–	(28)
Other countries	3,417	879	373	101	4,770	(26)	(27)	(125)	(75)	(253)
At 31 Dec 2018	93,524	7,676	1,717	117	103,034	(114)	(145)	(802)	(78)	(1,139)

Total wholesale lending for loans and other credit-related commitments and financial guarantees[1] by stage distribution

	Nominal amount					Allowance for ECL				
	Stage 1	Stage 2	Stage 3	POCI	Total	Stage 1	Stage 2	Stage 3	POCI	Total
The group	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Corporate and commercial	68,294	4,940	307	7	73,548	(30)	(34)	(17)	—	(81)
Financial	71,621	398	2	—	72,021	(1)	(1)	—	—	(2)
At 31 Dec 2018	**139,915**	**5,338**	**309**	**7**	**145,569**	**(31)**	**(35)**	**(17)**	**—**	**(83)**
By geography										
Europe	139,915	5,338	309	7	145,569	(31)	(35)	(17)	—	(83)
of which: UK	*46,682*	*2,715*	*175*	*—*	*49,572*	*(23)*	*(29)*	*(5)*	*—*	*(57)*
of which: France	*76,550*	*1,018*	*33*	*—*	*77,601*	*(1)*	*(2)*	*(7)*	*—*	*(10)*
of which: Germany	*14,772*	*1,019*	*78*	*—*	*15,869*	*—*	*(1)*	*(4)*	*—*	*(5)*

1 *Excludes performance guarantee contracts to which the impairment requirements in IFRS 9 are not applied.*

Collateral and other credit enhancement held

(Audited)

It is the group's practice to lend on the basis of the customer's ability to meet their obligations out of their cash flow resources rather than rely on the value of security offered. Depending on the customer's standing and the type of product, facilities may be provided unsecured.For other lending a charge over collateral is obtained and considered in determining the credit decision and pricing. In the event of a default, the group may utilise the collateral as a source of repayment. Depending on its form, collateral can have a significant financial effect in mitigating exposure to credit risk.

Other corporate, commercial and financial (non-bank) loans and advances

Other corporate, commercial and financial (non-bank) loans are analysed separately in the following table, which focuses on the countries containing the majority of our loans and advances balances. For financing activities in other corporate and commercial lending, collateral value is not strongly correlated to principal repayment performance.

Collateral values are generally refreshed when an obligor's general credit performance deteriorates and we have to assess the likely performance of secondary sources of repayment should it prove necessary to rely on them.

Wholesale lending - corporate, commercial and financial (non-bank) loans and advances including loan commitments by level of collateral for key countries by stage (excluding commercial real estate)

(Audited)

			Of which:					
	Total		UK		France		Germany	
	Gross carrying/ nominal amount	ECL coverage	Gross carrying/ nominal amount	ECL coverage	Gross carrying/ nominal amount	ECL coverage	Gross carrying/ nominal amount	ECL coverage
The group	£m	%	£m	%	£m	%	£m	%
Stage 1								
Not collateralised	116,011	0.1	71,762	0.1	14,057	0.1	20,857	–
Fully collateralised	48,699	–	9,890	–	38,582		–	
LTV ratio:								
– less than 50%	2,184	0.1	1,236	0.1	868	0.1	–	–
– 51% to 75%	38,068	–	2,066	–	36,001	–	–	–
– 76% to 90%	1,013	0.1	387	–	626	–	–	–
– 91% to 100%	7,434	–	6,201	–	1,087	0.1	–	–
Partially collateralised (A):	1,834	0.1	625	–	1,161	0.1	–	–
– *collateral value on A*	343		295		33		–	
Total Stage 1	166,544	0.1	82,277	0.1	53,800	–	20,857	–
Stage 2								
Not collateralised	9,327	1.4	5,852	1.7	1,184	0.3	1,261	0.2
Fully collateralised	2,429	0.9	1,280	0.9	1,082	0.6	–	–
LTV ratio:								
– less than 50%	294	0.7	240	–	39	2.6	–	–
– 51% to 75%	1,378	0.9	426	2.8	948	0.2	–	–
– 76% to 90%	19	–	14	–	5	–	–	–
– 91% to 100%	738	0.7	600	–	90	2.2	–	–
Partially collateralised (B):	163	0.6	8	–	148	0.7	–	–
– *collateral value on B*	11		1		7		–	
Total Stage 2	11,919	1.3	7,140	1.5	2,414	0.5	1,261	0.2
Stage 3								
Not collateralised	1,450	44.3	664	48.6	286	66.4	252	11.5
Fully collateralised	226	21.2	124	6.5	67	44.8	–	–
LTV ratio:								
– less than 50%	54	42.6	15	20.0	10	100.0	–	–
– 51% to 75%	75	12.0	25	–	51	29.4	–	–
– 76% to 90%	37	16.2	34	8.8	3	100.0	–	–
– 91% to 100%	60	16.7	50	6.0	3	100.0	–	–
Partially collateralised (C):	83	42.2	33	6.1	33	72.7	–	–
– *collateral value on C*	26		21		1		–	
Total Stage 3	1,759	41.3	821	40.6	386	63.2	252	11.5
POCI								
Not collateralised	102	72.5	–	–	–	–	–	–
Fully collateralised	13	23.1	–	–	9	33.3	–	–
LTV ratio:								
– less than 50%	–	–	–	–	–	–	–	–
– 51% to 75%	13	–	–	–	9	33.3	–	–
– 76% to 90%	–	–	–	–	–	–	–	–
– 91% to 100%	–	–	–	–	–	–	–	–
Partially collateralised (D):	6	–	6	–	–	–	–	–
– *collateral value on D*	3		3		–		–	
Total POCI	121	63.6	6	–	9	33.3	–	–
At 31 Dec 2018	180,343	0.6	90,244	0.6	56,608	0.5	22,370	0.1

Other credit risk exposures

In addition to collateralised lending, other credit enhancements are employed and methods used to mitigate credit risk arising from financial assets. These are described in more detail below:

- Some securities issued by governments, banks and other financial institutions benefit from additional credit enhancement provided by government guarantees that cover the assets;
- Debt securities issued by corporates are primarily unsecured;
- Debt securities issued by banks and financial institutions include ABSs and similar instruments which are supported by underlying pools of financial assets. Credit risk associated with ABSs is reduced through the purchase of credit default swap ('CDS') protection;
- Trading assets include loans and advances held with trading intent. These mainly consist of cash collateral posted to satisfy margin requirements on derivatives, settlement accounts, reverse repos and stock borrowing. There is limited credit risk on cash collateral posted since in the event of default of the counterparty these would be set off against the related liability. Reverse repos and stock borrowing are by their nature collateralised; and
- The group's maximum exposure to credit risk includes financial guarantees and similar contracts granted as well as loan commitments that we are irrevocably committed to. Depending on the terms of the arrangement, we may have recourse to

additional credit mitigation in the event that a guarantee is called upon or a loan commitment is drawn and subsequently defaults.

Derivatives

The group participates in transactions exposing it to counterparty credit risk. Counterparty credit risk is the risk of financial loss if the counterparty to a transaction defaults before completing the satisfactory settlement of the transaction, which varies in value by reference to a market factor such as interest rate, exchange rate or asset price. It arises principally from OTC derivatives and securities financing transactions ('SFTs') and is calculated in both the trading and non-trading books.

Transactions vary in value by reference to a market factor such as interest rate, exchange rate or asset price. The counterparty risk from derivative transactions is taken into account when reporting the fair value of derivative positions. The adjustment to the fair value is known as the credit value adjustment ('CVA').

The International Swaps and Derivatives Association ('ISDA') Master Agreement is the group's preferred agreement for documenting derivatives activity. It provides the contractual framework within which dealing activity across a full range of OTC products is conducted, and contractually binds both parties to apply close-out netting across all outstanding transactions covered by an agreement if either party defaults or other pre-agreed termination events occur. It is common, and the group's preferred practice, for the parties to execute a Credit Support Annex ('CSA') in conjunction with the ISDA Master Agreement. Under a CSA, collateral is passed between the parties to mitigate the market-contingent counterparty risk inherent in the outstanding positions.

We manage the counterparty exposure arising from market risk on our OTC derivative contracts by using collateral agreements with counterparties and netting agreements. Currently, we do not actively manage our general OTC derivative counterparty exposure in the credit markets, although we may manage individual exposures in certain circumstances.

HSBC has historically placed strict policy restrictions on collateral types and as a consequence the types of collateral received and pledged are, by value, highly liquid and of a strong quality, being predominantly cash.

Where a collateral type is required to be approved outside the collateral policy (which includes collateral that includes wrong–way risks), a submission to the Documentation Approval Committee ('DAC') for approval is required. The DAC requires the participation and sign-off of senior representatives from the Global Markets Chief Operating Officer, Legal and Risk.

The majority of the counterparties with whom we have a collateral agreement are European. The majority of the group's CSAs are with financial institutional clients.

Personal lending

This section provides further details on the countries and products comprising personal loans and advances to customers.

Further product granularity is also provided by stage, with geographical data presented for loans and advances to customers, loan and other credit-related commitments, and financial guarantees.

Total personal lending for loans and advances to customers at amortised costs by stage distribution

	Gross carrying amount				Allowance for ECL			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
The group	£m	£m	£m	£m	£m	£m	£m	£m
By portfolio								
First lien residential mortgages	6,832	349	276	7,457	(4)	(8)	(81)	(93)
– *of which: interest only (including offset)*	*3,323*	*244*	*126*	*3,693*	–	*(3)*	*(32)*	*(35)*
– *affordability including ARMs*	*290*	–	–	*290*	–	–	–	–
Other personal lending	15,338	857	251	16,446	(5)	(19)	(89)	(113)
– other	14,888	818	235	15,941	(4)	(15)	(88)	(107)
– credit cards	334	39	16	389	(1)	(4)	(1)	(6)
– second lien residential mortgages	116	–	–	116	–	–	–	–
At 31 Dec 2018	22,170	1,206	527	23,903	(9)	(27)	(170)	(206)
By geography								
UK[2]	3,133	92	24	3,249	(1)	(3)	(4)	(8)
France	16,756	984	328	18,068	(3)	(17)	(102)	(122)
Germany	186	40	–	226	–	–	–	–
Other countries	2,095	90	175	2,360	(5)	(7)	(64)	(76)
At 31 Dec 2018	22,170	1,206	527	23,903	(9)	(27)	(170)	(206)

Total personal lending for loans and other credit-related commitments and financial guarantees[1] by stage distribution

	Nominal amount				Allowance for ECL			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
The group	£m	£m	£m	£m	£m	£m	£m	£m
UK	305	3	–	308	–	–	–	–
France	1,022	31	3	1,056	–	–	–	–
Germany	181	5	–	186	–	–	–	–
Other countries	539	15	1	555	–	–	–	–
At 31 Dec 2018	2,047	54	4	2,105	–	–	–	–

1 *Excludes performance guarantee contracts to which the impairment requirements in IFRS 9 are not applied.*
2 *Includes primarily first lien residential mortgages in Channel Islands, Isle of Man, Jersey and Guernsey*

Collateral on loans and advances

The following table provides a quantification of the value of fixed charges we hold over specific assets where we have a history of enforcing, and are able to enforce, collateral in satisfying a debt in the event of the borrower failing to meet its contractual obligations, and where the collateral is cash or can be realised by sale in an established market.

The collateral valuation excludes any adjustment for obtaining and selling the collateral and in particular loans shown as collateralised or partially collateralised may also benefit from other forms of credit mitigants.

Personal lending: residential mortgage loans including loan commitments by level of collateral for key countries

(Audited)

	Total		Of which: UK		Of which: France	
	Gross exposure	ECL coverage	Gross exposure	ECL coverage	Gross exposure	ECL coverage
The group	**£m**	**%**	**£m**	**%**	**£m**	**%**
Stage 1						
Fully collateralised	6,875	0.1	2,473	–	2,278	–
LTV ratio:						
– less than 50%	3,029	0.1	1,004	–	884	–
– 51% to 60%	963	–	271	–	452	–
– 61% to 70%	896	–	227	–	436	–
– 71% to 80%	823	0.1	208	–	317	–
– 81% to 90%	422	0.2	92	–	128	–
– 91% to 100%	742	–	671	–	61	–
Partially collateralised (A):	323	–	179	–	100	–
LTV ratio:						
– 101% to 110%	222	–	176	–	23	–
– 111% to 120%	26	–	1	–	16	–
– greater than 120%	75	–	2	–	61	–
– *collateral value on A*	305		177		99	
Total	7,198	0.1	2,652	–	2,378	–
Stage 2						
Fully collateralised	297	2.4	38	–	199	0.5
LTV ratio:						
– less than 50%	130	1.5	16	–	84	1.2
– 51% to 60%	46	2.2	4	–	33	–
– 61% to 70%	41	2.4	–	–	32	–
– 71% to 80%	40	5.0	–	–	30	–
– 81% to 90%	18	5.6	–	–	16	–
– 91% to 100%	22	–	18	–	4	–
Partially collateralised (B):	52	3.8	34	–	10	–
LTV ratio:						
– 101% to 110%	39	2.6	34	–	2	–
– 111% to 120%	4	–	–	–	2	–
– greater than 120%	9	11.1	–	–	6	–
– *collateral value on B*	*52*		*34*		*10*	
Total	349	–	72	–	209	–
Stage 3						
Fully collateralised	222	22.1	17	11.8	98	16.3
LTV ratio:						
– less than 50%	113	11.5	13	7.7	46	15.2
– 51% to 60%	27	18.5	–	–	15	13.3
– 61% to 70%	32	28.1	2	–	13	15.4
– 71% to 80%	20	35.0	1	–	8	25.0
– 81% to 90%	8	25.0	–	–	5	20.0
– 91% to 100%	22	59.1	1	100.0	11	18.2
Partially collateralised (C):	57	71.9	1	–	20	70.0
LTV ratio:						
– 101% to 110%	11	36.4	1	–	4	25.0
– 111% to 120%	12	50.0	–	–	4	25.0
– greater than 120%	34	91.2	–	–	12	100.0
– *collateral value on C*	*47*		*1*		*20*	
Total	279	32.3	18	11.1	118	25.4
At 31 Dec 2018	7,826	–	2,742	–	2,705	–

Supplementary information

Summary of financial instruments to which the impairment requirements in IFRS 9 are applied – by global business

	Gross carrying/nominal amount					Allowance for ECL				
	Stage 1	Stage 2	Stage 3	POCI	Total	Stage 1	Stage 2	Stage 3	POCI	Total
The group	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Loans and advances to customers at amortised cost	102,129	8,816	2,244	117	113,306	(121)	(171)	(972)	(78)	(1,342)
– RBWM	20,331	1,263	532	—	22,126	(10)	(18)	(174)	—	(202)
– CMB	26,307	2,377	867	114	29,665	(46)	(81)	(439)	(78)	(644)
– GB&M	51,279	4,870	785	2	56,936	(64)	(60)	(348)	—	(472)
– GPB	3,296	209	48	1	3,554	(1)	(1)	(11)	—	(13)
– Corporate Centre	916	97	12	—	1,025	—	(11)	—	—	(11)
Loans and advances to banks at amortised cost	13,565	66	—	—	13,631	(2)	(1)	—	—	(3)
– RBWM	2,418	4	—	—	2,422	—	—	—	—	—
– CMB	348	3	—	—	351	—	—	—	—	—
– GB&M	6,100	38	—	—	6,138	(2)	(1)	—	—	(3)
– GPB	5	—	—	—	5	—	—	—	—	—
– Corporate Centre	4,694	21	—	—	4,715	—	—	—	—	—
Other financial assets measured at amortised cost	165,496	24	5	—	165,525	(1)	—	(1)	—	(2)
– RBWM	681	2	—	—	683	—	—	—	—	—
– CMB	421	1	1	—	423	—	—	—	—	—
– GB&M	116,790	18	4	—	116,812	—	—	(1)	—	(1)
– GPB	72	—	—	—	72	—	—	—	—	—
– Corporate Centre	47,532	3	—	—	47,535	(1)	—	—	—	(1)
Total gross carrying amount on balance sheet at 31 Dec 2018	281,190	8,906	2,249	117	292,462	(124)	(172)	(973)	(78)	(1,347)
Loans and other credit-related commitments	136,539	4,827	249	5	141,620	(27)	(26)	(13)	—	(66)
– RBWM	1,725	50	3	—	1,778	—	—	—	—	—
– CMB	18,832	1,584	111	4	20,531	(4)	(4)	(11)	—	(19)
– GB&M	107,965	2,600	135	1	110,701	(23)	(22)	(2)	—	(47)
– GPB	475	593	—	—	1,068	—	—	—	—	—
– Corporate Centre[1]	7,542	—	—	—	7,542	—	—	—	—	—
Financial guarantees	5,423	565	64	2	6,054	(4)	(9)	(4)	—	(17)
– RBWM	13	—	—	—	13	—	—	—	—	—
– CMB	1,472	319	17	2	1,810	(1)	(3)	(1)	—	(5)
– GB&M	3,288	245	46	—	3,579	(3)	(6)	(3)	—	(12)
– GPB	43	1	—	—	44	—	—	—	—	—
– Corporate Centre[1]	607	—	1	—	608	—	—	—	—	—
Total nominal amount off balance sheet at 31 Dec 2018	141,962	5,392	313	7	147,674	(31)	(35)	(17)	—	(83)
RBWM	10,005	120	—	—	10,125	(5)	—	—	—	(5)
CMB	—	—	—	1	1	—	—	—	—	—
GB&M	548	—	—	—	548	—	—	—	—	—
GPB	—	—	—	—	—	—	—	—	—	—
Corporate Centre	35,998	491	6	3	36,498	(3)	(36)	(1)	—	(40)
Debt instruments measured at FVOCI at 31 Dec 2018	46,551	611	6	4	47,172	(8)	(36)	(1)	—	(45)

1 *Corporate Centre includes £4,358m and £597m of inter-company balances for 'Loans and other-credit related commitments' and 'Financial guarantees' respectively.*

Securitisation exposures and other structured products

This section contains information about our exposure to ABSs, some of which are held through consolidated structured entities ('SEs') and summarised in the table below.

Also included within this section is information on the GB&M legacy credit activities in respect of Solitaire and the securities investment conduits ('SICs'). For further information on structured entities please refer to Note 19.

Carrying amount of the group's consolidated holdings of ABSs

The group	Trading £m	Financial investments at FVOCI £m	Held at amortised cost £m	Financial assets designated and otherwise mandatorily measured at fair value through profit and loss £m	Total £m	Of which held through consolidated SEs £m
Mortgage-related assets:	1,182	360	14	99	1,655	163
– sub-prime residential	–	233	–	–	233	39
– US Alt-A residential	–	36	–	73	109	33
– other residential	723	8	3	–	734	8
– commercial property	459	83	11	26	579	83
Leveraged finance-related assets	162	31	–	16	209	156
Student loan-related assets	28	1,421	–	1	1,450	1,410
Other assets	596	287	–	5	888	160
At 31 Dec 2018	**1,968**	**2,099**	**14**	**121**	**4,202**	**1,889**

Included in the above table are securities with a carrying amount of £78m (2017: £884m) held through the SICs, excluding Solitaire, that are consolidated by the group. Although the group includes these assets in full on its balance sheet, significant first loss risks are borne by the third-party capital notes investors. The carrying amount of the capital notes liability at the year ended 31 December 2018 was £84m (2017: £182m).

The financial assets at FVOCI reserve movement in relation to these ABSs for the year was a decrease of £27m (2017: increase of £25m). The impairment write-back attributed to the group for the year was £37m (2017: write-back of £40m).

2017 credit disclosures

The below disclosures were included in the *Interim Report 2017* and the *Annual Report and Accounts 2017* and do not reflect the adoption of IFRS 9. As these tables are not directly comparable to the current 2018 credit risk tables which are disclosed on an IFRS 9 basis, the 2017 disclosures have been shown below and not adjacent to the 2018 tables.

Total personal lending

	UK £m	Continental Europe £m	Total £m	As a % of total gross loans
First lien residential mortgages	88,653	4,171	92,824	31.28
– *of which:*				
interest-only (including endowment) mortgages	*24,773*	*14*	*24,787*	*8.35*
affordability mortgages, including adjustable rate mortgages	*—*	*303*	*303*	*0.10*
Other personal lending	14,648	12,817	27,465	9.25
– personal loans and overdrafts	7,430	12,386	19,816	6.68
– credit cards	7,218	358	7,576	2.55
– second lien residential mortgages	—	73	73	0.02
– motor vehicle finance	—	—	—	—
Total gross loans at 31 Dec 2017	103,301	16,988	120,289	40.53
Impairment allowances on personal lending				
First lien residential mortgages	(108)	(86)	(194)	
Other personal lending	(192)	(51)	(243)	
– personal loans and overdrafts	(110)	(51)	(161)	
– credit cards	(82)	—	(82)	
– second lien residential mortgages	—	—	—	
– motor vehicle finance	—	—	—	
Total impairment allowances at 31 Dec 2017	(300)	(137)	(437)	

Residential mortgage loans including loan commitments by level of collateral

(Audited)

	The group	The bank
	2017	2017
	£m	£m
Non-impaired loans and advances		
Fully collateralised	96,173	90,421
LTV ratio:		
– Less than 50%	52,940	51,015
– 51% to 60%	15,989	14,954
– 61% to 70%	12,083	10,818
– 71% to 80%	9,517	8,585
– 81% to 90%	4,698	4,218
– 91% to 100%	946	831
Partially collateralised:		
greater than 100% LTV (A)	228	91
– 101% to 110%	92	27
– 111% to 120%	34	15
– greater than 120%	102	49
Collateral value on A	190	59
Impaired loans and advances		
Fully collateralised	917	725
LTV ratio:		
– Less than 50%	470	396
– 51% to 60%	175	136
– 61% to 70%	115	91
– 71% to 80%	86	56
– 81% to 90%	40	28
– 91% to 100%	31	18
Partially collateralised:		
greater than 100% LTV (B)	64	19
– 101% to 110%	28	8
– 111% to 120%	10	6
– greater than 120%	26	5
Collateral value on B	49	18
At 31 Dec	97,382	91,256

Total wholesale lending

	2017	
	£m	As a % of total gross loans
Corporate and commercial	134,513	45.32
– manufacturing	21,494	7.24
– international trade and services	47,837	16.12
– commercial real estate	18,849	6.35
– other property-related	5,908	1.99
– government	2,583	0.87
– other commercial	37,842	12.75
Financial	41,991	14.15
– non-bank financial institutions	27,842	9.38
– banks	14,149	4.77
Gross loans at 31 Dec	176,504	59.47
Impairment allowances on wholesale lending		
Corporate and commercial	(1,671)	
– manufacturing	(226)	
– international trade and services	(497)	
– commercial real estate	(268)	
– other property-related	(256)	
– government	(2)	
– other commercial	(422)	
Financial	(134)	
– non-bank financial institutions	(134)	
– banks	—	
Impairment allowances at 31 Dec	(1,805)	
Impairment allowances % of impaired loans	41.41%	

Maximum exposure to credit risk

(Audited)

	2017		
	Maximum exposure	Offset	Exposure to credit risk (net)
The group	£m	£m	£m
Trading assets: loans and advances to banks	20,590	(97)	20,493
Trading assets: loans and advances to customers	22,520	(222)	22,298
Derivatives	143,335	(139,174)	4,161
Loans and advances to banks	14,149	(202)	13,947
Loans and advances to customers	280,402	(19,074)	261,328
Reverse repurchase agreements – non-trading	45,808	(2,748)	43,060
Total balance sheet exposure to credit risk	728,568	(161,517)	567,051
Total off-balance sheet	190,413	—	190,413
– financial guarantees[1]	15,642	—	15,642
– loan commitments and other credit-related commitments[1]	174,771	—	174,771
At 31 Dec	918,981	(161,517)	757,464
The bank	£m	£m	£m
Trading assets: loans and advances to banks	17,744	(97)	17,647
Trading assets: loans and advances to customers	22,254	(222)	22,032
Derivatives	135,236	(121,736)	13,500
Loans and advances to banks	15,160	—	15,160
Loans and advances to customers	220,450	(19,024)	201,426
Reverse repurchase agreements – non-trading	36,627	(342)	36,285
Total balance sheet exposure to credit risk	588,080	(141,421)	446,659
Total off-balance sheet	109,033	—	109,033
– financial guarantees	9,219	—	9,219
– loan commitments and other credit-related commitments	99,814	—	99,814
At 31 Dec	697,113	(141,421)	555,692

1 *31 December 2017 balances have been restated to include £32.5bn of loan commitments (unsettled reverse repurchase agreements) and £2.3bn of performance and other guarantees not previously identified for disclosure.*

Gross loans and advances to customers by industry sector

	2017	
	Gross loans and advances to customers	Gross loans by industry sector as a % of total gross loans to customers
The group	£m	%
Personal	120,289	42.56
Corporate and commercial	134,513	47.59
Financial	27,842	9.85
Total gross loans and advances to customers at 31 Dec	282,644	100.00
The bank		
Personal	97,248	43.80
Corporate and commercial	89,549	40.34
Financial	35,214	15.86
Total gross loans and advances to customers at 31 Dec	222,011	100.00

Distribution of financial instruments by credit quality

(Audited)

	2017								
	Neither past due nor impaired								
	Strong	Good	Satisfactory	Sub-standard	Past due not impaired	Impaired	Total gross amount	Impairment allowances	Total
The group	£m	£m	£m	£m	£m	£m	£m	£m	£m
Cash and balances at central banks	97,601	—	—	—	—	—	97,601	—	97,601
Items in the course of collection from other banks	2,023	—	—	—	—	—	2,023	—	2,023
Trading assets	57,965	11,279	12,132	1,218	—	—	82,594	—	82,594
– treasury and other eligible bills	775	252	139	782	—	—	1,948	—	1,948
– debt securities	29,038	3,577	4,744	177	—	—	37,536	—	37,536
– loans and advances to banks	12,980	4,207	3,385	18	—	—	20,590	—	20,590
– loans and advances to customers	15,172	3,243	3,864	241	—	—	22,520	—	22,520
Financial assets designated at fair value	898	118	24	—	—	—	1,040	—	1,040
Derivatives	122,547	17,143	3,113	532	—	—	143,335	—	143,335
Loans and advances to customers held at amortised cost	157,147	56,744	57,092	4,871	973	5,817	282,644	(2,242)	280,402
– personal	109,224	5,687	2,860	453	607	1,458	120,289	(437)	119,852
– corporate and commercial	30,262	45,954	49,458	4,266	355	4,218	134,513	(1,671)	132,842
– non-bank financial institutions	17,661	5,103	4,774	152	11	141	27,842	(134)	27,708
Loans and advances to banks held at amortised cost	11,509	1,651	982	7	—	—	14,149	—	14,149
Reverse repurchase agreements – non-trading	36,667	4,563	4,274	304	—	—	45,808	—	45,808
Financial investments	51,478	3,271	1,132	920	—	537	57,338	—	57,338
Other assets	2,118	609	1,358	185	4	4	4,278	—	4,278
At 31 Dec	539,953	95,378	80,107	8,037	977	6,358	730,810	(2,242)	728,568
Percentage of total gross amount	73.8%	13.1%	11.0%	1.1%	0.1%	0.9%	100.0%		

	2017								
	Neither past due nor impaired								
	Strong	Good	Satisfactory	Sub-standard	Past due not impaired	Impaired	Total gross amount	Impairment allowances	Total
The bank	£m	£m	£m	£m	£m	£m	£m	£m	£m
Cash and balances at central banks	81,358	—	—	—	—	—	81,358	—	81,358
Items in the course of collection from other banks	1,407	—	—	—	—	—	1,407	—	1,407
Trading assets	43,271	9,643	9,578	1,218	—	—	63,710	—	63,710
– treasury and other eligible bills	458	—	139	782	—	—	1,379	—	1,379
– debt securities	15,251	3,313	3,592	177	—	—	22,333	—	22,333
– loans and advances to banks	12,493	3,208	2,025	18	—	—	17,744	—	17,744
– loans and advances to customers	15,069	3,122	3,822	241	—	—	22,254	—	22,254
Derivatives	116,791	15,017	2,915	513	—	—	135,236	—	135,236
Loans and advances to customers held at amortised cost	133,341	38,408	41,835	3,735	488	4,204	222,011	(1,561)	220,450
– personal	91,589	2,688	1,175	390	451	955	97,248	(307)	96,941
– corporate and commercial	15,126	31,551	36,528	3,199	37	3,108	89,549	(1,100)	88,449
– non-bank financial institutions	26,626	4,169	4,132	146	—	141	35,214	(154)	35,060
Loans and advances to banks held at amortised	13,273	1,204	682	1	—	—	15,160	—	15,160
Reverse repurchase agreements – non-trading	30,807	2,914	2,605	301	—	—	36,627	—	36,627
Financial investments	29,607	1,034	42	291	—	1	30,975	—	30,975
Other assets	2,146	581	426	4	—	—	3,157	—	3,157
At 31 Dec	452,001	68,801	58,083	6,063	488	4,205	589,641	(1,561)	588,080
	%	%	%	%	%	%	%		
Percentage of total gross amount	76.6	11.7	9.9	1.0	0.1	0.7	100.0		

Ageing analysis of days past due but not impaired gross financial instruments

(Audited)

The group	Up to 29 days £m	30-59 days £m	60-89 days £m	90-179 days £m	Over 180 days £m	Total £m
Loans and advances held at amortised cost	726	161	86	—	—	973
– personal	426	116	65	—	—	607
– corporate and commercial	291	43	21	—	—	355
– financial	9	2	—	—	—	11
Other assets	4	—	—	—	—	4
At 31 Dec 2017	730	161	86	—	—	977
The bank						
Loans and advances held at amortised cost	340	93	55	—	—	488
– personal	312	87	52	—	—	451
– corporate and commercial	28	6	3	—	—	37
– financial	—	—	—	—	—	—
Other assets	—	—	—	—	—	—
At 31 Dec 2017	340	93	55	—	—	488

Loan impairment charges and other credit risk provisions

	2017 £m
Net impairment charge on loans and advances	(624)
Release of impairment on available-for-sale debt securities	145
Other credit risk provisions	(16)
Total	(495)

Impaired loans and advances to customers and banks by industry sector

(Audited)

	2017		
	Individually assessed £m	Collectively assessed £m	Total £m
Banks	—	—	—
Customers	5,365	452	5,817
– personal	1,061	397	1,458
– corporate and commercial	4,163	55	4,218
– financial	141	—	141
At 31 Dec	5,365	452	5,817

Renegotiated loans and advances to customers by industry sector

	2017				
	Residential mortgages £m	Other personal lending £m	Corporate and commercial £m	Non-bank financial institutions £m	Total £m
Neither past due nor impaired	252	57	1,203	6	1,518
Past due not impaired	33	6	42	—	81
Impaired	211	71	2,165	136	2,583
Renegotiated loans at 31 Dec	496	134	3,410	142	4,182
Impairment allowance on renegotiated loans					(684)

Loan impairment charge to the income statement by industry sector

	2017
	£m
Personal	120
– residential mortgages	7
– other personal	113
Corporate and commercial	454
– manufacturing and international trade and services	227
– commercial real estate and other property-related	149
– other commercial	78
Financial	50
Total loan impairment charge for the year ended 31 Dec	624
Individually assessed impairment allowances	529
– new allowances	919
– release of allowances no longer required	(366)
– recoveries of amounts previously written off	(24)
Collectively assessed impairment allowances	95
– new allowances net of allowance releases	327
– recoveries of amounts previously written off	(232)
Total loan impairment charge for the year ended 31 Dec	624

Movement in impairment allowances on loans and advances to customers and banks

(Audited)

	Banks	Customers		
	Individually assessed	Individually assessed	Collectively assessed	Total
The group	£m	£m	£m	£m
At 1 Jan 2017	—	1,729	828	2,557
Amounts written off	—	(310)	(173)	(483)
Recoveries of loans and advances written off in previous years	—	14	96	110
Loan impairment charge	—	10	31	41
Exchange and other movements	—	(53)	(236)	(289)
At 30 June 2017	—	1,390	546	1,936
As a percentage of gross loans and advances[1]	—	0.50%	0.20%	0.65%
At 1 July 2017	—	1,390	546	1,936
Amounts written off	—	(243)	(185)	(428)
Recoveries of loans and advances written off in previous years	—	10	136	146
Loan impairment charge	—	519	64	583
Exchange and other movements	—	1	4	5
At 31 Dec 2017	—	1,677	565	2,242
As a percentage of gross loans and advances[1]		0.59%	0.20%	0.76%

1 *Net of reverse repo transactions, settlement accounts and stock borrowings.*

	2017			
	Banks	Customers		
	Individually assessed	Individually assessed	Collectively assessed	Total
The bank	£m	£m	£m	£m
At 1 Jan	—	1,074	475	1,549
Amounts written off	—	(345)	(308)	(653)
Recoveries of loans and advances written off in previous years	—	20	201	221
Loan impairment charge	—	347	84	431
Exchange and other movements	—	1	12	13
At 31 Dec	—	1,097	464	1,561
as a percentage of gross loans and advances[1]	—	0.49%	0.21%	0.66%

1 *Net of reverse repo transactions, settlement accounts and stock borrowings.*

Carrying amount of consolidated holdings of ABS

	Trading	Available-for-sale	Loans and receivables	Total[1]	Of which held through consolidated SEs
	£m	£m	£m	£m	£m
Mortgage-related assets:					
– sub-prime residential	4	679	24	707	358
– US Alt-A residential	—	778	—	778	771
– other residential	603	134	816	1,553	56
– commercial property	444	198	41	683	167
Leveraged finance-related assets	38	276	—	314	209
Student loan-related assets	29	1,627	—	1,656	1,597
Other assets	573	455	1	1,029	317
At 31 Dec 2017	1,691	4,147	882	6,720	3,475

1 *The asset-backed securities are primarily US Dollar ('USD') denominated. Principal carrying amounts are converted into sterling ('GBP') at the prevailing exchange rates at 31 December 2017: 1GBP : USD 1.351.*

Liquidity and funding risk in 2018

Liquidity coverage ratio

The Liquidity Coverage Ratio ('LCR') aims to ensure that a bank has sufficient unencumbered high-quality liquid assets ('HQLA') to meet its liquidity needs in a 30-calendar-day liquidity stress scenario. HQLA consist of cash or assets that can be converted into cash at little or no loss of value in markets.

At 31 December 2018, all the group's principal operating entities were within the LCR risk tolerance level established by the Board and applicable under the LFRF.

The following table displays the individual LCR levels for HSBC Bank Plc's principal operating entities on an EC LCR Delegated Regulation basis.

Operating entities' LCRs

		At	
		31 Dec 2018	31 Dec 2017
	Footnotes	**%**	%
HSBC Bank Plc	*1,2*	**147**	139
HSBC France		**128**	149
HSBC Trinkaus & Burkhardt AG		**111**	114

1 *2017 figures are for HSBC UK Liquidity Group which comprises: HSBC Bank plc (pre ring-fencing), Marks and Spencer Financial Services plc, HSBC Trust Company (UK) Limited and Private Bank (UK) Limited.*
2 *2018 LCR is higher than 2017, as we carry surplus liquidity in preparation for the UK's withdrawal from the EU.*

Net stable funding ratio

The Net Stable Funding Ratio ('NSFR') requires institutions to maintain sufficient stable funding relative to required stable funding, and reflects a bank's long-term funding profile (funding with a term of more than a year). It is designed to complement the LCR.

At 31 December 2018, all the group's principal operating entities were within the NSFR risk tolerance level established by the Board and applicable under the LFRF.

The table below displays the NSFR levels for the principal operating entities on a BCBS 295 basis.

Operating entities' NSFRs

		At	
		31 Dec 2018	31 Dec 2017
	Footnotes	**%**	%
HSBC Bank Plc	*1*	**113**	108
HSBC France		**113**	116
HSBC Trinkaus & Burkhardt AG		**116**	117

1 *In adopting the NSFR (BCBS 295) as a key internal risk management metric, the HSBC Group has, until such time that the NSFR becomes a binding regulatory requirement on HSBC Group or the operating entity locally, permitted entities to reduce the amount of Required Stable Funding Requirement (RSF) for listed equities where the valuation risk has been hedged through an exchange traded daily cash margined derivative, due to management's view as to the speed at which these assets could be monetised under stress and the mitigation of the valuation risk. HSBC Bank Plc is applying a lower RSF to such equities.*

Depositor concentration and term funding maturity concentration

The LCR and NSFR metrics assume a stressed outflow based on a portfolio of depositors within each deposit segment. The validity of these assumptions is undermined if the underlying depositors do not represent a large enough portfolio so that a depositor concentration exists.

In addition to this, operating entities are exposed to term re-financing concentration risk if the current maturity profile results in future maturities being overly concentrated in any defined period.

Liquid assets of the group's principal operating entities

The table below shows the unweighted liquidity value of assets categorised as liquid, which is used for the purposes of calculating the LCR metric. This reflects the stock of unencumbered liquid assets at the reporting date, using the regulatory definition of liquid assets.

Operating entities' liquid assets

	Estimated liquidity value	At Estimated liquidity value
	At 31 Dec 2018	31 Dec 2017
	£m	£m
HSBC Bank Plc		
Level 1	**84,185**	119,198
Level 2a	**4,243**	2,157
Level 2b	**7,764**	13,899
HSBC France		
Level 1	**15,545**	16,441
Level 2a	**435**	741
Level 2b	**24**	2
HSBC Trinkaus & Burkhardt AG		
Level 1	**5,605**	6,237
Level 2a	**60**	50
Level 2b	**520**	590

Sources of funding

Our primary sources of funding are customer current accounts, repo and wholesale securities.

The following 'Funding sources and uses' table provides a consolidated view of how our balance sheet is funded, and should be read in light of the LFRF, which requires operating entities to manage liquidity and funding risk on a stand-alone basis.

The table analyses our consolidated balance sheet according to the assets that primarily arise from operating activities and the sources of funding primarily supporting these activities. Assets and liabilities that do not arise from operating activities are presented as a net balancing source or deployment of funds.

In 2018, the level of customer accounts continued to exceed the level of loans and advances to customers. The positive funding gap was predominantly deployed in liquid assets, cash and balances with central banks and financial investments, as required by the LFRF.

Funding sources and uses for the group

	2018 £m	2017 £m
Sources		
Customer accounts	**180,836**	381,546
Deposits by banks	**24,532**	29,349
Repurchase agreements – non-trading	**46,583**	37,775
Debt securities in issue	**22,721**	13,286
Cash collateral, margin and settlement accounts	**35,561**	N/A
Liabilities of disposal groups held for sale	**—**	454
Subordinated liabilities	**13,770**	16,494
Financial liabilities designated at fair value	**36,922**	18,249
Liabilities under insurance contracts	**20,657**	21,033
Trading liabilities	**49,514**	106,496
– repos	**1,027**	1,182
– stock lending	**9,161**	21,156
– settlement accounts	**N/A**	2,959
– other trading liabilities	**39,326**	81,199
Total equity	**27,409**	44,049
At 31 Dec	**458,505**	668,731

	2018 £m	2017 £m
Uses		
Loans and advances to customers	**111,964**	280,402
Loans and advances to banks	**13,628**	14,149
Reverse repurchase agreements – non-trading	**80,102**	45,808
Cash collateral, margin and settlement accounts	**28,870**	N/A
Assets held for sale	**37**	461
Trading assets	**95,420**	145,725
– reverse repos	**6,141**	5,987
– stock borrowing	**6,498**	5,189
– settlement accounts	**N/A**	4,947
– other trading assets	**82,781**	129,602
Financial investments	**47,272**	58,000
Cash and balances with central banks	**52,013**	97,601
Net deployment in other balance sheet assets and liabilities	**29,199**	26,585
At 31 Dec	**458,505**	668,731

Contingent liquidity risk arising from committed lending facilities

The group provides customers with committed facilities such as standby facilities to corporate customers and committed backstop lines to conduits sponsored by the group. All of the undrawn commitments provided to conduits or external customers are accounted for in the LCR and NSFR in line with the applicable regulations. This ensures that under a stress scenario any additional outflow generated by increased utilisation of these committed facilities by either customers or the group's sponsored conduits will not give rise to liquidity risk for the group.

Since the group controls the size of the portfolio of securities held by these conduits, no contingent liquidity risk exposure arises as a result of these undrawn committed lending facilities. In relation to commitments to customers, the table below shows the level of undrawn commitments outstanding in terms of the five largest single facilities and the largest market sector.

The group's contractual exposures at 31 December monitored under the contingent liquidity risk limit structure

	Footnotes	2018 £bn	2017 £bn
Commitments to conduits			
Consolidated multi-seller conduits	1		
– total lines		**5.6**	6.8
– largest individual lines		**0.3**	0.6
Consolidated securities investment conduits – total lines		**3.4**	3.4
Commitments to customers			
– five largest	2	**3.0**	2.5
– largest market sector	3	**9.1**	19.0

1 *Exposures relate to the Regency multi-seller conduit. This vehicle provides funding to group customers by issuing debt secured by a diversified pool of customer-originated assets.*
2 *Represents the undrawn balance for the five largest committed liquidity facilities provided to customers, other than those facilities to conduits.*
3 *Represents the undrawn balance for the total of all committed liquidity facilities provided to the largest market sector, other than those facilities to conduits.*

Asset encumbrance and collateral management

An asset is defined as encumbered if it has been pledged as collateral against an existing liability and, as a result, is no longer available to the group to secure funding, satisfy collateral needs or be sold to reduce the funding requirement. Collateral is managed on an operating entity basis consistent with the approach to managing liquidity and funding. Available collateral held in an operating entity is managed as a single consistent collateral pool from which each operating entity will seek to optimise the use of the available collateral. The objective of this disclosure is to facilitate an understanding of available and unrestricted assets that could be used to support potential future funding and collateral needs. The disclosure is not designed to identify assets which would be available to meet the claims of creditors or to predict assets that would be available to creditors in the event of a resolution or bankruptcy.

Summary of assets available to support potential future funding and collateral needs (on- and off-balance sheet)

	2018	2017
	£m	£m
Total on-balance sheet assets at 31 Dec	**604,958**	818,868
Less:		
– reverse repo/stock borrowing receivables and derivative assets	**(237,020)**	(200,319)
– other assets that cannot be pledged as collateral	**(56,982)**	(79,306)
Total on-balance sheet assets that can support funding and collateral needs at 31 Dec	**310,956**	539,243
Add: off-balance sheet assets		
– fair value of collateral received in relation to reverse repo/stock borrowing/derivatives that is available to sell or repledge	**250,277**	173,386
Total assets that can support future funding and collateral needs	**561,233**	712,629
Less:		
– on-balance sheet assets pledged	**(89,123)**	(88,768)
– re-pledging of off-balance sheet collateral received in relation to reverse repo/stock borrowing/derivatives	**(202,782)**	(130,430)
Assets available to support funding and collateral needs at 31 Dec	**269,328**	493,431

Market risk in 2018

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

There were no material changes to our policies and practices for the management of market risk in 2018.

Exposure to market risk is separated into two portfolios.

Trading portfolios comprise positions arising from market-making and warehousing of customer-derived positions.

Non-trading portfolios including BSM comprise positions that primarily arise from the interest rate management of the group's retail and commercial banking assets and liabilities, financial investments designated as as held-to-collect-and-sale ('HTCS'), and exposures arising from the group's insurance operations.

Trading portfolios

Value at risk of the trading portfolios

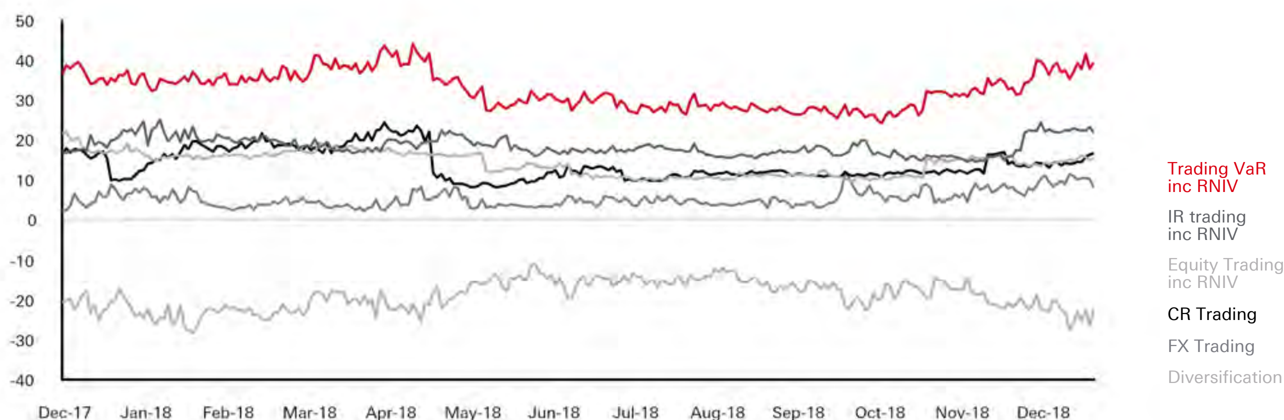
(Audited)

Trading VaR predominantly resides within Global Markets where it was £39.5m at 31 December 2018 compared with £36.3m at 31 December 2017. The Total Trading VaR moderately increased during the first half of 2018 and suddenly decreased in May 2018 following a change of methodology in HBFR to assess the shocks to apply on credit spreads. Both the Total Trading VaR and Credit VaR remained relatively stable until the last quarter of 2018. In December 2018, the IR Trading VaR increased from £17m to £22m following a change of positions, which resulted in an increase of the total trading VaR. The change in Equity Trading VaR was from fluctuations in dividend and correlation exposures.

The ALCO-trading book has been included in this exercise, which was not the case last year.

The long protection position held in the book against a Sterling devaluation for a future capital injection into HBFR results in a decrease of the FX Trading VaR since November 2018. The daily levels of Total Trading VaR over the past year are set out in the graph below.

Daily VaR (trading portfolios), 99% 1 day (£m)



The group's trading VaR for the year is shown in the table below.

Trading VaR, 99% 1 day

(Audited)

	Foreign exchange (FX) and commodity	Interest rate (IR)	Equity (EQ)	Credit Spread (CS)	Portfolio Diversification[1]	Total[2]
	£m	£m	£m	£m	£m	£m
Balance at 31 Dec 2018	**7.9**	**21.7**	**15.4**	**16.6**	**(22.0)**	**39.6**
Average	**5.2**	**18.4**	**14.1**	**13.9**	**(19.0)**	**32.6**
Maximum	**11.7**	**25.1**	**22.1**	**24.3**		**44.0**
Minimum	**2.1**	**14.5**	**9.6**	**8.1**		**24.1**
Balance at 31 Dec 2017	2.1	17.1	21.4	16.2	(20.5)	36.3
Average	5.2	25.3	12.0	9.2	(19.1)	32.6
Maximum	15.3	52.3	21.4	17.4		53.4
Minimum	0.9	17.1	7.5	3.4		26.2

1 *Portfolio diversification is the market risk dispersion effect of holding a portfolio containing different risk types. It represents the reduction in unsystematic market risk that occurs when combining a number of different risk types, for example, interest rate, equity and foreign exchange, together in one portfolio. It is measured as the difference between the sum of the VaR by individual risk type and the combined total VaR. A negative number represents the benefit of portfolio diversification. As the maximum occurs on different days for different risk types, it is not meaningful to calculate a portfolio diversification benefit for this measure.*

2 *The total VaR is non-additive across risk types due to diversification effect and it includes VaR RNIV.*

Back-testing

In 2018, the group experienced two back-testing exceptions, one against hypothetical loss and one against actual loss. There was no evidence of model failure or control error.

Non-trading portfolios

Value at risk of the non-trading portfolios

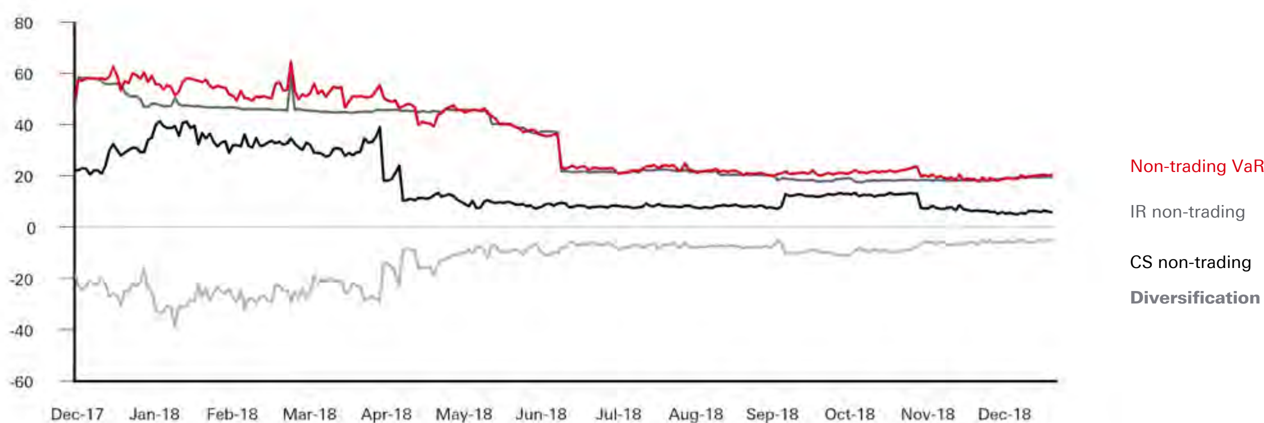
(Audited)

Following the go live of the ring-fenced bank HSBC UK on 1 July, the non-trading VaR of our London Balance Sheet Management (BSM) desk dropped by £19m. This is to reflect the legal transfer of certain positions into HSBC UK. These positions were made up of ALCM buy in for the management of the structural interest rate risk (50% of the risk transferred to the combined to the bank), the existing cash flow hedge (CFH) positions referencing transferred asset pools and the high quality liquid asset (HQLA) (and corresponding hedges) purchased to form part of the newly formed HSBC UK Liquid Asset Buffer (LAB).

Our non trading ALCO books have been included in the non trading VaR. They contain capital issuances for the group (including TLAC) and any corresponding hedges. This resulted in an average decrease of the non trading VaR by £6m.

The daily levels of total non-trading VaR over the last year are set out in the graph below.

Daily VaR (non-trading portfolios), 99% 1 day (£m)



The group's non-trading VaR for the year is shown in the table below.

Non-trading VaR, 99% 1 day

(Audited)

	Interest rate (IR)	Credit spread (CS)	Portfolio diversification	Total
	£m	£m	£m	£m
Balance at 31 Dec 2018	**19.4**	**5.7**	**(4.6)**	**20.5**
Average	**32.8**	**16.4**	**(13.7)**	**35.5**
Maximum	**59.3**	**41.3**		**64.6**
Minimum	**17.4**	**4.9**		**17.7**
Balance at 31 Dec 2017	45.8	22.1	(17.8)	50.1
Average	64.1	29.3	(23.6)	69.8
Maximum	92.0	53.4		91.2
Minimum	44.8	9.3		47.7

Structural foreign exchange exposures

The group's structural foreign currency exposure is represented by the net asset value of its foreign currency equity and subordinated debt investments in subsidiary undertakings, branches, joint ventures and associates.

For our policies and procedures for managing structural foreign exchange exposures, see page 30 of the 'Risk management' section.

Net structural foreign exchange exposures

	2018	2017
	£m	£m
Currency of structural exposure		
Euro[1]	**12,866**	11,896
US Dollars[1]	**805**	648
South African rand[1]	**357**	349
Russian rouble	**197**	225
Others, each less than £150m[1]	**433**	404
At 31 Dec	**14,658**	13,522

1 *The net structural exposure at 31 December 2017 has been restated by £946m to increase the Euro (£764m), US dollar (£133m), Armenian dram (£25m), South African rand (£23m), and Swiss franc (£1m) exposures. This is due to incorrect currency classification of dotation capital to branches, elimination of subsidiaries' shareholders' equity on date of acquisition, and Additional Tier 1 instruments held in the UK.*

Operational risk in 2018

Operational risk is the risk to achieving our strategy or objectives as a result of inadequate or failed internal processes, people and systems or from external events.

Responsibility for minimising operational risk lies with HSBC's employees. They are required to manage the operational risks of the business and operational activities for which they are responsible.

A summary of our current policies and practices regarding the management of operational risk is set out on page 31.

Operational risk exposures

In 2018 we continued our ongoing work to strengthen those controls that manage our most material risks. Among other measures, we:

- further enhanced our controls to help ensure that we know our customers, ask the right questions, monitor transactions and escalate concerns to detect, prevent and deter financial crime risk;
- implemented a number of initiatives to raise our standards in relation to the conduct of our business as described on page 31 of the 'Regulatory compliance risk management' section;
- increased monitoring and enhanced detective controls to manage fraud risks which arise from new technologies and new ways of banking;
- strengthened internal security controls to help prevent cyber-attacks;
- improved controls and security to protect customers when using digital channels; and
- enhanced our third-party risk management capability to help enable the consistent risk assessment of any third-party service.

Further information on the nature of these risks is provided in 'Top and emerging risks' on page 20 and in 'Risk management' from pages 23 to 24.

Operational risk losses

Operational risk losses in 2018 are higher than in 2017. Total losses in both years were reduced by the write-back of provisions for a large conduct-related event. For further details, see Note 32 on the Financial Statements and on conduct-related costs included in significant items on page 12.

Insurance manufacturing operations risk in 2018

Our insurance manufacturing operations are subject to insurance risk and financial risk, including market risk, credit risk and liquidity risk.

A summary of our current policies and practices regarding the management of insurance risk is set out on page 33.

The group's bancassurance model

We operate an integrated bancassurance model that provides insurance products principally for customers with whom we have a banking relationship.

The insurance contracts we sell relate to the underlying needs of our banking customers, which we can identify from our point-of-sale contacts and customer knowledge. The majority of sales are of savings and investment products and term and credit life contracts.

By focusing largely on personal and SME lines of business, we are able to optimise volumes and diversify individual insurance risks.

We choose to manufacture these insurance products in HSBC subsidiaries based on an assessment of operational scale and risk appetite. Manufacturing insurance allows us to retain the risks and rewards associated with writing insurance contracts by keeping part of the underwriting profit and investment income within the bank.

We have life insurance manufacturing subsidiaries in France, Malta and the UK. Where we do not have the risk appetite or operational scale to be an effective insurance manufacturer, we engage with a handful of leading external insurance companies in order to provide insurance products to our customers through our banking network and direct channels. These arrangements are generally structured with our exclusive strategic partners and earn the bank a combination of commissions, fees and a share of profits.

Insurance products are sold through all global businesses, but predominantly by RBWM, GPB and CMB through our branches and direct channels.

Measurement

(Audited)

The risk profile of our insurance manufacturing businesses is measured using an economic capital approach. Assets and liabilities are measured on a market value basis, and a capital requirement is defined to ensure that there is a less than one-in-200 chance of insolvency over a one-year time horizon, given the risks to which the businesses are exposed. The methodology for the economic capital calculation is largely aligned to the pan-European Solvency II insurance capital regulations. The economic capital coverage ratio (economic net asset value divided by the economic capital requirement) is a key risk appetite measure. The business has a current appetite to remain above 140% with a tolerance of 110%. In addition to economic capital, the regulatory solvency ratio is also a metric used to manage risk appetite on an entity basis.

The following table shows the composition of assets and liabilities by contract type.

Balance sheet of insurance manufacturing subsidiaries by type of contract

(Audited)

	Footnotes	With DPF £m	Unit- linked £m	Other contracts[1] £m	Shareholder assets and liabilities £m	Total £m
Financial assets		**18,619**	**1,602**	**253**	**1,872**	**22,346**
– financial assets designated and otherwise mandatorily measured at fair value through profit or loss		**7,850**	**1,548**	**87**	**809**	**10,294**
– derivatives		**92**	**—**	**—**	**3**	**95**
– financial investments – at amortised cost		**182**	**—**	**—**	**6**	**188**
– financial investments – at fair value through other comprehensive income		**8,698**	**—**	**108**	**947**	**9,753**
– other financial assets	2	**1,797**	**54**	**58**	**107**	**2,016**
Reinsurance assets		**—**	**50**	**145**	**—**	**195**
PVIF	3	**—**	**—**	**—**	**652**	**652**
Other assets and investment properties		**774**	**1**	**—**	**48**	**823**
Total assets at 31 Dec 2018		**19,393**	**1,653**	**398**	**2,572**	**24,016**
Liabilities under investment contracts designated at fair value		**—**	**611**	**—**	**—**	**611**
Liabilities under insurance contracts		**19,262**	**1,041**	**354**	**—**	**20,657**
Deferred tax	4	**—**	**1**	**—**	**162**	**163**
Other liabilities		**—**	**—**	**—**	**1,294**	**1,294**
Total liabilities at 31 Dec 2018		**19,262**	**1,653**	**354**	**1,456**	**22,725**
Total equity at 31 Dec 2018		**—**	**—**	**—**	**1,291**	**1,291**
Total liabilities and equity at 31 Dec 2018		**19,262**	**1,653**	**354**	**2,747**	**24,016**
Financial assets		18,749	1,530	190	1,906	22,375
– financial assets designated at fair value		7,020	1,466	85	630	9,201
– derivatives		95	—	—	30	125
– financial investments – HTM		—	—	—	—	—
– financial investments – AFS		9,918	—	104	1,188	11,210
– other financial assets	2	1,716	64	1	58	1,839
Reinsurance assets		—	188	159	—	347
PVIF	3	—	—	—	572	572
Other assets and investment properties		784	1	1	449	1,235
Total assets at 31 Dec 2017		19,533	1,719	350	2,927	24,529
Liabilities under investment contracts designated at fair value		—	548	—	—	548
Liabilities under insurance contracts		19,533	1,166	334	—	21,033
Deferred tax	4	—	5	—	156	161
Other liabilities		—	—	—	1,561	1,561
Total liabilities at 31 Dec 2017		19,533	1,719	334	1,717	23,303
Total equity at 31 Dec 2017		—	—	—	1,226	1,226
Total liabilities and equity at 31 Dec 31 Dec 2017		19,533	1,719	334	2,943	24,529

1 *'Other contracts' includes term assurance and credit life insurance.*
2 *Comprise mainly loans and advances to banks, cash and intercompany balances with other non-insurance legal entities.*
3 *Present value of in-force long-term insurance business.*
4 *'Deferred tax' includes the deferred tax liabilities arising on recognition of PVIF.*

Key risk types

The key risks for the insurance operations are market risks (in particular interest rate and equity) and credit risks, followed by insurance underwriting risks and operational risks. Liquidity risk, whilst significant for the bank, is minor for our insurance operations.

Market risk

(Audited)

Description and exposure

Market risk is the risk of changes in market factors affecting the bank's capital or profit. Market factors include interest rates, equity and growth assets and foreign exchange rates.

Our exposure varies depending on the type of contract issued. Our most significant life insurance products are investment contracts with discretionary participating features ('DPF') issued in France. These products typically include some form of capital guarantee or guaranteed return on the sums invested by the policyholders, to which discretionary bonuses are added if allowed by the overall performance of the funds. These funds are primarily invested in bonds with a proportion allocated to other asset classes, to provide customers with the potential for enhanced returns.

DPF products expose the bank to the risk of variation in asset returns, which will impact our participation in the investment performance. In addition, in some scenarios the asset returns can become insufficient to cover the policyholders' financial guarantees, in which case the shortfall has to be met by the bank. Reserves are held against the cost of such guarantees, calculated by stochastic modelling.

Where local rules require, these reserves are held as part of liabilities under insurance contracts. Any remainder is accounted for as a deduction from the present value of in-force 'PVIF' long-term insurance contracts. The table below shows the total reserve held for the cost of guarantees, the range of investment returns on assets supporting these products and the implied investment return that would enable the business to meet the guarantees.

The financial guarantees offered on some portfolios exceeded the current yield on the assets that back them.

For unit-linked contracts, market risk is substantially borne by the policyholder, but some market risk exposure typically remains as fees earned are related to the market value of the linked assets.

Financial return guarantees

(Audited)

		2018			2017		
		Investment returns implied by guarantee	**Long-term investment returns on relevant portfolios**	**Cost of guarantees**	Investment returns implied by guarantee	Long-term investment returns on relevant portfolios	Cost of guarantees
	Footnotes	**%**	**%**	**£m**	%	%	£m
Capital		**–**	**1.5 - 2.7**	**73**	0.0	3.2	67
Nominal annual return	1	**2.6**	**2.7**	**73**	2.6	3.2	80
Nominal annual return		**4.5**	**2.7**	**45**	4.5	3.2	44
At 31 Dec				**191**			191

1 *A block of contracts in France with guaranteed nominal annual returns in the range 1.25%-3.72% are reported in line with the average guaranteed return of 2.6% (2017: 2.6%) offered to policyholders on these contracts.*

Sensitivities

The following table illustrates the effects of selected interest rate and equity price scenarios on our profit for the year and the total equity of our insurance manufacturing subsidiaries.

Where appropriate, the effects of the sensitivity tests on profit after tax and equity incorporate the impact of the stress on the PVIF. Due in part to the impact of the cost of guarantees and hedging strategies which may be in place, the relationship between the profit and total equity and the risk factors is non-linear. Therefore, the results disclosed should not be extrapolated to measure sensitivities to different levels of stress. For the same reason, the impact of the stress is not necessarily symmetrical on the upside and downside. The sensitivities are stated before allowance for management actions which may mitigate the effect of changes in the market environment. The sensitivities presented allow for adverse changes in policyholder behaviour that may arise in response to changes in market rates.

Changes in sensitivity compared to 2017 were primarily driven by the impact of increasing yields in France on the projected cost of options and guarantees.

Sensitivity of the group's insurance manufacturing subsidiaries to market risk factors

(Audited)

	2018		2017	
	Effect on profit after tax	**Effect on total equity**	Effect on profit after tax	Effect on total equity
	£m	**£m**	£m	£m
+100 basis point parallel shift in yield curves	**32**	**18**	24	9
-100 basis point parallel shift in yield curves	**(35)**	**(19)**	(44)	(28)
10% increase in equity prices	**23**	**23**	20	20
10% decrease in equity prices	**(21)**	**(21)**	(19)	(19)

Credit risk

(Audited)

Description and exposure

Credit risk arises in two main areas for our insurance manufacturers:

- risk associated with credit spread volatility and default by debt security counterparties after investing premiums to generate a return for policyholders and shareholders; and
- risk of default by reinsurance counterparties and non-reimbursement for claims made after ceding insurance risk.

The amounts outstanding at the balance sheet date in respect of these items are shown in the table on page 66.

The credit quality of the reinsurers' share of liabilities under insurance contracts is assessed as 'satisfactory' or higher as defined on page 27, with 100% of the exposure being neither past due nor impaired.

Credit risk on assets supporting unit-linked liabilities is predominantly borne by the policyholder; therefore our exposure is primarily related to liabilities under non-linked insurance and investment contracts and shareholders' funds. The credit quality of these financial assets is included in the table on page 46.

Liquidity risk

(Audited)

Description and exposure

Liquidity risk is the risk that an insurance operation, though solvent, either does not have sufficient financial resources available to meet its obligations when they fall due, or can secure them only at excessive cost.

The following table shows the expected undiscounted cash flows for insurance contract liabilities at 31 December 2018. The liquidity risk exposure is wholly borne by the policyholder in the case of unit-linked business and is shared with the policyholder for non-linked insurance.

The profile of the expected maturity of insurance contracts at 31 December 2018 remained comparable with 2017.

The remaining contractual maturity of investment contract liabilities is included in Note 27.

Expected maturity of insurance contract liabilities

(Audited)

	Expected cash flows (undiscounted)				
	Within 1 year	1-5 years	5-15 years	Over 15 years	Total
	£m	£m	£m	£m	£m
Unit-linked	**177**	**362**	**472**	**433**	**1,444**
With DPF and Other contracts	**1,445**	**6,735**	**6,606**	**4,787**	**19,573**
At 31 Dec 2018	**1,622**	**7,097**	**7,078**	**5,220**	**21,017**
Unit-linked	289	323	436	440	1,488
With DPF and Other contracts	1,460	6,665	6,625	5,212	19,962
At 31 Dec 2017	1,749	6,988	7,061	5,652	21,450

Insurance risk

Description and exposure

Insurance risk is the risk of loss through adverse experience, in either timing or amount, of insurance underwriting parameters (non-economic assumptions). These parameters include mortality, morbidity, longevity, lapses and unit costs.

The principal risk we face is that, over time, the cost of the contract, including claims and benefits, may exceed the total amount of premiums and investment income received.

The table on page 66 analyses our insurance manufacturing exposures by type of contract.

The insurance risk profile and related exposures remain largely consistent with those observed at 31 December 2017.

Sensitivities

The table below shows the sensitivity of profit and total equity to reasonably possible changes in non-economic assumptions across all our insurance manufacturing subsidiaries.

Mortality and morbidity risk is typically associated with life insurance contracts. The effect on profit of an increase in mortality or morbidity depends on the type of business being written. Our largest exposure to mortality and morbidity risk exists in the UK.

Sensitivity to lapse rates depends on the type of contracts being written. For a portfolio of term assurance, an increase in lapse rates typically has a negative effect on profit due to the loss of future income on the lapsed policies. However, some contract lapses have a positive effect on profit due to the existence of policy surrender charges. We are most sensitive to a change in lapse rates in France.

Expense rate risk is the exposure to a change in the cost of administering insurance contracts. To the extent that increased expenses cannot be passed on to policyholders, an increase in expense rates will have a negative effect on our profits.

Sensitivity analysis

(Audited)

	2018	2017
	£m	£m
Effect on profit after tax and total equity at 31		
10% increase in mortality and/or morbidity rates	**(19)**	(18)
10% decrease in mortality and/or morbidity rates	**19**	18
10% increase in lapse rates	**(27)**	(22)
10% decrease in lapse rates	**30**	25
10% increase in expense rates	**(33)**	(31)
10% decrease in expense rates	**34**	31

Capital

Capital management

Approach and policy

(Audited)

Our objective in managing the group's capital is to maintain appropriate levels of capital to support our business strategy and meet regulatory and stress testing related requirements.

We manage group capital to ensure that we exceed current and expected future requirements, and that we respect the payment priority of our capital providers. Throughout 2018, we complied with the Prudential Regulation Authority's ('PRA') regulatory capital adequacy requirements, including those relating to stress testing.

Capital measurement

The PRA is the supervisor of the bank and lead supervisor of the group. The PRA sets capital requirements and receives information on the capital adequacy of the bank and the group.

Individual banking subsidiaries are directly regulated by their local banking supervisors, who set and monitor their capital adequacy requirements. Since 1 January 2014, our capital at group level is calculated under CRD IV and the PRA Rulebook.

Our policy and practice in capital measurement and allocation at the group level is underpinned by the CRD IV rules. In most jurisdictions, non-bank financial subsidiaries are also subject to the supervision and capital requirements of local regulatory authorities.

The Basel III framework, like Basel II, is structured around three 'pillars': minimum capital requirements, supervisory review process and market discipline. Basel III also introduces a number of capital buffers, including the Capital Conservation Buffer ('CCB'), Countercyclical Capital Buffer ('CCyB'), and other systemic buffers such as the Globally/Other Systemically Important Institutions ('G-SII'/'O-SII') buffer. CRD IV legislation implemented Basel III in the EU and the 'PRA Rulebook' for CRR Firms transposed the various national discretions under the CRD IV legislation into UK requirements.

Regulatory capital

Our capital base is divided into three main categories, namely common equity tier 1, additional tier 1 and tier 2, depending on their characteristics.

- Common equity tier 1 ('CET 1') capital is the highest quality form of capital, comprising shareholders' equity and related non-controlling interests (subject to limits). Under CRD IV various capital deductions and regulatory adjustments are made against these items; these include deductions for goodwill and intangible assets, deferred tax assets that rely on future profitability, negative amounts resulting from the calculation of expected loss amounts under internal ratings based ('IRB') approach and surplus defined benefit pension fund assets.
- Additional tier 1 capital comprises eligible non-common equity capital instruments and any related share premium; it also includes other qualifying instruments issued by subsidiaries subject to certain limits. Holdings of additional tier 1 instruments of financial sector entities are deducted from our additional tier 1 capital.
- Tier 2 capital comprises eligible capital instruments and any related share premium and other qualifying tier 2 capital instruments issued by subsidiaries, subject to limits. Holdings of tier 2 capital instruments of financial sector entities are deducted from our tier 2 capital.

Pillar 3 disclosure requirements

Pillar 3 of the Basel regulatory framework is related to market discipline and aims to increase market transparency by requiring firms to publish, at least annually, wide-ranging information on their risks and capital, and how these are managed. Our Pillar 3 Disclosures 2018 are published on HSBC's website, www.hsbc.com, under 'Investors'.

Capital overview

Key capital numbers

		At 31 Dec	
	Footnotes	**2018**	2017[1]
Available capital (£m)			
Common equity tier 1 capital		**19,831**	27,409
Tier 1 capital		**23,079**	32,243
Total regulatory capital		**37,671**	39,288
Risk-weighted assets (£m)			
Credit risk	*2*	**88,822**	164,767
Counterparty credit risk		**24,669**	24,018
Market risk		**17,534**	20,978
Operational risk		**12,850**	23,310
Total risk-weighted assets		**143,875**	233,073
Capital ratios (%)			
Common equity tier 1		**13.8**	11.8
Total tier 1		**16.0**	13.8
Total capital		**26.2**	16.9
Leverage ratio			
Tier 1 capital (£m)		**22,213**	31,165
Total leverage ratio exposure measure (£m)		**570,001**	787,220
Leverage ratio (%)	*3*	**3.9**	4.0

1 *All figures presented as reported under IAS 39 at 31 December 2017.*
2 *'Credit risk' here, and in all tables where the term is used, excludes counterparty credit risk.*
3 *Leverage ratio is calculated on a fully phased-in basis.*

Capital structure at 31 December

(Audited)

Own funds disclosure

Ref[1]		At 31 Dec 2018 £m	At 31 Dec 2017 £m
	Common equity tier 1 ('CET1') capital: instruments and reserves		
1	Capital instruments and the related share premium accounts	**797**	797
	– ordinary shares	**797**	797
2	Retained earnings	**30,668**	32,601
3	Accumulated other comprehensive income (and other reserves)	**2,953**	4,341
5	Minority interests (amount allowed in consolidated CET1)	**372**	337
5a	Independently reviewed interim net profits net of any foreseeable charge or dividend	**(12,049)**	217
6	**Common equity tier 1 capital before regulatory adjustments**	**22,741**	38,293
	Common equity tier 1 capital: regulatory adjustments		
7	Additional value adjustments	**(623)**	(587)
8	Intangible assets (net of related deferred tax liability)	**(1,970)**	(5,337)
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability)	**(40)**	(39)
11	Fair value reserves related to gains or losses on cash flow hedges	**7**	41
12	Negative amounts resulting from the calculation of expected loss amounts	**(183)**	(864)
14	Gains or losses on liabilities at fair value resulting from changes in own credit standing	**(79)**	452
15	Defined-benefit pension fund assets	**(22)**	(4,550)
28	**Total regulatory adjustments to common equity tier 1**	**(2,910)**	(10,884)
29	**Common equity tier 1 capital**	**19,831**	27,409
	Additional tier 1 ('AT1') capital: instruments		
30	Capital instruments and the related share premium accounts	**2,403**	3,781
31	– classified as equity under IFRSs	**2,403**	3,781
33	Amount of qualifying items and the related share premium accounts subject to phase out from AT1	**866**	1,083
34	Qualifying tier 1 capital included in consolidated AT1 capital (including minority interests not included in CET1) issued by subsidiaries and held by third parties	**26**	44
36	**Additional tier 1 capital before regulatory adjustments**	**3,295**	4,908
	Additional tier 1 capital: regulatory adjustments		
37	Direct and indirect holdings of own AT1 instruments	**(47)**	(45)
41b	Residual amounts deducted from AT1 capital with regard to deduction from tier 2 ('T2') capital during the transitional	**–**	(29)
	– direct and indirect holdings by the institution of the T2 instruments and subordinated loans of financial sector entities where the institution has a significant investment in those entities	**–**	(29)
43	**Total regulatory adjustments to additional tier 1 capital**	**(47)**	(74)
44	**Additional tier 1 capital**	**3,248**	4,834
45	**Tier 1 capital (T1 = CET1 + AT1)**	**23,079**	32,243
	Tier 2 capital: instruments and provisions		
46	Capital instruments and the related share premium accounts	**13,962**	5,977
47	Amount of qualifying items and the related share premium accounts subject to phase out from T2	**881**	1,194
48	Qualifying own funds instruments included in consolidated T2 capital (including minority interests and AT1 instruments not included in CET1 or AT1) issued by subsidiaries and held by third parties	**152**	169
49	*– of which: instruments issued by subsidiaries subject to phase out*	***107***	*146*
51	**Tier 2 capital before regulatory adjustments**	**14,995**	7,340
	Tier 2 capital: regulatory adjustments		
52	Direct and indirect holdings of own T2 instruments	**(31)**	(30)
55	Direct and indirect holdings by the institution of the T2 instruments and subordinated loans of financial sector entities where the institution has a significant investment in those entities (net of eligible short positions)	**(372)**	(265)
57	**Total regulatory adjustments to tier 2 capital**	**(403)**	(295)
58	**Tier 2 capital**	**14,592**	7,045
59	**Total capital (TC = T1 + T2)**	**37,671**	39,288

1 The references identify the lines prescribed in the EBA template, which are applicable and where there is a value.

CET1 capital decreased during the year by £7.6bn, mainly due to:

- £11.2bn reduction from implementing the ring-fencing transfer scheme; and
- £0.1bn of capital reduction through profits, net of dividends;

These decreases were partly offset by:

- £3.5bn capital contribution from HSBC Holdings plc and HSBC UK Holdings Ltd; and
- £0.1bn of IFRS 9 day one transition impact.

Risk-Weighted Assets ('RWAs')

RWA movement by business by key driver

	Credit risk, counterparty credit risk and operational risk						
	RBWM	CMB	GB&M	GPB	Corporate Centre	Market risk	Total RWAs
	£m	£m	£m	£m	£m	£m	£m
RWAs at 31 Dec 2017	26,676	85,448	76,790	3,540	19,641	20,978	233,073
Asset size	248	6,177	(3,622)	(7)	(7,143)	(4,309)	(8,656)
Asset quality	(32)	1,206	370	116	(49)	–	1,611
Model updates	332	1,300	328	–	–	–	1,960
– portfolios moving onto IRB approach	–	–	–	–	–	–	–
– new/updated models	332	1,300	328	–	–	–	1,960
Methodology and policy	726	3,792	(4,185)	196	(324)	(219)	(14)
– internal updates	726	3,792	(4,185)	196	(635)	(219)	(325)
– external updates – regulatory	–	–	–	–	311	–	311
Acquisitions, disposals and transfers	(20,982)	(66,241)	2,264	(1,848)	(811)	(38)	(87,656)
Foreign exchange movement	64	228	1,929	15	199	1,122	3,557
Write-offs	–	–	–	–	–	–	–
Total RWA movement	(19,644)	(53,538)	(2,916)	(1,528)	(8,128)	(3,444)	(89,198)
RWAs at 31 Dec 2018	7,032	31,910	73,874	2,012	11,513	17,534	143,875

RWAs fell by £89.2bn in the year, principally as a result of an £87.7bn reduction due to acquisitions, disposals and transfers. On 1 July the bank transferred business and assets worth £89.7bn to HSBC UK bank plc to complete the ring-fencing of its qualifying retail business. This transfer was partly offset by other movements, primarily the acquisition of HSBC Investment Bank Holdings and HSBC Specialist Investment Limited which added £2.6 bn RWAs.

Excluding these movements, and an increase of £3.6bn due to foreign currency translation differences, the bank's RWAs reduced by £5.1bn mainly as a result of an £8.7bn fall in asset size, less a £2.0bn increase due to model updates and a £1.6bn increase due to movements in asset quality.

The following comments describe RWA movements in 2018 excluding foreign currency translation differences and acquisitions and disposals.

Asset size

Asset size movements were mainly driven by management initiatives which reduced legacy securitisation assets in Corporate Centre and GB&M RWAs by £10.7bn. This was partly offset by £6.4bn of lending growth in CMB corporate book and in RBWM mortgages and credit card exposure. Market risk RWAs fell by £4.3bn due to management initiatives to lower exposures.

Asset quality

RWAs increased by £1.6bn mainly as a result of changes in portfolio mix across CMB and GB&M.

Methodology and policy

The £0.3bn decrease in RWAs from internal updates is principally the result of a fall of £4.2bn in GB&M RWAs and a £3.8bn increase in CMB. These movements include the transfer of £1.6bn of RWAs from GB&M to CMB as part of resegmentation activity prior to ring-fencing. Excluding this transfer:

- GB&M RWAs fell by £2.6bn as a result of management initiatives and calculation refinements; and
- CMB RWAs rose by £2.1bn primarily as a result of calculation refinements following IFRS 9 implementation.

This is offset by a £0.3bn increase in external updates as a result of IFRS 9 implementation.

Model updates

The £2.0bn increase in RWAs was largely due to updates to UK retail and corporate PD models and to the implementation of a German receivable finance model.

Leverage ratio

Our fully phased-in CRD IV leverage ratio was 3.9% at 31 December 2018, down from 4.0% at 31 December 2017. Fall in tier 1 capital was largely offset by a decrease in the leverage exposure measure, primarily due to a transfer of qualifying exposures to HSBC UK bank plc.

Corporate Governance Report

The statement of corporate governance practices set out on pages 72 to 77 and information incorporated by reference constitute the Corporate Governance Report of HSBC Bank plc.

The Directors serving at 31 December 2018 are set out below.

Directors

Stephen O'Connor

Chairman

Chairman of the Chairman's Nominations and Remuneration Committee

Appointed to the Board: May 2018. Chairman since August 2018

Stephen is Founder and Chairman of Quantile Technologies Limited, and a non-executive Director, Chairman of the Risk Committee and member of both the Audit and Nomination Committees of The London Stock Exchange Group plc. He has more than 25 years' investment banking experience in London and New York. Former appointments include: Chairman of the International Swaps and Derivatives Association and prior to that he was Managing Director and a member of the Fixed Income Management Committee at Morgan Stanley.

James Emmett

Executive Director and Chief Executive Officer

Chairman of the Executive Committee

Appointed to the Board and as Chief Executive Officer: September 2018

James joined HSBC in 1994 and has performed a variety of senior management roles. He is a Director of HSBC France and a member of the Supervisory Board of HSBC Trinkaus & Burkhardt AG. Former appointments include: Group General Manager and Chief Operating Officer of HSBC Bank plc, and Group General Manager and CEO of HSBC Bank A.S. (Turkey).

Jacques Fleurant

Executive Director and Chief Financial Officer

Member of the Executive Committee

Appointed to the Board and as Chief Financial Officer: August 2018

Jacques joined HSBC in 2000 in Toronto, and has held a variety of senior roles in finance and operations. Prior to joining HSBC he performed senior roles at Merrill Lynch and for the Canadian Revenue Agency.

Dame Mary Marsh

Independent non-executive Director

Member of the Risk Committee

Appointed to the Board: January 2009

Mary is the non-executive Chair of Trustees of the Royal College of Paediatrics and Child Health, a director of the London Symphony Orchestra, a member of the Governing Body of the London Business School and a Trustee of Teach First. Former appointments include: founding Director of the Clore Social Leadership Programme and Chief Executive of the National Society for the Prevention of Cruelty to Children.

Yukiko Omura

Independent non-executive Director

Member of the Risk Committee

Appointed to the Board: May 2018

Yukiko is a non-executive Director of The Private Infrastructure Development Group Limited ("PIDG"), as well as Chair of GuarantCo Limited, a subsidiary of PIDG. She also serves as a non-executive Director of Assured Guaranty Ltd, and on the Supervisory Board member of Nishimoto HD Co. Ltd. She has more than 35 years' international professional experience in both the public and private financial sector, performing senior roles for JP Morgan, Lehman Brothers, UBS and Dresdner Bank. Former appointments include: Under-Secretary General and COO/Vice President of the International Fund for Agricultural Development and, Executive Vice President and CEO of the Multilateral Investment Guarantee Agency of the World Bank Group.

Dr Eric Strutz

Independent non-executive Director

Chairman of the Risk Committee, Member of the Audit Committee and the Chairman's Nominations and Remuneration Committee

Appointed to the Board: October 2016

Eric is a member of the Supervisory Board and Chairman of the Risk and Audit Committees of HSBC Trinkaus & Burkhardt AG, Germany, member of the Board of Directors and Chairman of the Risk and Audit Committee of Partners Group Holding AG, Switzerland, a member of the Board of Directors and Chairman of the Audit Committee of Global Blue SA, and a member of the Advisory Board and Chairman of the Audit & Risk Committee of Luxembourg Investment Company 261 Sarl. Former appointments include: Chief Financial Officer of Commerzbank Group, Partner and Director of the Boston Consulting Group, as well as non-executive Director of Mediobanca Banca di Credito Finanziario SpA.

John Trueman

Deputy Chairman and independent non-executive Director

Member of the Audit Committee, the Risk Committee and the Chairman's Nominations and Remuneration Committee

Appointed to the Board: 2004. Deputy Chairman since December 2013

John is Chairman of HSBC Global Asset Management Limited and non-executive director of HSBC Private Bank (UK) Limited. Former appointments include: Deputy Chairman of S.G. Warburg & Co Ltd.

Andrew Wright

Independent non-executive Director

Chairman of the Audit Committee, Member of the Risk Committee and the Chairman's Nominations and Remuneration Committee

Appointed to the Board: May 2018

Andrew has been the Treasurer to the Prince of Wales and the Duchess of Cornwall since 2012. Former appointments include: Global Chief Financial Officer for the Investment Bank at UBS AG, Chief Financial Officer, Europe and the Middle East at Lehman Brothers and Chief Financial Officer for the Private Client and Asset Management Division at Deutsche Bank.

Company Secretary

Loren Wulfsohn was appointed Company Secretary of HSBC Bank plc with effect from 1 January 2018.

Board of Directors

The objective of the Board of Directors, led by the Chairman, is to deliver sustainable value to shareholders and internal and external stakeholders. Implementation of the strategy is delegated to the Bank's Executive Committee.

The Board meets regularly and Directors receive information between meetings about the activities of committees and developments in the bank's business. All Directors have full and timely access to all relevant information and may take independent professional advice if necessary.

All Directors are subject to annual re-election at the HSBC Bank plc Annual General Meeting.

Board Changes during 2018

The Board regularly reviews its composition and in 2018 a number of changes were made to the Board to ensure that the Board has the right mix of skills and experience.

In May 2018 Stephen O'Connor, Yukiko Omura and Andrew Wright were appointed to the Board as independent non-executive Directors.

The following Board changes took place:

In August 2018;

- Jonathan Symonds stepped down as Chairman of the Board;
- Stephen O'Connor was appointed as Chairman of the Board;
- Jim Coyle, Dame Denise Holt and David Lister resigned, having each been appointed to the Board of HSBC UK Bank plc;
- Eric Strutz and Andrew Wright were appointed as Chairman of the Risk and Audit Committees respectively; and
- Jacques Fleurant was appointed as Chief Financial Officer and Executive Director.

In September 2018;

- Thierry Moulonguet resigned as a non-executive Director having served since July 2012;
- Antonio Simoes who served on the Board and as Chief Executive Officer since 2012 resigned; and
- James Emmett, who had been appointed as acting Chief Executive Officer in March 2018, was appointed as Chief Executive Officer and to the Board.

Directors' emoluments

Details of the emoluments of the Directors of the bank for 2018, disclosed in accordance with the Companies Act, are shown in Note 6 'Employee compensation and benefits'.

Non-executive Directors do not have service contracts, but are bound by letters of appointment.

Board committees

The Board has established a number of committees to assist it in discharging its responsibilities. The Chairman of each non-executive Board committee reports to the Board on the activities of the committee since the previous Board meeting. All of the members of the Audit, Risk and Chairman's Nomination and Remuneration Committees are independent non-executive directors.

At the date of this report, the following are the principal committees of the Board:

Audit Committee

The Audit Committee is accountable to the Board and has non-executive responsibility for oversight of and advice to the Board on financial reporting related matters and internal controls over financial reporting.

The Committee meets regularly with the bank's senior financial and internal audit management and the external Auditors to consider, among other matters, the bank's financial reporting, the nature and scope of audit reviews, the effectiveness of the systems of internal control relating to financial reporting, the review of the financial underpinnings of structural reform projects and the monitoring of the finance function transformation program. The current members are Andrew Wright (Chairman), Eric Strutz and John Trueman.

Significant accounting judgements and related matters considered by the Audit Committee during 2018 included:

Key area	Action taken
Appropriateness of provisioning for legal proceedings and regulatory matters	The HSBC Bank plc Audit Committee ('AC') received reports from management on the recognition and measurement of provisions and contingent liabilities for legal proceedings and regulatory matters. Specific matters included accounting judgements in relation to provisions and contingent liabilities arising from investigations by regulators and competition and law enforcement authorities around the world into trading on the foreign exchange market.
IBOR transition	The AC considered the accounting implications of benchmark interest rate replacement for hedge accounting relationships at 31 December 2018, the longer term broader implications for financial instruments and other areas of accounting, and the related disclosures. The AC considered management's judgement that no change to hedge accounting is appropriate as at 31 December 2018 and that this position will be kept under review in the context of future market developments in the transition of interest rate benchmarks to new risk free rates.
Interim and annual reporting	The AC considered key judgements in relation to interim and annual reporting.
Expected credit loss ('ECL') allowances and charges	The AC considered the key judgements related to IFRS 9 and the related disclosures, The AC considered ECL allowances and charges for personal and wholesale lending. Specific attention was paid to credit risk in the UK and adjustment to ECL for UK economic uncertainty.
Valuation of financial instruments	The AC considered the key valuation metrics and judgements involved in the determination of the fair value of financial instruments.
Going concern	The AC considered a wide range of information relating to present and potential conditions, including projections for profitability, cash flows, liquidity and capital. Specific attention was paid to the effects of ring-fencing and the potential impact of the UK's withdrawal from the European Union.
UK customer remediation	The AC considered the provisions for redress for mis-selling of payment protection insurance ('PPI') policies in the UK and the associated redress on PPI commissions earned under certain criteria, including management's judgements regarding the effect of the time-bar for claims ending August 2019. In addition, the AC monitored progress on the remediation of operational processes and associated customer redress.
Goodwill impairment testing	The AC considered the results of the annual goodwill impairment test and subsequent review for any impairment indicators. Whilst there were no indicators of impairment at 31 December 2018, the AC noted the sensitivity of Commercial Banking goodwill to reasonably possible changes in assumptions and the risk of impairment in the future should business performance or economic factors diverge from forecasts
Controls	The AC considered the financial control environment and reviewed action taken to enhance controls over IT access management, balance sheet substantiation, disclosure preparation and other areas. The AC reviewed the progress of ongoing action to enhance controls over general ledger reconciliation and substantiation, model governance, IFRS 9 data quality and control monitoring.
Tax	The AC considered key judgements in relation to tax, notably the contingent liability for retrospective VAT assessments issued by HMRC.
Estimated impact of IFRS 16, Leases	The AC considered the estimated impact of implementation of IFRS 16 Leases on 1 January 2019 and the related disclosures.
Ring-fenced bank ('RFB')	The AC considered the accounting in relation to the creation of the RFB and the associated judgements, including those related to the disclosure of discontinued operations.

Risk Committee

The Risk Committee is accountable to the Board and has non-executive responsibility for oversight of and advice to the Board on high-level risk related matters and risk governance.

The Committee meets regularly with the bank's senior financial, risk, internal audit and compliance management and the external Auditors to consider, among other matters, risk reports and internal audit reports and the effectiveness of compliance.

The current members are: Dr Eric Strutz (Chairman); Dame Mary Marsh; Yukiko Omura; John Trueman and Andrew Wright.

Post ring-fencing, the sub Committee of the Risk Committee for Global Banking and Markets ("GB&M") Risk Oversight was demised and its role assumed by the Risk Committee.

Operations and Technology Committee

Following implementation of ring-fencing in the UK, the Operations and Technology Committee was demised in July 2018. The Committee's responsibilities, which included the oversight of systems, operational resilience and the bank's IT infrastructure, were assigned to the Risk Committee which will be assisted in the discharge of its duties by the newly formed Operations and Technology Forum.

Before its demise, the Committee met regularly in 2018 with the bank's senior risk, operations, security and fraud risk and technology audit management to consider, among other matters, internal audit reports and reports on the risks associated with the bank's IT infrastructure and transformation projects, cybersecurity and data management.

The current members are Stephen O'Connor and Eric Strutz.

Chairman's Nominations and Remuneration Committee

The Chairman's Nominations and Remuneration Committee has responsibility for: (i) leading the process for Board appointments and for identifying and nominating, for the approval of the Board, candidates for appointment to the Board; (ii) the endorsement of the appointment of the chairman and any director to the Board of certain subsidiaries of the bank; and (iii) reviewing the implementation and appropriateness of HSBC Group's remuneration policy and the remuneration of the bank's senior executives.

The current members are: Stephen O'Connor (Chairman); Eric Strutz; John Trueman and Andrew Wright.

Executive Committee

The Executive Committee meets regularly and operates as a general management committee under the direct authority of the Board, exercising all of the powers, authorities and discretions of the Board in so far as they concern the management and day-to-day running of the bank, in accordance with such policies and directions as the Board may from time to time determine. The bank's Chief Executive Officer, James Emmett, chairs the Committee.

Regular Risk Management Meetings of the Executive Committee, chaired by the Chief Risk Officer, Europe, are held to establish, maintain and periodically review the policy and guidelines for the management of risk within the bank.

The following committees are sub-committees of the Executive Committee:

- International Executive Committee; and
- International Risk Management Meeting.

The International Executive Committee is responsible for monitoring and, where appropriate, implementing and driving execution of the group's strategy as it pertains to the portion of the group's operations designated as International.

The International Risk Management Committee is responsible for the oversight and management of all risks impacting the group's operations designated as International.

Dividends

Information about dividends is provided on page 15 of the Strategic Report.

Internal control

The Board is responsible for maintaining and reviewing the effectiveness of risk management and internal control systems and for determining the aggregate level and types of risks the bank is willing to take in achieving its strategic objectives.

The bank has procedures in place designed to safeguard assets against unauthorised use or disposal, maintain proper accounting records and ensure the reliability and usefulness of financial information whether used within the business or for publication.

These procedures can only provide reasonable assurance against material mis–statement, errors, losses or fraud. They are designed to provide effective internal control within the bank. The procedures have been in place throughout the year and up to the date of approval of the *Annual Report and Accounts 2018.*

In the case of companies acquired during the year, the risk management and internal controls in place are being reviewed against HSBC's benchmarks and integrated into HSBC's processes.

Key risk management and internal control procedures include the following:

- **Adherence to the Group's Global Standards Manual ('GSM').** The GSM outlines the core principles within which all members of the HSBC Group must operate wherever business is conducted. The GSM overlays all other policies and procedures throughout the HSBC Group. The requirements of the GSM are mandatory, apply to and must be observed by all businesses within the HSBC Group, regardless of the nature or location of their activities. In 2019, the GSM process will be replaced by a set of Global Principles.
- **Delegation of authority within limits set by the Board.** Authority to manage the day–to–day running of the bank is delegated within limits set by the Board to the Chief Executive who has responsibility for overseeing the establishment and maintenance of systems of control appropriate to the business and who has the authority to delegate such duties and responsibilities as he sees fit. Appointments to the most senior positions require Board approval.
- **Risk identification and monitoring.** Systems and procedures are in place to identify, control and report on the material risk types facing the group.
- **Changes in market conditions/practices.** Processes are in place to identify new risks arising from changes in market conditions/practices or customer behaviours, which could expose the group to heightened risk of loss or reputational damage. The group employs a top and emerging risks framework at all levels of the organisation, which enables it to identify current and forward-looking risks and to take action which either prevents them materialising or limits their impact.
- **Responsibility for risk management.** All employees are responsible for identifying and managing risk within the scope of their role as part of the three lines of defence model, which is an activity-based model to delineate management accountabilities and responsibilities for risk management and the control environment. The second line of defence sets the policy and guidelines for managing specific areas, provides advice and guidance in relation to the risk, and challenges the first line of defence (the risk owners) on effective risk management.
- **Strategic plans.** Strategic plans are prepared for global businesses, global functions and geographical regions within the framework of the HSBC Group's overall strategy. The bank also prepares and adopts an Annual Operating Plan, which is informed by detailed analysis of risk appetite, describing the types and quantum of risk that the bank is prepared to take in executing its strategy and sets out the key business initiatives and the likely financial effects of those initiatives.

The key risk management and internal control procedures over financial reporting include the following:

- **Entity level controls:** The primary mechanism through which comfort over risk management and internal control systems is achieved, is through assessments of the effectiveness of entity level controls ('ELC'), and the reporting of risk and control issues on a regular basis through the various risk management and risk governance forums. ELCs are internal controls that have a pervasive influence over the entity as a whole. They include controls related to the control environment, for example the Company's values and ethics, the promotion of effective risk management and the overarching governance exercised by the Board and its non-executive committees. The design and operational effectiveness of ELCs are assessed annually as part of the assessment of the effectiveness of internal controls over financial reporting.
- Key process level controls that mitigate risk of financial misstatement are recorded in the Operation Risk system and monitored in accordance with the ORMF. Further details on the framework can be found on page 31.
- **Disclosure Forum.** The Disclosure Forum reviews financial reporting disclosures made by the bank for any material errors, misstatements or omissions. The integrity of disclosures is underpinned by structures and processes within the group's Finance and Risk functions that support rigorous analytical review of financial reporting and the maintenance of proper accounting records.
- **Financial reporting.** The bank's financial reporting process for preparing the consolidated *Annual Report and Accounts 2018* is controlled using documented accounting policies and reporting formats, supported by detailed instructions and guidance on reporting requirements, issued to all reporting entities within the Group in advance of each reporting period end.
- **Subsidiary certifications.** Full and half–yearly certifications are provided to the Audit Committee and the Risk Committee from audit and risk committees of principal subsidiary companies, confirming that their financial statements have been prepared in accordance with Group policies, present fairly the state of affairs of the relevant principal subsidiary and are prepared on a going concern basis.

In 2018, the acceleration of operational resilience and investment in technology controls were particular areas of focus for HSBC. The Group continued to embed the operational risk management framework and invest in the non-financial risk infrastructure. Work also continued to enhance the risk appetite framework for non-financial risks and improve the consistency of adoption of the end-to-end risk and control assessment process. Whilst there remains more to do, considerable progress has been made to strengthen HSBC's control environment and it will continue to be a priority for 2019.

During the year, the Audit and Risk Committees keep under review the effectiveness of this system of internal control and report regularly to the Board. In carrying out their reviews, the Audit and Risk Committees receive regular business and operational risk assessments; regular reports from the heads of key risk functions, which cover all internal controls, both financial and non-financial; internal audit reports; external audit reports; prudential reviews; and regulatory reports.

The Risk Committee monitors the status of principal risks and considers whether the mitigating actions put in place are

appropriate. In addition, when unexpected losses have arisen or when incidents have occurred which indicate gaps in the control framework or in adherence to Group policies, the Risk and Audit Committees review special reports, prepared at the instigation of management, which analyse the cause of the issue, the lessons learned and the actions proposed by management to address the issue.

Employees

Health and safety

The group is committed to providing a healthy and safe working environment for our employees, contractors, customers and visitors on HSBC premises and where impacted by our operations. We aim to be compliant with all applicable health and safety legal requirements, and that best practice health and safety management standards are implemented and maintained across the HSBC Group.

Everyone at HSBC has a responsibility for helping to create a healthy and safe working environment. Employees are expected to take ownership of their safety and are encouraged and empowered to report any concerns.

Chief Operating Officers have overall responsibility for ensuring that the correct policies, procedures and safeguards are put into practice. This includes making sure that everyone in HSBC has access to appropriate information, instruction, training and supervision.

Putting our commitment into practice, in 2018 the group delivered a health and safety education and information training programme to every one of our employees, and a range of programmes to help us understand and effectively manage the risks we face and improve the buildings in which we operate:

- We developed and implemented a health and safety continuous improvement programme, focusing on education, engineering and enforcement/reward, to improve our health and safety culture and to implement the highest standards of control for managing health and safety.
- We developed and implemented an improved health and safety training and awareness programme for all employees globally, ensuring roles and responsibilities were clear and understood; and processes for identifying and reporting hazards and incidents were clearly defined and communicated.
- We implemented, through our global facilities management service provider, an electronic permit to work system to provide effective controls for all high risk work undertaken.
- We developed and implemented a global earthquake risk management programme, to ensure all HSBC properties in earthquake zones were risk assessed and controls implemented to manage the risk.
- We ensured all our properties had been assessed for fire and asbestos risk, with over 40,000 individual actions taken to improve standards.

Employee health and safety

	Footnotes	2018	2017	2016
Number of workplace fatalities	1,2	—	—	—
Number of major injuries to employees	1,2	9	19	21
All injury rate per 100,000 employees	2	343	448	470

1 *Fractures, dislocation, concussion.*
2 *Comparative data has been restated to show Europe figures.*

Diversity and inclusion

We are committed to enabling a thriving environment where people are valued, respected and supported to fulfil their potential; and where leveraging the extraordinary range of ideas, backgrounds, styles and perspectives of our employees means we can effectively meet the needs of our different stakeholder groups and drive better business outcomes for all. Our employees are expected to build positive and lasting relationships among the variety of people they interact with.

We focus on enhancing the diversity profile of our workforce so that it is more reflective of the communities we operate in and the customers we serve.

To support an inclusive environment, our policy is that each of us must treat colleagues with dignity and respect. We have zero tolerance for discrimination, bullying, harassment and victimisation on any ground, including age, race, ethnic or national origin, colour, mental or physical health conditions, disability, pregnancy, gender, gender expression, gender identity, sexual orientation, marital status or other domestic circumstances, employment status, working hours or other flexible working arrangements, or religion or belief. Such behaviour is considered a personal conduct matter and managed in accordance with applicable local policies and procedures and our consequence management framework.

Diversity and inclusion carries the highest level of executive support and is governed by the Group People Committee.

More information about our diversity and inclusion activity is available at https://www.hsbc.com/our-approach.

Key achievements

In 2018, the UK created and launched the 'Inclusion Hub', which holds an abundance of information and resources relating to Diversity & Inclusion ('D&I'). This effectively provides UK employees with a 'one stop shop' for all of their D&I questions and requirements. The Driving Inclusion Workshops were delivered to UK leaders, with the HR Leadership Team, UK Inclusion Board and the UK Executive Committee already having participated during 2018. The workshop has been designed to support our inclusion strategy underpinned by inclusive behaviours. To focus the agenda around the five areas of priority for the UK business; gender, LGBT+, ethnicity, flexible working, and disability, a framework has been designed to progress the agenda at pace. The framework provides for business led actions with clear UK Executive Committee accountability and ownership.

HSBC France launched its first Diversity & Inclusion week to raise awareness in partnership with its two Employee Resource Groups: 50 50 Partner of Balance and HSBC Pride Network France. HSBC France also continued to raise managers' awareness of diversity and unconscious bias via dedicated workshops.

HSBC Malta was accredited as an Equal Employer by the National Commission Promoting Equality. The company demonstrated commitment towards its equality and sexual harassment policy; taking measures to ensure equal opportunities in recruitment and employment practices, and in career and personal development opportunities; promoting family-friendly measures and work-life balance options for men and women with caring responsibilities. It is an affirmation that the company truly demonstrates its commitment towards gender equality and provides true equal opportunities without judgements based on stereotypes. Ultimately, this showcases a quality standard for job seekers to look out for and makes the company an employer of choice.

HSBC Germany continued to establish an integrated talent development and D&I approach by increasing talent development activities. These include initiatives such as progression and targeted development of female talents by implementing the Female Leadership Accelerator Programme and implementing individual development plans for female key talent. HSBC Germany also continued to focus on unconscious bias awareness by deploying Unconscious Bias workshops for leaders. The local Balance network continues to provide its members opportunities to have an open dialogue and share insights around career development within the firm. Typical activities include speeches by senior women, blind date lunches and quarterly newsletters. Additionally events are supported by external speakers who share best practices around gender balance. The local mentoring programme continues successfully. To date, 148 senior leaders offered their guidance for junior colleagues.

Diverse representation in Europe

Our focus on improving gender balance in senior leadership across Europe is on going.

Female representation by management level:

- All grades: 48%
- Clerical grades: 68%
- Junior management: 56%
- Management: 39%
- Senior management: 24%
- Executive management: 12%

Employment of people with a disability

We believe in providing equal opportunities for all employees. The employment of people with a disability is included in this commitment. The recruitment, training, career development and promotion of people with a disability are based on the aptitudes and abilities of the individual. Should employees become disabled during their employment with us, efforts are made to continue their employment and, if necessary, appropriate training and reasonable equipment and facilities are provided.

A number of countries have dedicated teams to ensure that barriers to work are removed for colleagues. HSBC France has taken actions to create a more inclusive environment for disabled people, for example HOST and Finance are ensuring disabilities are accommodated through assisted technologies. A deaf employee who benefits from interpreters and technological support was interviewed on French television (France 24) to explain how the support put in place and the commitment of his colleagues make his integration successful. HSBC France has worked with a non profit organisation to coach young disabled people on their CV and prepare them for interviews.

Learning and talent development

The development of our people is fundamental to the ongoing success of our organisation. We continue to develop and implement practices that build employee capability and identify, develop and deploy talented employees to ensure an appropriate supply of high calibre individuals with the right values, skills and experience for current and future senior management positions.

Since the launch of HSBC University in 2017 we have continued to add to the portfolio of world class leadership and professional programmes that provide opportunity for leaders and people managers to both develop and connect with each other across the group. In 2018 as part of our drive to use our own leaders to share experiences and the skill sets that they possess, we successfully launched a programme of development that enables our leaders to do just this. As a result we now have a growing number of HSBC leaders who actively help facilitate and bring our HSBC leadership development programmes to life.

As well as growing our learning and talent offering in traditional format, we also spent the year testing new technology platforms that make personal development accessible to all in HSBC. In addition we closed the year with the launch of our first digital learning curriculum covering the topic of personal leadership in HSBC. The target audience for this development is wide and includes HSBC front–line staff, meaning format and accessibility will be crucial to the overall success of the programme.

During 2018 a total of 75,000 formal days of training were received by 170,000 participants across Europe. Over 4,800 participants across Europe attended a flagship leadership programme in 2018 and all courses continue to receive positive feedback.

Employee relations

We consult with and, where appropriate, negotiate with employee representative bodies. It is our policy to maintain well-developed communications and consultation programmes with all employee representative bodies and there have been no material disruptions to our operations from labour disputes during the past five years.

Auditor

PricewaterhouseCoopers LLP ('PwC') is external Auditors to the bank. PwC has expressed its willingness to continue in office and the Board recommends that PwC be re-appointed as the bank's Auditors. A resolution proposing the re-appointment of PwC as the bank's Auditors and giving authority to the Audit Committee to determine its remuneration will be submitted to the forthcoming AGM.

Articles of Association, Conflicts of interest and indemnification of Directors

On 23 November 2018 the Articles of Association of HSBC Bank plc were amended to reflect the redesignation of the preferred ordinary share to an ordinary share as set out in Note 29 of the financial statements.

The Articles of Association of HSBC Bank plc gives the Board authority to approve Directors' conflicts and potential conflicts of interest. The Board has adopted a policy and procedures for the approval of Directors' conflicts or potential conflicts of interest. A review of situational conflicts which have been authorised, including the terms of authorisation, is undertaken by the Board annually.

The Articles of Association provide that Directors and directors of associated companies are entitled to be indemnified out of the assets of the company against claims from third parties in respect of certain liabilities arising in connection with the performance of their functions, in accordance with the provisions of the UK Companies Act 2006. Such indemnity provisions have been in place during the financial year but have not been utilised by the Directors. All Directors have the benefit of directors' and officers' liability insurance.

Statement on going concern

The Directors consider it appropriate to prepare the financial statements on the going concern basis. In making their going concern assessment, the Directors have considered a wide range of detailed information relating to present and potential conditions, including profitability, cash flows, capital requirements and capital resources.

Further information relevant to the assessment is provided in the Strategic Report and the Report of the Directors, in particular:

- a description of the group's strategic direction;
- a summary of the group's financial performance and a review of performance by business;
- the group's approach to capital management and its capital position; and
- the top and emerging risks facing the group, as appraised by the Directors, along with details of the group's approach to mitigating those risks and its approach to risk management in general.

In addition, the objectives, policies and processes for managing credit, liquidity and market risk are set out in the 'Report of the Directors: Risk'.

Statement of directors' responsibilities in respect of the financial statements

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulation.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the group and company and of the profit or loss of the group and company for that period. In preparing the financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- state whether applicable IFRSs as adopted by the European Union have been followed for the group financial statements and IFRSs as adopted by the European Union have been followed for the company financial statements, subject to any material departures disclosed and explained in the financial statements;
- make judgements and accounting estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the group and company will continue in business.

The directors are also responsible for safeguarding the assets of the group and company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the group and company's transactions and disclose with reasonable accuracy at any time the financial position of the group and company and enable them to ensure that the financial statements comply with the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

The directors of HSBC Holdings plc are responsible for the maintenance and integrity of the website on which the bank’s financial results are located. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

By order of the Board

Loren Wulfsohn

Company Secretary

HSBC Bank plc

19 February 2019

Registered number 14259

Independent auditors' report to the member of HSBC Bank plc

Report on the audit of the financial statements

Opinion

In our opinion, HSBC Bank plc's group financial statements and parent company financial statements (the "financial statements"):

- give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2018 and of the group's profit and the group's and the parent company's cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the parent company's financial statements, as applied in accordance with the provisions of the Companies Act 2006; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

We have audited the financial statements, included within the Annual Report and Accounts 2018, which comprise:

- the consolidated and HSBC Bank plc balance sheets as at 31 December 2018;
- the consolidated income statement and consolidated statement of comprehensive income for the year then ended;
- the consolidated and HSBC Bank plc statements of cash flows for the year then ended;
- the consolidated and HSBC Bank plc statements of changes in equity for the year then ended; and
- the notes to the financial statements, which include a description of the significant accounting policies.

Our opinion is consistent with our reporting to the Audit Committee.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the group or the parent company.

Other than those disclosed in Note 7 to the financial statements, we have provided no non-audit services to the group or the parent company in the period from 1 January 2018 to 31 December 2018.

Our audit approach

Overview

- Overall group materiality: £282 million (2017: £183 million), based on 0.75% of Total Regulatory Capital.
- Overall parent company materiality: £235 million (2017: £183 million), based on the lower of the group materiality or 0.75% of the parent's regulatory capital. 0.75% of the parent company's regulatory capital was lower and therefore was the benchmark used.
- HSBC Bank plc (the 'Bank') is a member of the HSBC Holdings plc Group, the ultimate parent company of which is HSBC Holdings plc. HSBC Bank plc operates in 18 countries.
- We performed audits of the complete financial information of two components, namely the UK business of the Bank (referred to as UK Operations) and HSBC France.
- For five further reporting units, specific audit procedures were performed over selected significant account balances.

The following areas were identified as key audit matters. These are discussed in further detail in the Appendix:

- Application of IFRS 9 in the calculation of impairment of loans and advances;
- Execution of structural reform required by the UK Financial Services (Banking Reform) Act 2013;
- IT access management; and
- Valuation of financial instruments.

The scope of our audit

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we looked at where the directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain.

Capability of the audit in detecting irregularities, including fraud

We focused on laws and regulations that could give rise to a material misstatement in the financial statements, including, but not limited to, the Companies Act 2006, the Financial Conduct Authority's regulations, the Prudential Regulation Authority's regulations, UK Listing Rules, the UK tax legislation and equivalent local laws and regulations applicable to significant component teams. One identified risk related to the execution of structural reform required by the UK Financial Services (Banking Reform) Act 2013; our audit procedures are explained in the key audit matter in the Appendix. Further to this, our tests in relation to laws and regulations included, but were not limited to, review of the financial statement disclosures to underlying supporting documentation, review of correspondence with and reports to the regulators, review of correspondence with legal advisors, enquiries of management, enquiries of legal counsel, review of

significant component auditors' work and review of internal audit reports in so far as they related to the financial statements. We also designed audit procedures at a group and significant component level to respond to the risk of fraud. This included identifying specific fraud criteria as part of our journals testing which were relevant to HSBC Bank plc and its business, for example unusual account combinations.

There are inherent limitations in the audit procedures described above and the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely we would become aware of it. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

Key audit matters

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditors, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters, and any comments we make on the results of our procedures thereon, were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. This is not a complete list of all risks identified by our audit. The key audit matters are discussed further in the Appendix.

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the group and the parent company, the accounting processes and controls, and the industry in which they operate.

HSBC Bank plc is structured into four divisions being Retail Banking and Wealth Management, Commercial Banking, Global Banking & Markets and Global Private Banking. The divisions operate across a number of operations, subsidiary entities and branches throughout Europe. Within the group's main consolidation and financial reporting system, the consolidated financial statements are an aggregation of the operations, subsidiary entities and branches ('reporting units'). Each reporting unit submits their financial information to the group in the form of a consolidation pack.

The ring-fencing requirements of the UK Financial Services (Banking Reform) Act 2013 and associated secondary legislation and regulatory rules, required UK deposit-taking banks with more than £25bn of 'core deposits' (broadly from individuals and small to medium-sized businesses) to separate their UK retail banking activities from their other wholesale and investment banking activities by 1 January 2019. As a result, on 1 July 2018, the UK Retail Banking and Wealth Management and the majority of the Commercial Banking divisions were transferred from HSBC Bank plc into a separately regulated legal entity, HSBC UK Bank plc (the 'ring-fenced bank'). This transaction had a significant impact on the audit of HSBC Bank plc and was considered as part of the scoping and execution of our testing.

In establishing the overall approach to the group and parent company audit, we scoped using the balances included in the consolidation pack. We determined the type of work that needed to be performed over the reporting units by us, as the group engagement team, or auditors within PwC UK and from other PwC network firms operating under our instruction ('component auditors').

As a result of our scoping, for the parent company we determined that an audit of the complete financial information of the UK Operations of the Bank was necessary, owing to its financial significance. For group purposes, we additionally performed an audit of the complete financial information of HSBC France. We instructed component auditors, PwC UK and PwC France, to perform the audits of these components. Our interactions with component auditors included regular communication throughout the audit, including visits to France, the issuance of instructions, a review of working papers relating to the key audit matters and formal clearance meetings. The group audit engagement partner was also the partner on the audit of the UK Operations significant component.

We then considered the significance of other reporting units in relation to primary statement account balances. In doing this we also considered the presence of any significant audit risks and other qualitative factors (including history of misstatements through fraud or error). For five reporting units, specific audit procedures were performed over selected significant account balances. For the remainder, the risk of material misstatement was mitigated through group audit procedures including testing of entity level controls and group and parent company level analytical review procedures.

Certain group-level account balances (including goodwill) were audited by the group engagement team.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

	Group financial statements	Parent company financial statements
Overall materiality	£282 million (2017: £183 million).	£235 million (2017: £183 million).
How we determined it	0.75% of Total Regulatory Capital.	0.75% of Total Regulatory Capital.
Rationale for benchmark applied	Regulatory capital is used as a benchmark as it is considered to be a key driver of HSBC's decision making process and is a primary focus for regulators.	Materiality is determined as the lower of the group materiality or 0.75% of the parent company's regulatory capital. 0.75% of the parent company's regulatory capital was lower.

In the prior year an adjusted profit before tax benchmark was used to determine materiality. However, due to the change in the nature of the group's business activities following the separation of the ring-fenced bank, the basis for determining materiality was re-evaluated and a regulatory capital based benchmark for materiality was chosen instead.

For each component in the scope of our group audit, we allocated a materiality that is less than our overall group materiality. The range of materiality allocated across components was £10m to £168m. Certain components were audited to a local statutory audit materiality that was also less than our overall group materiality.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £10 million (group audit and parent company audit) (2017: £9 million) as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

Conclusions relating to going concern

ISAs (UK) require us to report to you when:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the group's and parent company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

We have nothing to report in respect of the above matters.

However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the group's and parent company's ability to continue as a going concern.

Reporting on other information

The other information comprises all of the information in the Annual Report and Accounts 2018 other than the financial statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic Report and Report of the Directors, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on the responsibilities described above and our work undertaken in the course of the audit, ISAs (UK) require us also to report certain opinions and matters as described below.

Strategic Report and Report of the Directors

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Report of the Directors for the year ended 31 December 2018 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the group and parent company and their environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Report of the Directors.

Responsibilities for the financial statements and the audit

Responsibilities of the directors for the financial statements

As explained more fully in the Statement of Directors' Responsibilities set out on page 78, the directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group's and the parent company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

Auditors' responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

Use of this report

This report, including the opinions, has been prepared for and only for the parent company's member as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Other required reporting

Companies Act 2006 exception reporting

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- certain disclosures of directors' remuneration specified by law are not made; or
- the parent company financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Appointment

Following the recommendation of the HSBC Bank plc Audit Committee, we were appointed by the directors on 31 March 2015 to audit the financial statements for the year ended 31 December 2015 and subsequent financial periods. The period of total uninterrupted engagement is 4 years, covering the years ended 31 December 2015 to 31 December 2018.

Simon Hunt

(Senior Statutory Auditor)

for and on behalf of **PricewaterhouseCoopers LLP**

Chartered Accountants and Statutory Auditors

London

19 February 2019

Appendix: Key audit matters discussed with the Audit Committee ('AC')

The key audit matters are discussed below together with an explanation of how the audit was tailored to address these specific areas.

All key audit matters are applicable to both the group and parent company.

Application of IFRS 9 in the calculation of impairment of loans and advances

Nature of key audit matter	Matters discussed with the Audit Committee
As this is the first year of adoption of IFRS 9, there is limited experience available to back-test the charge for expected credit losses ('ECL') with actual results. There is also a significant increase in the number of data inputs required for the impairment calculation. The data is sourced from a number of systems that have not been used previously for the preparation of the accounting records. This increases risk around completeness and accuracy of certain data used to create assumptions and operate the models. The credit environment has remained benign for an extended period of time, in part due to low interest rates and relative strength of the European economy. However, there are a number of headwinds to the regional economy as well as certain country specific risks. As a result, whilst the current levels of delinquencies and defaults remains low, the risk of impairment remains significant.	At each Audit Committee and Risk Committee meeting there was a discussion on changes to risk factors and other inputs within the models, geopolitical risks, such as Brexit, as well as discussions on individually significant loan impairments. The more judgemental interpretations of IFRS 9 made by management continued to be discussed, in particular the application of forward economic guidance, including the severity and magnitude of modelled downside scenarios; and associated considerations of post model adjustments. As the control environment for the calculation of ECL under IFRS 9 continued to be strengthened following initial adoption, we provided updates on the changes being made and the results of our testing procedures.

Procedures performed to support our discussions and conclusions

Controls were tested over:
- Model performance monitoring, including periodic policy and independent model reviews, back testing of performance and approval of model changes.
- Review and challenge of multiple economic scenarios by an expert panel and internal governance committee.
- Inputs of critical data into source systems, and the flow and transformation of data between source systems to the impairment calculation engine.
- User acceptance testing over the automated calculation of ECL to ensure it is performed in line with business requirements.
- Review and challenge forums to assess the ECL output and approval of post model adjustments.
- Approval of the key inputs, assumptions and discounted cash-flows that support the significant individual impairments.

Further substantive procedures included:
- Risk based testing of models, including independent rebuild of certain assumptions.
- Testing the multiple economic scenarios and variables using our economic experts to assess their reasonableness.
- Testing of the critical data used in the year end ECL calculation.
- Review of the SAS script codes for the impairment engine against business requirements and our expectations of how the calculation should operate.
- Testing discounted cash flows for a sample of individually assessed loans including, in specific instances, using experts to assess the valuation of collateral.

Relevant references in the Annual Report and Accounts 2018

Credit Risk Disclosures, page 35.
AC Report, page 74.
Note 34: Effects of reclassifications upon adoption of IFRS9, page 158.

Execution of structural reform required by the UK Financial Services (Banking Reform) Act 2013

Nature of key audit matter

On 1 July 2018, the Retail Banking and Wealth Management, Global Private Banking, the majority of the Commercial Banking and specific elements of Global Banking and Markets divisions of HSBC Bank plc were transferred to HSBC UK Bank plc. The transfer was accounted for as a group reorganisation and predecessor accounting values applied to the balances transferred.

The separation of most financial statement line items was straightforward, however, the allocation of certain intangible assets, certain provisions and specific balances in other assets and other liabilities involved a higher degree of management judgement, specifically:

- the allocation of intangible assets based on an historic apportionment of central costs;
- the nature of underlying transactions relating to specific balances in other assets and other liabilities;
- the allocation of goodwill between the banks; and
- whether the separation of certain provisions was appropriate and reasonable.

While not requiring substantial management judgement, the allocation of customer accounts was also a key driver for assignment of multiple balances to each bank and therefore also a key area of audit focus.

Matters discussed with the Audit Committee

The application of predecessor accounting and the method of allocation of goodwill to the ring-fenced bank was reviewed and discussed with the Audit Committee.

In addition, we discussed the approach taken by management to identify and allocate customer accounts defined by regulation as core deposits, Relevant Financial Institutions and complex products. We also discussed the results of quality assurance procedures undertaken by management to test the appropriateness of the allocation process.

We discussed with the Audit Committee the appropriateness of allocations involving a higher degree of judgement. We also discussed the appropriateness of customer account allocations to either HSBC Bank plc or HSBC UK Bank plc.

We discussed the results of our controls and substantive testing, which found no material errors.

Procedures performed to support our discussions and conclusions

Controls were tested over:

- The quality assurance measures performed by management over customer allocations. Evidence corroborating the conclusions drawn by management was also obtained and reviewed.
- Internal governance over the separation of HSBC UK Bank plc from HSBC Bank plc.

Further substantive procedures included:

- We assessed the appropriateness of the accounting treatment applied by management.
- We tested the customers allocated to each entity and assessed the nature of the customers and the appropriateness of the sort-code applied.
- We recalculated the allocation of goodwill between the entities.
- We obtained an understanding of management's approach to judgemental allocations in relation to vacant space provisions. We agreed the properties to the entity fixed asset register together with the associated vacant space provision. The allocation of property to the entity fixed asset register was tested.
- For other assets and other liabilities not aligned to a specific customer, samples were selected and evidence obtained to validate the nature of the underlying transactions and corroborate the allocation.
- In relation to intangible assets aligned to more than one business line, the allocation percentage, based on predefined rates upon which all central costs are allocated, was recalculated.

Relevant references in the Annual Report and Accounts 2018

AC Report, page 74.
Economic background and outlook - Structural reform, page 18

IT Access Management

Nature of key audit matter	Matters discussed with the Audit Committee
The audit approach relies extensively on automated controls and therefore on the effectiveness of controls over IT systems. In previous years, we identified and reported that controls over access to applications, operating systems and data in the financial reporting process required improvements. Access management controls are critical to ensure that changes to applications and underlying data are made in an appropriate manner. Appropriate access controls contribute to mitigating the risk of potential fraud or errors as a result of changes to application and data. However, issues related to privileged access and business user access remained unresolved on parts of the technology infrastructure, requiring our audit approach to respond to the risks presented.	Over the past 4 years, management implemented remediation activities that have contributed to reducing the risk over access management in the financial reporting process. The status of the remediation was discussed at several Audit Committee meetings.

Procedures performed to support our discussions and conclusions

Access rights were tested over applications, operating systems and databases relied upon for financial reporting. Specifically the audit tested that:

- New access requests for joiners were properly reviewed and authorised.
- User access rights were removed on a timely basis when an individual left or moved role.
- Access rights to applications, operating systems and databases were periodically monitored for appropriateness.
- Highly privileged access was restricted to appropriate personnel.

Other areas that were independently assessed included password policies, security configurations, controls over changes to applications and databases and that business users, developers and production support did not have access to change applications, the operating system or databases in the production environment.

As a consequence of the deficiencies identified, a range of other procedures were performed:

- Where inappropriate access was identified, we understood the nature of the access, and, where possible, obtained additional evidence on the appropriateness of the activities performed.
- Additional substantive testing was performed on specific year-end reconciliations (i.e. custodian, bank account and suspense account reconciliations) and confirmations with external counterparties.
- Testing was performed on other compensating controls such as review controls undertaken by management.
- Testing was performed over toxic combination controls.
- A list of users' access permissions was obtained and manually compared to other access lists where segregation of duties was deemed to be of higher risk, for example users having access to both core banking and payments systems.

Relevant references in the Annual Report and Accounts 2018

AC Report, page 74.
Effectiveness of internal controls, page 75.

Valuation of financial instruments

Nature of key audit matter	Matters discussed with the Audit Committee
The financial instruments held by HSBC range from those that are traded daily on active markets with quoted prices, to more complex and bespoke positions. The valuation of these complex financial instruments can require the use of prices or inputs which are not readily observable in the market. Financial instruments classified as Level 3 (L3), per the IFRS 13 fair value hierarchy, are valued using some unobservable inputs. There is a risk that certain L3 portfolios are not valued appropriately due to the complexity of the trades and/or unobservability of some inputs. Valuation of the following L3 portfolios was therefore classified as a significant risk for the audit: asset-backed securities and certain long-dated interest rate derivatives.	We discussed with the Audit Committee our risk assessment with respect to valuation and the results of our controls testing. This included a number of observations on how controls may be improved including controls over valuation models. We also discussed the results of our substantive testing which included independent revaluation of a range of financial instruments, including a sample of Level 3 positions.

Procedures performed to support our discussions and conclusions

- We evaluated the design and tested the operating effectiveness of the key controls supporting the identification, measurement and oversight of the valuation of financial instruments, including the independent price verification process and governance and reporting controls. This included review of the year end independent price verification results by the HSBC Bank plc Valuation Committee.
- Methodology and underlying assumptions of key valuation adjustments, including the Credit Valuation Adjustment, Debt Valuation Adjustment and Funding Fair Value Adjustment, were assessed, and compared with our knowledge of current industry practice. Controls over the calculation of these adjustments were also tested.
- We utilised our valuation specialists to perform independent valuations to determine if management's valuations fell within a reasonable range. The revaluation covered a range of product classes and was performed across Level 1, 2 and 3 of the group's IFRS 13 fair value hierarchy. This testing specifically included a sample of Level 3 positions as at the balance sheet date. Where revaluation was not possible, alternative testing procedures were performed.
- As a response to the control findings noted, we increased the sample of independent revaluations performed.

Relevant references in the Annual Report and Accounts 2018

AC Report, page 74.
Note 11: Fair values of financial instruments carried at fair value, page 120.

Financial Statements

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Consolidated income statement

for the year ended 31 December

	Notes	2018 £m	2017 £m
Net interest income		**3,660**	6,181
– interest income		**7,422**	9,043
– interest expense		**(3,762)**	(2,862)
Net fee income	2	**2,044**	2,989
– fee income		**3,402**	4,345
– fee expense		**(1,358)**	(1,356)
Net income from financial instruments held for trading or managed on a fair value basis[3,4]	3	**2,733**	2,790
Net income/(expense) from assets and liabilities of insurance businesses, including related derivatives, measured at fair value through profit or loss[3]	3	**(604)**	602
Changes in fair value of long-term debt and related derivatives[3]	3	**5**	113
Changes in fair value of other financial instruments mandatorily measured at fair value through profit or loss[3]	3	**511**	N/A
Gains less losses from financial investments		**12**	262
Net insurance premiums	4	**2,005**	1,809
Other operating income		**580**	796
Total operating income		**10,946**	15,542
Net insurance claims incurred and movement in liabilities to policyholders	4	**(1,478)**	(2,490)
Net operating income before change in expected credit losses and other credit impairment charges[5]		**9,468**	13,052
Change in expected credit losses and other credit impairment charges	5	**(159)**	N/A
Loan impairment charges and other credit risk provisions	5	**N/A**	(495)
Net operating income		**9,309**	12,557
Total operating expenses		**(7,351)**	(10,208)
– employee compensation and benefits	6	**(2,529)**	(3,129)
– general and administrative expenses		**(4,501)**	(6,523)
– depreciation and impairment of property, plant and equipment		**(150)**	(320)
– amortisation and impairment of intangible assets	20	**(171)**	(236)
Operating profit	5	**1,958**	2,349
Share of profit in associates and joint ventures	17	**16**	21
Profit before tax[2]		**1,974**	2,370
Tax expense[4]	8	**(442)**	(528)
Profit for the year[4]		**1,532**	1,842
Profit attributable to shareholders of the parent company		**1,506**	1,809
Profit attributable to non-controlling interests		**26**	33
Profit from discontinued operations attributable to shareholders of the company[1]	35	**820**	802

1 *Profit from discontinued operations relates to profit attributable to shareholders of the group from the separation of HSBC UK Bank plc from the group. HSBC completed the ring-fencing of its UK retail banking activities on 1 July 2018, transferring qualifying RBWM, CMB and GPB customers of the group to HSBC UK Bank plc, HSBC's ring-fenced bank.*

2 *The group adopted IFRS 9 on 1 January 2018. Comparative information has not been restated, apart from the re-presentation of certain income statement line items as explained in footnote 3.*

3 *The presentation of net income from financial instruments measured at fair value through profit or loss has been revised based on the classification and measurement requirements of IFRS 9. In addition, the effect of foreign exchange exposure on certain long-term debt instruments has been included in 'Net income from financial instruments held for trading or managed on a fair value basis' from 1 January 2018. Comparative information has been re-presented. The restatement decreased 'Changes in fair value of long-term debt and related derivatives' by £402m for 2017 with an equivalent increase in 'Net income from financial instruments held for trading or managed on a fair value basis'.*

4 *We have considered market practices for the presentation of certain financial liabilities which contain both deposit and derivative components and were previously included in 'Trading liabilities'. Such liabilities amounted to £17,958m at 31 December 2017. These liabilities are classified as 'Financial liabilities designated at fair value' from 1 January 2018. Comparative information has not been restated. For 2017, a loss of £335m relating to changes in the credit risk of these liabilities was included in 'Net income from financial instruments held for trading or managed on a fair value basis' with a credit of £96m recognised in 'Tax expense'. If the change in accounting policy had been applied retrospectively, these amounts would have been recognised in other comprehensive income, thereby resulting in a net increase in profit for 2017 of £239m.*

5 *Net operating income before change in expected credit losses and other credit impairment charges is also referred to as 'revenue'.*

Consolidated statement of comprehensive income

for the year ended 31 December

	2018	2017
	£m	£m
Profit for the year	**1,532**	1,842
Other comprehensive income/(expense)		
Items that will be reclassified subsequently to profit or loss when specific conditions are met:		
Available-for-sale investments	**N/A**	84
– fair value gains	**N/A**	414
– fair value gains reclassified to the income statement	**N/A**	(354)
– amounts reclassified to the income statement in respect of impairment losses	**N/A**	26
– income taxes	**N/A**	(2)
Debt instruments at fair value through other comprehensive income	**83**	N/A
– fair value gains	**178**	N/A
– fair value gains transferred to the income statement on disposal	**(2)**	N/A
– expected credit losses recognised in the income statement	**(73)**	N/A
– income taxes	**(20)**	N/A
Cash flow hedges	**(16)**	(125)
– fair value losses	**(159)**	(133)
– fair value losses/(gains) reclassified to the income statement	**157**	(26)
– income taxes	**(14)**	34
Exchange differences	**100**	380
Items that will not be reclassified subsequently to profit or loss:		
Remeasurement of defined benefit asset/liability	**171**	1,797
– before income taxes[3,4]	**255**	2,393
– income taxes	**(84)**	(596)
Equity instruments designated at fair value through other comprehensive income	**36**	N/A
– fair value gains	**1**	N/A
– income taxes	**35**	N/A
Changes in fair value of financial liabilities designated at fair value upon initial recognition arising from changes in own credit risk[2]	**504**	(164)
– Fair value gains/(losses)	**707**	(185)
– income taxes	**(203)**	21
Other comprehensive income for the year, net of tax[2]	**878**	1,972
Total comprehensive income for the year	**2,410**	3,814
Attributable to:		
– shareholders of the parent company	**2,387**	3,772
– non-controlling interests	**23**	42
Total comprehensive income for the year[1]	**2,410**	3,814

1 *The group adopted IFRS 9 on 1 January 2018. Comparative information has not been restated.*

2 *We have considered market practices for the presentation of certain financial liabilities which contain both deposit and derivative components and were previously included in 'Trading liabilities'. Such liabilities amounted to £17,958m at 31 December 2017. These liabilities are classified as 'Financial liabilities designated at fair value' from 1 January 2018. Comparative information has not been restated. For 2017, a loss of £335m relating to changes in the credit risk of these liabilities was included in 'Net income from financial instruments held for trading or managed on a fair value basis' with a credit of £96m recognised in 'Tax expense'. If the change in accounting policy had been applied retrospectively, these amounts would have been recognised in other comprehensive income, thereby resulting in a net increase in profit for 2017 of £239m. Refer to Note 34 for further details.*

3 *An actuarial gain of £247m has arisen as a result of the remeasurement of the defined benefit pension of the HSBC Bank (UK) Pension Plan. An increase in the discount rate of 0.2%, a 0.1% reduction in the inflation assumption, and an update of demographic assumptions led to a gain of £1,073m. This was broadly offset by an adverse movement of £826m in plan assets, due to the hedged nature of the scheme. Other plans within the group, including defined benefit healthcare plans, had a net gain of £8m.*

4 *An error in an input to the actuarial model resulted in the pension liability being understated by up to an estimated £150m at 31 December 2017. This has been corrected in the 31 December 2018 position.*

Consolidated balance sheet

at 31 December

	Notes	2018 £m	2017 £m
Assets			
Cash and balances at central banks		**52,013**	97,601
Items in the course of collection from other banks		**839**	2,023
Trading assets	10	**95,420**	145,725
Financial assets designated and otherwise mandatorily measured at fair value through profit and loss	13	**17,799**	N/A
Financial assets designated at fair value	13	**N/A**	9,266
Derivatives	14	**144,522**	143,335
Loans and advances to banks		**13,628**	14,149
Loans and advances to customers		**111,964**	280,402
Reverse repurchase agreements – non-trading		**80,102**	45,808
Financial investments	15	**47,272**	58,000
Prepayments, accrued income and other assets	21	**37,497**	16,026
Current tax assets		**337**	140
Interests in associates and joint ventures	17	**399**	327
Goodwill and intangible assets	20	**2,626**	5,936
Deferred tax assets	8	**540**	130
Total assets[1]		**604,958**	818,868
Liabilities and equity			
Liabilities			
Deposits by banks		**24,532**	29,349
Customer accounts		**180,836**	381,546
Repurchase agreements – non-trading		**46,583**	37,775
Items in the course of transmission to other banks		**351**	1,089
Trading liabilities	22	**49,514**	106,496
Financial liabilities designated at fair value	23	**36,922**	18,249
Derivatives	14	**139,932**	140,070
Debt securities in issue		**22,721**	13,286
Accruals, deferred income and other liabilities	24	**41,036**	6,615
Current tax liabilities		**128**	88
Liabilities under insurance contracts	4	**20,657**	21,033
Provisions	25	**538**	1,796
Deferred tax liabilities	8	**29**	933
Subordinated liabilities	26	**13,770**	16,494
Total liabilities[1]		**577,549**	774,819
Equity			
Total shareholders' equity		**26,878**	43,462
– called up share capital	29	**797**	797
– other equity instruments	29	**2,403**	3,781
– other reserves		**(4,971)**	2,744
– retained earnings		**28,649**	36,140
Non-controlling interests		**531**	587
Total equity[1]		**27,409**	44,049
Total liabilities and equity[1]		**604,958**	818,868

1 *The group adopted IFRS 9 together with voluntary changes to accounting policy and presentation on 1 January 2018. Comparative information has not been restated. For further details, refer to Note 34 'Effects of reclassifications upon adoption of IFRS 9'.*

The accompanying notes on pages 97 to 165, and the audited sections of the 'Financial summary' on pages 10 to 15 and the 'Report of the Directors' on pages 20 to 77 form an integral part of these financial statements.

The financial statements on pages 87 to 96 were approved by the Board of Directors on 19 February 2019 and signed on its behalf by:

J Fleurant

Director

Consolidated statement of cash flows

for the year ended 31 December

	2018	2017
	£m	£m
Profit before tax	**1,974**	2,370
Adjustments for non-cash items		
Depreciation, amortisation and impairment of intangible assets	**321**	556
Net gain from investing activities	**(14)**	(314)
Share of profits in associates and joint ventures	**(16)**	(21)
Gain on disposal of subsidiaries, businesses, associates and joint ventures	**—**	(61)
Change in expected credit losses gross of recoveries and other credit impairment charges	**220**	N/A
Loan impairment losses gross of recoveries and other credit risk provisions	**N/A**	877
Provisions including pensions	**(41)**	170
Share-based payment expense	**99**	114
Other non-cash items included in profit before tax	**40**	(130)
Elimination of exchange differences[1]	**(2,074)**	67
Changes in operating assets and liabilities	**(670)**	11,458
– change in net trading securities and derivatives	**7,837**	(1,828)
– change in loans and advances to banks and customers	**(6,377)**	(5,605)
– change in reverse repurchase agreements – non-trading	**(22,893)**	(9,792)
– change in financial assets designated and otherwise mandatorily measured at fair value	**(2,246)**	(921)
– change in other assets	**(1,769)**	(415)
– change in deposits by banks and customer accounts	**(347)**	15,381
– change in repurchase agreements – non-trading	**8,807**	18,065
– change in debt securities in issue	**9,435**	(2,854)
– change in financial liabilities designated at fair value	**1,982**	(400)
– change in other liabilities	**5,394**	968
– contributions paid to defined benefit plans	**(20)**	(233)
– tax paid	**(473)**	(908)
Net cash from operating activities	**(161)**	15,086
– purchase of financial investments	**(29,235)**	(16,573)
– proceeds from the sale and maturity of financial investments	**26,888**	39,990
– net cash flows from the purchase and sale of property, plant and equipment	**(111)**	(304)
– net investment in intangible assets	**(433)**	(357)
– net cash outflow from acquisition of businesses and subsidiaries	**(227)**	(43)
– net cash flow on disposal of subsidiaries, business, associates and joint ventures[4]	**(29,371)**	(19)
Net cash from investing activities	**(32,489)**	22,694
– issue of ordinary share capital and other equity instruments	**818**	—
– subordinated loan capital issued[2]	**12,274**	10,092
– subordinated loan capital repaid[2]	**(12,765)**	(1,251)
– dividends paid to shareholders of the parent company	**(13,044)**	(873)
– funds received from the shareholder of the parent company	**3,512**	1,081
– dividends paid to non-controlling interests	**(28)**	(22)
Net cash from financing activities	**(9,233)**	9,027
Net (decrease)/increase in cash and cash equivalents	**(41,883)**	46,807
Cash and cash equivalents at 1 Jan	**129,737**	82,037
Exchange difference in respect of cash and cash equivalents	**1,148**	893
Cash and cash equivalents at 31 Dec	**89,002**	129,737
Cash and cash equivalents comprise of[3]:		
– cash and balances at central banks	**52,013**	97,601
– items in the course of collection from other banks	**839**	2,023
– loans and advances to banks of one month or less	**6,333**	5,381
– reverse repurchase agreement with banks of one month or less	**22,928**	11,528
– treasury bills, other bills and certificates of deposit less than three months	**7,240**	14,293
– less: items in the course of transmission to other banks	**(351)**	(1,089)
Cash and cash equivalents at 31 Dec	**89,002**	129,737

1 *Adjustment to bring changes between opening and closing balance sheet amounts to average rates. This is not done on a line-by-line basis, as details cannot be determined without unreasonable expense.*
2 *Subordinated liabilities changes during the year are attributable to cash flows from issuance (£12,274m (2017: £10,092m)) and repayment (£(12,765)m (2017: £(1,251)m)) of securities as presented in the Consolidated statement of cash flows. Non-cash changes during the year included foreign exchanges gains/(losses) (£112m (2017: £(463)m)) and fair value gains/(losses) (£(132)m (2017: £94m)).*
3 *At 31 December 2018, £1,410m (2017: £4,159m) was not available for use by the group, of which £1,410m (2017: £1,585m) related to mandatory deposits at central banks.*
4 *No cash or cash equivalent was received as part of the Part VII transfer of asset and liabilities. The aggregate amount of cash and cash equivalent in the subsidiaries and other businesses over which control transferred was £29,410m.*

Interest received was £8,034m (2017: £10,172m), interest paid was £3,177m (2017: £2,650m) and dividends received were £938m (2017: £1,332m).

Consolidated statement of changes in equity

for the year ended 31 December

				Other reserves						
	Called up share capital and share premium	Other equity instruments	Retained earnings	Financial assets at FVOCI reserve	Cash flow hedging reserve	Foreign exchange reserve	Group reorganisation reserve (GRR)	Total share-holders' equity	Non-controlling interests	Total equity
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
At 31 Dec 2017	797	3,781	36,140	1,099	(38)	1,683	—	43,462	587	44,049
Impact on transition to IFRS 9	—	—	(283)	(249)	—	—	—	(532)	—	(532)
At 1 Jan 2018[1]	797	3,781	35,857	850	(38)	1,683	—	42,930	587	43,517
Profit for the period	—	—	1,506	—	—	—	—	1,506	26	1,532
Other comprehensive income (net of tax)	—	—	677	126	(16)	94	—	881	(3)	878
– debt instruments at fair value through other comprehensive income	—	—	—	90	—	—	—	90	(7)	83
– equity instruments designated at fair value through other comprehensive income	—	—	—	36	—	—	—	36	—	36
– cash flow hedges	—	—	—	—	(16)	—	—	(16)	—	(16)
– changes in fair value of financial liabilities designated at fair value due to movement in own credit risk[2]	—	—	504	—	—	—	—	504	—	504
– remeasurement of defined benefit asset/liability[3]	—	—	173	—	—	—	—	173	(2)	171
– exchange differences	—	—	—	—	—	94	—	94	6	100
Total comprehensive income for the year	—	—	2,183	126	(16)	94	—	2,387	23	2,410
Capital securities issued during the period[4]	—	818	—	—	—	—	—	818	—	818
Dividends to shareholders[5]	—	—	(13,044)	—	—	—	—	(13,044)	(28)	(13,072)
Transfer[6]	—	(2,196)	—	—	—	—	—	(2,196)	—	(2,196)
Net impact of equity-settled share-based payments	—	—	17	—	—	—	—	17	—	17
Capital contribution[7]	—	—	3,377	—	—	—	—	3,377	—	3,377
Change in business combinations and other movements[8]	—		218	(3)	—	—	—	215	(51)	164
Tax on items taken directly to equity	—	—	41	—	—	—	—	41	—	41
Group reorganisation reserve (GRR)[9]	—	—	—	(4)	29	—	(7,692)	(7,667)	—	(7,667)
At 31 Dec 2018	797	2,403	28,649	969	(25)	1,777	(7,692)	26,878	531	27,409

Consolidated statement of changes in equity (continued)

for the year ended 31 December

					Other reserves					
	Called up share capital	Share premium	Other equity instruments	Retained earnings	Available-for-sale fair value reserve	Cash flow hedging reserve	Foreign exchange reserve	Total share-holders' equity	Non-controlling interests	Total equity
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
At 1 Jan 2017	797	20,733	3,781	12,737	1,007	89	786	39,930	695	40,625
Profit for the year	—	—	—	1,809	—	—	—	1,809	33	1,842
Other comprehensive income (net of tax)	—	—	—	1,632	92	(125)	364	1,963	9	1,972
– available-for-sale investments	—	—	—	—	92	—	—	92	(8)	84
– cash flow hedges	—	—	—	—	—	(125)	—	(125)	—	(125)
– remeasurement of defined benefit asset/liability	—	—	—	1,796	—	—	—	1,796	1	1,797
– changes in fair value of financial liabilities designated at fair value due to movement in own credit risk	—	—	—	(164)	—	—	—	(164)	—	(164)
– exchange differences and other	—	—	—	—	—	—	364	364	16	380
Total comprehensive income for the year	—	—	—	3,441	92	(125)	364	3,772	42	3,814
Dividends to shareholders	—	—	—	(872)	—	—	—	(872)	(22)	(894)
Distribution in-specie of HSBC Bank A.S.[10]	—	—	—	(1,174)	—	(2)	533	(643)	—	(643)
Net impact of equity-settled share-based payments	—	—	—	(21)	—	—	—	(21)	—	(21)
Transfer of share premium to retained earnings[11]	—	(20,733)	—	20,733	—	—	—	—	—	—
Change in business combinations and other movements	—	—	—	1,241	—	—	—	1,241	(128)	1,113
Tax on items taken directly to equity	—	—	—	55	—	—	—	55	—	55
At 31 Dec 2017	797	—	3,781	36,140	1,099	(38)	1,683	43,462	587	44,049

1 *Balances at 1 January 2018 have been prepared in accordance with accounting policies referred to on page 97. 31 December 2017 balances have not been represented.*
2 *At 1 January 2018, the cumulative changes in fair value attributable to changes in own credit risk of financial liabilities designated at fair value was a loss of £312m.*
3 *An actuarial gain has arisen as a result of the remeasurement of the defined benefit pension obligation of the HSBC Bank (UK) Pension Scheme.*
4 *HSBC Bank plc issued additional tier 1 capital instruments of £818m to HSBC Holdings plc in March 2018. See Note 29 for further details.*
5 *The dividend to shareholders includes a £12,000m dividend distributed to HSBC Holdings plc in July 2018 to capitalise HSBC UK Bank plc. See Note 9 for further details of the remaining £1,044m dividend paid to shareholders.*
6 *HSBC Bank plc transferred two additional tier 1 capital instruments of £2,196m to HSBC UK Bank plc in July 2018.*
7 *HSBC Holdings plc injected £1,900m of CET1 capital into HSBC Bank plc during March 2018. There was no new issuance of share capital. In December 2018 HSBC UK Holdings Ltd injected £1,477m of CET1 capital into HSBC Bank plc. There was no new issuance of share capital.*
8 *HSBC Holdings plc provided £135m to HSBC Bank plc for the acquisition of HSBC Investment Bank Holdings Limited and its subsidiaries from HSBC Holdings plc in January 2018. The difference between the cost of investment and the net assets on acquisition was recognised as a further capital contribution of £102m.*
9 *The Group reorganisation reserve ('GRR') of £7,692m is an accounting reserve, which relates primarily to the recognition of goodwill (£3,285m) and the pension asset net of deferred tax (£4,776m), resulting from the ring-fencing implementation. The GRR does not form part of regulatory capital. For further details refer to Note 35.*
10 *The distribution in-specie of HSBC Bank A.S. comprises of the return of cost of investment in HSBC Bank A.S.*
11 *On 15 March 2017, the High Court confirmed the conversion of the share premium in full to distributable reserves by means of a capital reduction.*

HSBC Bank plc balance sheet

at 31 December

	Notes	2018 £m	2017 £m
Assets			
Cash and balances at central banks		**40,657**	81,358
Items in the course of collection from other banks		**442**	1,407
Trading assets	10	**77,765**	124,094
Financial assets designated and otherwise mandatorily measured at fair value through profit and loss		**5,745**	N/A
Derivatives	14	**139,229**	135,236
Loans and advances to banks		**12,686**	15,160
Loans and advances to customers		**58,783**	220,450
Reverse repurchase agreements – non-trading		**56,495**	36,627
Financial investments	15	**26,699**	31,382
Prepayments, accrued income and other assets	21	**30,488**	12,858
Current tax assets		**278**	195
Interests in associates and joint ventures	17	**–**	5
Investments in subsidiary undertakings	18	**7,215**	8,476
Goodwill and intangible assets	20	**500**	1,048
Deferred tax assets	8	**447**	5
Total assets[1]		**457,429**	668,301
Liabilities and equity			
Liabilities			
Deposits by banks		**18,148**	24,626
Customer accounts		**125,871**	320,026
Repurchase agreements – non-trading		**35,693**	35,220
Items in the course of transmission to other banks		**83**	600
Trading liabilities	22	**27,301**	77,303
Financial liabilities designated at fair value	23	**22,931**	11,006
Derivatives	14	**135,307**	133,035
Debt securities in issue		**19,085**	6,108
Accruals, deferred income and other liabilities	24	**35,150**	3,367
Current tax liabilities		**40**	54
Provisions	25	**400**	1,394
Deferred tax liabilities	8	**2**	932
Subordinated liabilities	26	**13,323**	15,930
Total liabilities[1]		**433,334**	629,601
Equity			
Called up share capital	29	**797**	797
Other equity instruments	29	**2,403**	3,781
Other reserves		**(5,138)**	277
Retained earnings		**26,033**	33,845
Total equity[1]		**24,095**	38,700
Total liabilities and equity[1]		**457,429**	668,301

1 *The group adopted IFRS 9 together with voluntary changes to accounting policy and presentation on 1 January 2018. Comparative information has not been restated. For further details, refer to Note 34 'Effects of reclassifications upon adoption of IFRS 9'.*

Profit after tax for the year was £1,411m (2017: £2,565m).

The accompanying notes on pages 97 to 165, and the audited sections of the 'Report of the Directors' on pages 20 to 77 form an integral part of these financial statements.

The financial statements on pages 87 to 96 were approved by the Board of Directors on 19 February 2019 and signed on its behalf by:

J Fleurant

Director

HSBC Bank plc statement of cash flows

for the year ended 31 December

	2018	2017
	£m	£m
Profit before tax	**1,699**	2,898
Adjustments for non-cash items		
Depreciation, amortisation and impairment of intangible assets	**238**	460
Net gain from investing activities	**(24)**	(208)
Gain on disposal of subsidiaries, businesses, associates and joint ventures	**—**	(61)
Change in expected credit losses gross of recoveries and other credit impairment charges	**294**	N/A
Loan impairment losses gross of recoveries and other credit risk provisions	**N/A**	548
Provisions including pensions	**(113)**	37
Share-based payment expense	**74**	85
Other non-cash items included in profit before tax	**25**	17
Elimination of exchange differences[1]	**(1,578)**	826
Changes in operating assets and liabilities	**(2,055)**	5,619
– change in net trading securities and derivatives	**7,860**	(12,326)
– change in loans and advances to banks and customers	**(4,001)**	(3,695)
– change in reverse repurchase agreements – non-trading	**(18,033)**	(10,416)
– change in financial assets designated and otherwise mandatorily measured at fair value	**(2,032)**	—
– change in other assets	**(2,566)**	80
– change in deposits by banks and customer accounts	**(220)**	14,773
– change in repurchase agreements – non-trading	**472**	19,801
– change in debt securities in issue	**12,977**	(758)
– change in financial liabilities designated at fair value	**(2,183)**	692
– change in other liabilities	**6,063**	(1,685)
– contributions paid to defined benefit plans	**(20)**	(233)
– tax paid	**(372)**	(614)
Net cash from operating activities	**(1,440)**	10,221
– purchase of financial investments	**(23,545)**	(12,624)
– proceeds from the sale and maturity of financial investments	**17,303**	28,834
– net cash flows from the purchase and sale of property, plant and equipment	**(75)**	(168)
– net investment in intangible assets	**(295)**	(276)
– net cash outflow from acquisition of businesses and subsidiaries	**—**	(1)
– net cash flow on disposal of subsidiaries, business, associates and joint ventures	**(29,246)**	599
Net cash from investing activities	**(35,858)**	16,364
– issue of ordinary share capital and other equity instruments	**818**	—
– subordinated loan capital issued[2]	**12,274**	10,067
– subordinated loan capital repaid[2]	**(12,726)**	(1,085)
– funds received from the shareholder of the parent company	**3,512**	1,081
– dividends paid to shareholders of the parent company	**(13,044)**	(1,368)
Net cash from financing activities	**(9,166)**	8,695
Net (decrease)/increase in cash and cash equivalents	**(46,464)**	35,280
Cash and cash equivalents at 1 Jan	**106,067**	70,344
Exchange difference in respect of cash and cash equivalents	**817**	443
Cash and cash equivalents at 31 Dec	**60,420**	106,067
Cash and cash equivalents comprise of:		
– cash and balances at central banks	**40,657**	81,358
– items in the course of collection from other banks	**442**	1,407
– loans and advances to banks of one month or less	**3,764**	4,264
– reverse repurchase agreement with banks of one month or less	**8,829**	6,995
– treasury bills, other bills and certificates of deposit less than three months	**6,811**	12,643
– less: items in the course of transmission to other banks	**(83)**	(600)
Cash and cash equivalents at 31 Dec	**60,420**	106,067

1 *Adjustment to bring changes between opening and closing balance sheet amounts to average rates. This is not done on a line-by-line basis, as details cannot be determined without unreasonable expense.*

2 *Subordinated liabilities changes during the year are attributable to cash flows from issuance (£12,274m (2017: £10,067m)) and repayment (£(12,726)m (2017: £(1,085)m)) of securities as presented in the bank's statement of cash flows. Non-cash changes during the year included foreign exchanges gain(losses) (£108m (2017: £(110)m)) and fair value gains(losses) (£(150)m (2017: £94m)).*

Interest received was £6,328m (2017: £7,498m), interest paid was £2,304m (2017: £1,634m) and dividends received was £905m (2017: £1,294m).

HSBC Bank plc statement of changes in equity

for the year ended 31 December

	Called up share capital and share premium	Other equity instruments	Retained earnings	Other reserves				Total shareholders' equity
				Financial assets at FVOCI reserve	Cash flow hedging reserve	Foreign exchange reserve	Group reorganisation reserve (GRR)	
	£m	£m	£m	£m	£m	£m	£m	£m
At 31 Dec 2017	**797**	**3,781**	**33,845**	**190**	**(18)**	**105**	–	**38,700**
Impact on transition to IFRS 9	—	—	(227)	(163)	—	—	—	(390)
At 1 Jan 2018[1]	**797**	**3,781**	**33,618**	**27**	**(18)**	**105**	**—**	**38,310**
Profit for the year	—	—	1,411	—	—	—	—	1,411
Other comprehensive income (net of tax)	—	—	543	33	(58)	(25)	—	493
– debt instruments at fair value through other comprehensive income	—	—	—	(3)	—	—	—	(3)
– equity instruments designated at fair value through other comprehensive income	—	—	—	36	—	—	—	36
– cash flow hedges	—	—	—	—	(58)	—	—	(58)
– changes in fair value of financial liabilities designated at fair value due to movement in own credit risk[2]	—	—	364	—	—	—	—	364
– remeasurement of defined benefit asset/ liability[3]	—	—	179	—	—	—	—	179
– exchange differences	—	—	—	—	—	(25)	—	(25)
Total comprehensive income for the period	—	—	1,954	33	(58)	(25)	—	1,904
Capital securities issued during the period[4]	—	818	—	—	—	—	—	818
Dividends to shareholders[5]	—	—	(13,044)	—	—	—	—	(13,044)
Transfers[6]	—	(2,196)	—	—	—	—	—	(2,196)
Net impact of equity-settled share-based payments	—	—	12	—	—	—	—	12
Capital contribution[7]	—	—	3,377	—	—	—	—	3,377
Change in business combinations and other movements	—	—	75	21	—	—	—	96
Tax on items taken directly to equity	—	—	41	—	—	—	—	41
Group reorganisation reserve (GRR)[8]	—	—	—	(4)	29	—	(5,248)	(5,223)
At 31 Dec 2018	**797**	**2,403**	**26,033**	**77**	**(47)**	**80**	**(5,248)**	**24,095**

HSBC Bank plc statement of changes in equity (continued)

for the year ended 31 December

					Other reserves			
	Called up share capital	Share premium	Other equity instruments	Retained earnings	Available- for-sale fair value reserve	Cash flow hedging reserve	Foreign exchange reserve	Total share-holders' equity
	£m	£m	£m	£m	£m	£m	£m	£m
At 1 Jan 2017	797	20,733	3,781	9,007	218	137	73	34,746
Profit for the year	—	—	—	2,565	—	—	—	2,565
Other comprehensive income (net of tax)	—	—	—	1,641	(28)	(155)	32	1,490
– available-for-sale investments	—	—	—	—	(28)	—	—	(28)
– cash flow hedges	—	—	—	—	—	(155)	—	(155)
– remeasurement of defined benefit asset/ liability	—	—	—	1,790	—	—	—	1,790
– changes in fair value of financial liabilities designated at fair value due to movement in own credit risk	—	—	—	(149)	—	—	—	(149)
– exchange differences and other	—	—	—	—	—	—	32	32
Total comprehensive income for the year from continued operations	—	—	—	4,206	(28)	(155)	32	4,055
Dividends to shareholders	—	—	—	(872)	—	—	—	(872)
Distribution in specie of HSBC Bank A.S.[9]	—	—	—	(496)	—	—	—	(496)
Net impact of equity-settled share-based payments	—	—	—	(20)	—	—	—	(20)
Transfer of share premium to retained earnings[10]	—	(20,733)	—	20,733	—	—	—	—
Change in business combinations and other movements	—	—	—	1,232	—	—	—	1,232
Tax on items taken directly to equity	—	—	—	55	—	—	—	55
At 31 Dec 2017	797	—	3,781	33,845	190	(18)	105	38,700

1 Balances at 1 January 2018 have been prepared in accordance with accounting policies referred to on page 97. 31 December 2017 balances have not been represented.
2 At 1 January 2018, the cumulative changes in fair value attributable to changes in own credit risk of financial liabilities designated at fair value was a loss of £204m.
3 An actuarial gain has arisen as a result of the remeasurement of the defined benefit pension obligation of the HSBC Bank (UK) Pension Scheme. Refer to Note 6 for further details.
4 HSBC Bank plc issued additional tier 1 capital instruments of £818m to HSBC Holdings plc in March 2018. See Note 29 for further details.
5 The dividend to shareholders includes a £12,000m dividend distributed to HSBC Holdings plc in July 2018 to capitalise HSBC UK Bank plc. See Note 9 for further details of the remaining £1,044m dividend paid tp shareholders.
6 HSBC Bank plc transferred two additional tier 1 capital instruments of £2,196m to HSBC UK Bank plc in July 2018.
7 HSBC Holdings plc injected £1,900m of CET1 capital into HSBC Bank plc during March 2018. There was no new issuance of share capital. In December 2018 HSBC UK Holdings Ltd injected £1,477m of CET1 capital into HSBC Bank plc. There was no new issuance of share capital.
8 The Group reorganisation reserve ('GRR') of £5,248m is an accounting reserve, which relates primarily to the recognition of goodwill (£223m) and the pension asset net of deferred tax (£4,776m), resulting from the ring-fencing implementation. The GRR does not form part of regulatory capital. For further details refer to Note 35.
9 The distribution in-specie of HSBC Bank A.S. comprises of the return of cost of investment in HSBC Bank A.S.
10 On 15 March 2017, the High Court confirmed the conversion of the share premium in full to distributable reserves by means of a capital reduction.

Notes on the Financial Statements

1 Basis of preparation and significant accounting policies

1.1 Basis of preparation

(a) Compliance with International Financial Reporting Standards

The consolidated financial statements of the group and the separate financial statements of HSBC Bank plc have been prepared in accordance with International Financial Reporting Standards ('IFRSs') as issued by the International Accounting Standards Board ('IASB'), including interpretations issued by the IFRS Interpretations Committee, and as endorsed by the European Union ('EU'). At 31 December 2018, there were no unendorsed standards effective for the year ended 31 December 2018 affecting these consolidated and separate financial statements, and the group's application of IFRSs results in no differences between IFRSs as issued by the IASB and IFRSs as endorsed by the EU.

Standards adopted during the year ended 31 December 2018

The group has adopted the requirements of IFRS 9 'Financial Instruments' from 1 January 2018, with the exception of the provisions relating to the presentation of gains and losses on financial liabilities designated at fair value, which were adopted from 1 January 2017. This includes the adoption of 'Prepayment Features with Negative Compensation ('Amendments to IFRS 9') which is effective for annual periods beginning on or after 1 January 2019 with early adoption permitted. The effect of its adoption is not considered to be significant. IFRS 9 includes an accounting policy choice to remain with IAS 39 hedge accounting, which HSBC has exercised. The classification and measurement, and impairment requirements are applied retrospectively by adjusting the opening balance sheet at the date of initial application. As permitted by the transitional requirements of IFRS 9, comparatives have not been restated. Adoption reduced net assets at 1 January 2018 by £532m as set out in Note 34.

In addition, the group has adopted the requirements of IFRS 15 'Revenue from contracts with customers' and a number of interpretations and amendments to standards, which have had an insignificant effect on the consolidated financial statements of the group and the separate financial statements of HSBC Bank plc.

IFRS 9 transitional requirements

The transitional requirements of IFRS 9 necessitated a review of the designation of financial instruments at fair value. IFRS 9 requires that the designation is revoked where there is no longer an accounting mismatch at 1 January 2018 and permits designations to be revoked or additional designations created at 1 January 2018 if there are accounting mismatches at that date. As a result:

- fair value designations for financial liabilities were revoked where the accounting mismatch no longer exists, as required by IFRS 9; and
- fair value designations were revoked for certain long-dated securities where accounting mismatches continue to exist, but where HSBC has revoked the designation as permitted by IFRS 9 since it will better mitigate the accounting mismatch by undertaking fair value hedge accounting. The results of these changes are included in the reconciliation set out in Note 34.

Changes in accounting policy

While not necessarily required by the adoption of IFRS 9, the following voluntary changes in accounting policy and presentation were made as a result of reviews carried out in conjunction with its adoption. The effect of presentational changes at 1 January 2018 is included in the reconciliation set out in Note 34 and comparatives have not been restated.

- We considered market practices for the presentation of certain financial liabilities which contain both deposit and derivative components. We concluded that it would be appropriate to change the accounting policy and presentation of 'trading customer accounts and other debt securities in issue' to better align with the presentation of similar financial instruments by peers. This would therefore provide more relevant information about the effect of these financial liabilities on our financial position and performance. As a result, rather than being classified as held for trading, we will designate these financial liabilities as at fair value through profit or loss since they are managed and their performance evaluated on a fair value basis. A further consequence of this change in presentation is that the effects of changes in the liabilities' credit risk will be presented in 'Other comprehensive income' with the remaining effect presented in profit or loss in accordance with group accounting policy adopted in 2017 (following the adoption of the requirements in IFRS 9 relating to the presentation of gains and losses on financial liabilities designated at fair value).
- Cash collateral, margin and settlement accounts have been reclassified from 'Trading assets' and 'Loans and advances to banks and customers' to 'Prepayments, accrued income and other assets' and from 'Trading liabilities' and 'Deposits by banks' and 'Customer accounts' to 'Accruals, deferred income and other liabilities'. The change in presentation for financial assets is in accordance with IFRS 9 and the change in presentation for financial liabilities is considered to provide more relevant information, given the change in presentation for the financial assets. The change in presentation for financial liabilities has had no effect on the measurement of these items and therefore on retained earnings or profit for any period.
- Certain stock borrowing assets have been reclassified from 'Loans and advances to banks and customers' to 'Trading assets'. The change in measurement is a result of the determination of the global business model for this activity and will align the presentation throughout HSBC Group.
- Prior to 2018, foreign exchange exposure on some financial instruments designated at fair value was presented in the same line in the income statement as the underlying fair value movement on these instruments. In 2018, we have grouped the presentation of the entire effect of foreign exchange exposure in profit or loss and presented it within 'Net income from financial instruments held for trading or managed on a fair value basis'. Comparative data has been re-presented.

(b) Separation of the Ring-fenced bank

In order to meet HSBC Holdings plc's UK ring-fencing obligations in accordance with the UK Banking Reform Act, on 1 July 2018, HSBC Bank plc's UK Retail and SME operations were legally separated into a ring-fenced bank, HSBC UK Bank plc. This legal separation resulted in the split of the ring-fenced businesses in accordance with the application made to the High Court. The transfer of the various assets and liabilities making up the ring-fenced bank followed a variety of legal mechanisms (the most significant mechanism being a

transfer under Part VII of the Financial Services and Markets Act 2000). Further information is set out in Note 35 Discontinued operations.

The separation results in the creation of an equity reserve used to recognise the distribution of equity reserves associated with the ring-fenced businesses which are notionally transferred from HSBC Bank plc. It reflects the distribution of net assets or OCI reserves which were not compensated for through cash or high quality liquid assets.

(c) Future accounting developments

Minor amendments to IFRSs

The IASB published a number of minor amendments to IFRSs which are effective from 1 January 2019, some of which have been endorsed for use in the EU. The group expects they will have an insignificant effect, when adopted, on the consolidated financial statements of the group and the separate financial statements of HSBC Bank plc.

Major new IFRSs

The IASB has published IFRS 16 'Leases' and IFRS 17 'Insurance Contracts'. IFRS 16 has been endorsed for use in the EU and IFRS 17 has not yet been endorsed . In addition, an amendment to IAS 12 'Income Taxes' has not yet been endorsed.

IFRS 16 'Leases'

IFRS 16 'Leases' has an effective date for annual periods beginning on or after 1 January 2019. IFRS 16 results in lessees accounting for most leases within the scope of the standard in a manner similar to the way in which finance leases are currently accounted for under IAS 17 'Leases'. Lessees will recognise a right of use ('ROU') asset and a corresponding financial liability on the balance sheet. The asset will be amortised over the length of the lease, and the financial liability measured at amortised cost. Lessor accounting remains substantially the same as under IAS 17. At 1 January 2019, HSBC Group expects to adopt the standard using a modified retrospective approach where the cumulative effect of initially applying it is recognised as an adjustment to the opening balance of retained earnings and comparatives are not restated. The implementation is expected to increase assets by approximately £0.9bn in the group (£0.6bn in the separate financial statements of HSBC Bank plc) and increase liabilities by the same amounts with no effect on net assets or retained earnings.

IFRS 17 'Insurance Contracts'

IFRS 17 'Insurance Contracts' was issued in May 2017, and sets out the requirements that an entity should apply in accounting for insurance contracts it issues and reinsurance contracts it holds. IFRS17 is currently effective from 1 January 2021. However, the IASB is considering delaying the mandatory implementation date by one year and may make additional changes to the standard. The group is in the process of implementing IFRS17. Industry practice and interpretation of the standard are still developing and there may be changes to it, therefore the likely impact of its implementation remains uncertain.

Amendment to IAS 12 'Income Taxes'

An amendment to IAS 12 was issued in December 2017 as part of the annual improvement cycle. The amendment clarifies that an entity should recognise the tax consequences of dividends in the same place where the transactions or events that generated the distributable profits are recognised. This amendment is effective for the annual periods beginning on or after 1 January 2019 and is applied to the income tax consequences of distributions recognised on or after the beginning of the earliest comparative period. As a result of its application, the income tax consequences of distributions on certain capital securities classified as equity will be presented in profit or loss rather than directly in equity. If the amendment had been applied in 2018 the impact for the year ended 31 December 2018 would have been £49m increase in profit after tax (2017: £55m) with no affect on equity.

(d) Foreign currencies

The functional currency of the bank is sterling, which is also the presentational currency of the consolidated financial statements of the group.

Transactions in foreign currencies are recorded at the rate of exchange on the date of the transaction. Assets and liabilities denominated in foreign currencies are translated at the rate of exchange at the balance sheet date except non-monetary assets and liabilities measured at historical cost, which are translated using the rate of exchange at the initial transaction date. Exchange differences are included in other comprehensive income or in the income statement depending on where the gain or loss on the underlying item is recognised.

In the consolidated financial statements, the assets, liabilities and results of foreign operations, whose functional currency is not sterling, are translated into the group's presentation currency at the reporting date. Exchange differences arising are recognised in other comprehensive income. On disposal of a foreign operation, exchange differences previously recognised in other comprehensive income are reclassified to the income statement.

(e) Presentation of information

Certain disclosures required by IFRSs have been included in the audited sections of this *Annual Report and Accounts* as follows:

- segmental disclosures are included in the 'Strategic Report: Financial Summary' on pages 10 to 15;
- disclosures concerning the nature and extent of risks relating to financial instruments and insurance contracts are included in the 'Report of the Directors: Risk' on pages 26 to 68;
- capital disclosures are included in the 'Report of the Directors: Capital' on pages 69 to 70; and
- disclosures relating to HSBC's securitisation activities and structured products are included in the 'Report of the Directors: Risk' on pages 54 and 55.
- in publishing the parent company financial statements together with the group financial statements, the bank has taken advantage of the exemption in section 408(3) of the Companies Act 2006 not to present its individual income statement and related notes.

(f) Critical accounting estimates and judgements

The preparation of financial information requires the use of estimates and judgements about future conditions. In view of the inherent uncertainties and the high level of subjectivity involved in the recognition or measurement of items highlighted as the critical accounting estimates and judgements in section 1.2 below, it is possible that the outcomes in the next financial year could differ from those on which management's estimates are based. This could result in materially different estimates and judgements from those reached by management for the purposes of the these financial statements. Management's selection of the group's accounting policies

that contain critical estimates and judgements reflects the materiality of the items to which the policies are applied and the high degree of judgement and estimation uncertainty involved.

(g) Segmental analysis

HSBC Bank plc's chief operating decision maker is the group Chief Executive, supported by the group Executive Committee, and operating segments are reported in a manner consistent with the internal reporting provided to the group Chief Executive and the group Executive Committee.

Measurement of segmental assets, liabilities, income and expenses is in accordance with the bank's accounting policies. Segmental income and expenses include transfers between segments and these transfers are conducted at arm's length. Shared costs are included in segments on the basis of the actual recharges made.

The types of products and services from which each reportable segment derives its revenue are discussed in the 'Strategic Report – Products and services'.

(h) Going concern

The financial statements are prepared on a going concern basis, as the Directors are satisfied that the group and bank have the resources to continue in business for the foreseeable future. In making this assessment, the Directors have considered a wide range of information relating to present and future conditions, including future projections of profitability, cash flows and capital resources.

1.2 Summary of significant accounting policies

(a) Consolidation and related policies

Investments in subsidiaries

Where an entity is governed by voting rights, the group consolidates when it holds - directly or indirectly - the necessary voting rights to pass resolutions by the governing body. In all other cases, the assessment of control is more complex and requires judgement of other factors, including having exposure to variability of returns, power to direct relevant activities and whether power is held as agent or principal.

Business combinations are accounted for using the acquisition method. The amount of non-controlling interest is measured either at fair value or at the non-controlling interest's proportionate share of the acquiree's identifiable net assets.

The bank's investments in subsidiaries are stated at cost less impairment losses.

Critical accounting estimates and judgements

Investments in subsidiaries are tested for impairment when there is an indication that the investment may be impaired. Impairment testing involves significant judgement in determining the value in use ('VIU'), and in particular estimating the present values of cash flows expected to arise from continuing to hold the investment and the rates used to discount these cash flows.

Goodwill

Goodwill is allocated to cash-generating units ('CGUs') for the purpose of impairment testing, which is undertaken at the lowest level at which goodwill is monitored for internal management purposes. The group's CGUs are based on global businesses. Impairment testing is performed once a year, or whenever there is an indication of impairment, by comparing the recoverable amount of a CGU with its carrying amount.

Goodwill is included in a disposal group if the disposal group is a CGU to which goodwill has been allocated or it is an operation within such a CGU. The amount of goodwill included in a disposal group is measured on the basis of the relative values of the operation disposed of and the portion of the CGU retained.

Critical accounting estimates and judgements

The review of goodwill for impairment reflects management's best estimate of the future cash flows of the CGUs and the rates used to discount these cash flows, both of which are subject to uncertain factors as follows:

- The future cash flows of the CGUs are sensitive to the cash flows projected for the periods for which detailed forecasts are available and to assumptions regarding the long-term pattern of sustainable cash flows thereafter. Forecasts are compared with actual performance and verifiable economic data, but they reflect management's view of future business prospects at the time of the assessment;
- The rates used to discount future expected cash flows can have a significant effect on their valuation and are based on the costs of capital assigned to individual CGUs. The cost of capital percentage is generally derived from a capital asset pricing model, which incorporates inputs reflecting a number of financial and economic variables, including the risk-free interest rate in the country concerned and a premium for the risk of the business being evaluated. These variables are subject to fluctuations in external market rates and economic conditions beyond management's control. They are therefore subject to uncertainty and require the exercise of significant judgement.

The accuracy of forecast cash flows is subject to a high degree of uncertainty in volatile market conditions. In such circumstances, management retests goodwill for impairment more frequently than once a year when indicators of impairment exist. This ensures that the assumptions on which the cash flow forecasts are based continue to reflect current market conditions and management's best estimate of future business prospects.

Group sponsored structured entities

The group is considered to sponsor another entity if, in addition to ongoing involvement with the entity, it had a key role in establishing that entity or in bringing together relevant counterparties so the transaction that is the purpose of the entity could occur. The group is generally not considered a sponsor if the only involvement with the entity is merely administrative.

Interests in associates and joint arrangements

Joint arrangements are investments in which the group, together with one or more parties, has joint control. Depending on the group's rights and obligations, the joint arrangement is classified as either a joint operation or a joint venture. The group classifies investments in entities over which it has significant influence, and that are neither subsidiaries nor joint arrangements, as associates.

The group recognises its share of the assets, liabilities and results in a joint operation. Investments in associates and interests in joint ventures are recognised using the equity method. The attributable share of the results and reserves of joint ventures and associates are included in the consolidated financial statements of the group based on either financial statements made up to 31 December or pro-rated amounts adjusted for any material transactions or events occurring between the date the financial statements are available and 31 December.

Investments in associates and joint ventures are assessed at each reporting date and tested for impairment when there is an indication that the investment may be impaired. Goodwill on acquisition of interests in joint ventures and associates is not tested separately for impairment, but is assessed as part of the carrying amount of the investment.

(b) Income and expense

Operating income

Interest income and expense

Interest income and expense for all financial instruments, excluding those classified as held for trading or designated at fair value, are recognised in 'Interest income' and 'Interest expense' in the income statement using the effective interest method. However, as an exception to this, interest on debt securities issued by the group that are designated under the fair value option and derivatives managed in conjunction with those debt securities is included in interest expense.

Interest on credit-impaired financial assets is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Non-interest income and expense

The group generates fee income from services provided at a fixed price over time, such as account service and card fees, or when the group delivers a specific transaction at a point in time, such as broking services and import/export services. With the exception of certain fund management and performance fees, all other fees are generated at a fixed price. Fund management and performance fees can be variable depending on the size of the customer portfolio and HSBC's performance as fund manager. Variable fees are recognised when all uncertainties are resolved. Fee income is generally earned from short-term contracts with payment terms that do not include a significant financing component.

The group acts as principal in the majority of contracts with customers, with the exception of broking services. For most brokerage trades, the group acts as agent in the transaction and recognises broking income net of fees payable to other parties in the arrangement.

The group recognises fees earned on transaction-based arrangements at a point in time when we have fully provided the service to the customer. Where the contract requires services to be provided over time, income is recognised on a systematic basis over the life of the agreement.

Where the group offers a package of services that contains multiple non-distinct performance obligations, such as those included in account service packages, the promised services are treated as a single performance obligation. If a package of services contains distinct performance obligations, such as those including both account and insurance services, the corresponding transaction price is allocated to each performance obligation based on the estimated stand-alone selling prices.

Dividend income is recognised when the right to receive payment is established. This is the ex-dividend date for listed equity securities, and usually the date when shareholders approve the dividend for unlisted equity securities.

Net income/(expense) from financial instruments measured at fair value through profit or loss includes the following:

- 'Net income from financial instruments held for trading or managed on a fair value basis': This comprises net trading income, which includes all gains and losses from changes in the fair value of financial assets and financial liabilities held for trading, together with the related interest income, expense and dividends. It also includes all gains and losses from changes in the fair value of derivatives that are managed in conjunction with financial assets and liabilities measured at fair value through profit or loss.
- 'Net income/(expense) from assets and liabilities of insurance businesses, including related derivatives, measured at fair value through profit or loss': This includes interest income, interest expense and dividend income in respect of financial assets and liabilities measured at fair value through profit or loss; and those derivatives managed in conjunction with the above that can be separately identifiable from other trading derivatives.
- 'Changes in fair value of long-term debt and related derivatives': Interest paid on the external long-term debt and interest cash flows on related derivatives is presented in interest expense.
- 'Changes in fair value of other financial instruments mandatorily measured at fair value through profit or loss': This includes interest on instruments that fail the solely payments of principal and interest ('SPPI') test, see (d) below.

The accounting policies for insurance premium income are disclosed in Note 1.2(j).

(c) Valuation of financial instruments

All financial instruments are initially recognised at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of a financial instrument on initial recognition is generally its transaction price (that is, the fair value of the consideration given or received). However, if there is a difference between the transaction price and the fair value of financial instruments whose fair value is based on a quoted price in an active market or a valuation technique that uses only data from observable markets, the group recognises the difference as a trading gain or loss at inception (a 'day 1 gain or loss'). In all other cases, the entire day 1 gain or loss is deferred and recognised in the income statement over the life of the transaction either until the transaction matures or is closed out or the valuation inputs become observable.

The fair value of financial instruments is generally measured on an individual basis. However, in cases where the group manages a group of financial assets and liabilities according to its net market or credit risk exposure, the fair value of the group of financial instruments is measured on a net basis but the underlying financial assets and liabilities are presented separately in the financial statements, unless they satisfy the IFRS offsetting criteria. Financial instruments are classified into one of three fair value hierarchy levels, described in Note 11, 'Fair values of financial instruments carried at fair'.

Critical accounting estimates and judgements

The majority of valuation techniques employ only observable market data. However, certain financial instruments are classified on the basis of valuation techniques that feature one or more significant market inputs that are unobservable, and for them the measurement of fair value is more judgemental. An instrument in its entirety is classified as valued using significant unobservable inputs if, in the opinion of management, greater than 5% of the instrument's valuation is driven by unobservable inputs. 'Unobservable' in this context means that there is little or no current market data available from which to determine the price at which an arm's length transaction would be likely to occur. It generally does not mean that there is no data available at all upon which to base a determination of fair value (consensus pricing data may, for example, be used).

(d) Financial instruments measured at amortised cost

Financial assets that are held to collect the contractual cash flows and which contain contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest are measured at amortised cost. Such financial assets include most loans and advances to banks and customers and some debt securities. In addition, most financial liabilities are measured at amortised cost. The group accounts for regular way amortised cost financial instruments using trade date accounting. The carrying value of these financial assets at initial recognition includes any directly attributable transactions costs. If the initial fair value is lower than the cash amount advanced, such as in the case of some leveraged finance and syndicated lending activities, the difference is deferred and recognised over the life of the loan through the recognition of interest income.

The group may commit to underwriting loans on fixed contractual terms for specified periods of time. When the loan arising from the lending commitment is expected to be held for trading, the commitment to lend is recorded as a derivative. When the group intends to hold the loan, the loan commitment is included in the impairment calculations set out below.

Non-trading reverse repurchase, repurchase and similar agreements

When debt securities are sold subject to a commitment to repurchase them at a predetermined price ('repos'), they remain on the balance sheet and a liability is recorded in respect of the consideration received. Securities purchased under commitments to resell ('reverse repos') are not recognised on the balance sheet and an asset is recorded in respect of the initial consideration paid. Non-trading repos and reverse repos are measured at amortised cost. The difference between the sale and repurchase price or between the purchase and resale price is treated as interest and recognised in net interest income over the life of the agreement.

Contracts that are economically equivalent to reverse repo or repo agreements (such as sales or purchases of debt securities entered into together with total return swaps with the same counterparty) are accounted for similarly to, and presented together with, reverse repo or repo agreements.

(e) Financial assets measured at fair value through other comprehensive income

Financial assets held for a business model that is achieved by both collecting contractual cash flows and selling and which contain contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest are measured at fair value through other comprehensive income ('FVOCI'). These comprise primarily debt securities. They are recognised on the trade date when HSBC enters into contractual arrangements to purchase and are normally derecognised when they are either sold or redeemed. They are subsequently remeasured at fair value and changes therein (except for those relating to impairment, interest income and foreign currency exchange gains and losses) are recognised in other comprehensive income until the assets are sold. Upon disposal, the cumulative gains or losses in other comprehensive income are recognised in the income statement as 'Gains less losses from financial instruments'. Financial assets measured at FVOCI are included in the impairment calculations set out below and impairment is recognised in profit or loss.

(f) Equity securities measured at fair value with fair value movements presented in other comprehensive income

The equity securities for which fair value movements are shown in other comprehensive income are business facilitation and other similar investments where HSBC holds the investments other than to generate a capital return. Gains or losses on the derecognition of these equity securities are not transferred to profit or loss. Otherwise, equity securities are measured at fair value through profit or loss (except for dividend income which is recognised in profit or loss).

(g) Financial instruments designated at fair value through profit or loss

Financial instruments, other than those held for trading, are classified in this category if they meet one or more of the criteria set out below and are so designated irrevocably at inception:

- the use of the designation removes or significantly reduces an accounting mismatch;
- a group of financial assets and liabilities or a group of financial liabilities is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy; and
- the financial liability contains one or more non-closely related embedded derivatives.

Designated financial assets are recognised when HSBC enters into contracts with counterparties, which is generally on trade date, and are normally derecognised when the rights to the cash flows expire or are transferred. Designated financial liabilities are recognised when HSBC enters into contracts with counterparties, which is generally on settlement date, and are normally derecognised when extinguished. Subsequent changes in fair values are recognised in the income statement in 'Net income from financial instruments held for trading or managed on a fair value basis' or 'Net income/(expense) from assets and liabilities of insurance businesses, including related derivatives, measured at fair value through profit or loss'.

Under the above criterion, the main classes of financial instruments designated by HSBC are:

- Long-term debt issues: The interest and/or foreign exchange exposure on certain fixed-rate debt securities issued has been matched with the interest and/or foreign exchange exposure on certain swaps as part of a documented risk management strategy.
- Financial assets and financial liabilities under unit-linked and non-linked investment contracts: A contract under which HSBC does not accept significant insurance risk from another party is not classified as an insurance contract, other than investment contracts with discretionary participation features ('DPF'), but is accounted for as a financial liability. Customer liabilities under linked and certain non-linked investment contracts issued by insurance subsidiaries are determined based on the fair value of the assets held in the linked funds. If no fair value designation was made for the related assets, at least some of the assets would otherwise be measured at either fair value through other comprehensive income or amortised cost. The related financial assets and liabilities are managed and reported to management on a fair value basis. Designation at fair value of the financial assets and related liabilities allows changes in fair values to be recorded in the income statement and presented in the same line.

(h) Derivatives

Derivatives are financial instruments that derive their value from the price of underlying items such as equities, interest rates or other indices. Derivatives are recognised initially and are subsequently measured at fair value through profit or loss, with changes in fair value generally recorded in the income statement. Derivatives are classified as assets when their fair value is positive or as liabilities when their fair value is negative. This includes embedded derivatives in financial liabilities, which are bifurcated from the host contract when they meet the definition of a derivative on a stand-alone basis. Where the derivatives are managed with debt securities issued by HSBC that are designated at fair value, the contractual interest is shown in 'Interest expense' together with the interest payable on the issued debt.

Hedge accounting

When derivatives are not part of fair value designated relationships, if held for risk management purposes they are designated in hedge accounting relationships where the required criteria for documentation and hedge effectiveness are met. The group uses these derivatives or, where allowed, other non-derivative hedging instruments in fair value hedges, cash flow hedges or hedges of net investments in foreign operations as appropriate to the risk being hedged.

Fair value hedge

Fair value hedge accounting does not change the recording of gains and losses on derivatives and other hedging instruments, but results in recognising changes in the fair value of the hedged assets or liabilities attributable to the hedged risk that would not otherwise be recognised in the income statement. If a hedge relationship no longer meets the criteria for hedge accounting, hedge accounting is discontinued; the cumulative adjustment to the carrying amount of the hedged item is amortised to the income statement on a recalculated effective interest rate, unless the hedged item has been derecognised, in which case it is recognised in the income statement immediately.

Cash flow hedge

The effective portion of gains and losses on hedging instruments is recognised in other comprehensive income; the ineffective portion of the change in fair value of derivative hedging instruments that are part of a cash flow hedge relationship is recognised immediately in the income statement within 'Net trading income'. The accumulated gains and losses recognised in other comprehensive income are reclassified to the income statement in the same periods in which the hedged item affects profit or loss. When a hedge relationship is discontinued, or partially discontinued, any cumulative gain or loss recognised in other comprehensive income remains in equity until the forecast transaction is recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss previously recognised in other comprehensive income is immediately reclassified to the income statement.

Net investment hedge

Hedges of net investments in foreign operations are accounted for in a similar way to cash flow hedges. The effective portion of gains and losses on the hedging instrument is recognised in other comprehensive income; other gains and losses are recognised immediately in the income statement. Gains and losses previously recognised in other comprehensive income are reclassified to the income statement on the disposal, or part disposal, of the foreign operation.

Derivatives that do not qualify for hedge accounting

Non-qualifying hedges are derivatives entered into as economic hedges of assets and liabilities for which hedge accounting was not applied.

Critical accounting estimates and judgements

As a result of the request received by the Financial Stability Board from the G20, a fundamental review and reform of the major interest rate benchmarks is underway across the world's largest financial markets. The process of replacing existing benchmark interbank offered rates ('Ibors') with alternative risk free rates ('RFRs') is at different stages, and is progressing at different speeds, across several major jurisdictions. There is therefore uncertainty as to the timing and the methods of transition for many financial products affected by these changes, and whether some existing benchmarks will continue to be supported in some way.

As a result of these developments, significant accounting judgement is involved in determining whether certain hedge accounting relationships that hedge the variability of cash flows and interest rate risk due to changes in Ibors continue to qualify for hedge accounting as at 31 December 2018. Management's judgement is that those existing hedge accounting relationships continue to be supported at the 2018 year-end. Even though there are plans to replace those rates with economically similar rates based on new RFRs over the next few years, there is widespread continued reliance on Ibors in market pricing structures for long term products with maturities over hedging horizons that extend beyond the timescales for replacing Ibors. In addition, there is a current absence of term structures based on the new RFRs. This judgement will be kept under review in the future as markets based on the new RFRs develop, taking into consideration any specific accounting guidance that may be developed to deal with these unusual circumstances. The IASB has commenced the due process for providing clarification on how the guidance for hedge accounting in IAS 39 'Financial Instruments: Recognition and Measurement' and IFRS 9: 'Financial Instruments' should be applied in these circumstances, which were not contemplated when the standards were published.

(i) Impairment of amortised cost and FVOCI financial assets

Expected credit losses are recognised for loans and advances to banks and customers, non-trading reverse repurchase agreements, other financial assets held at amortised cost, debt instruments measured at FVOCI, and certain loan commitments and financial guarantee contracts. At initial recognition, allowance (or provision in the case of some loan commitments and financial guarantees) is required for ECL resulting from default events that are possible within the next 12 months, or less, where the remaining life is less than 12 months, ('12-month ECL'). In the event of a significant increase in credit risk, allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument ('lifetime ECL'). Financial assets where 12-month ECL is recognised are considered to be 'stage 1'; financial assets which are considered to have experienced a significant increase in credit risk are in 'stage 2'; and financial assets for which there is objective evidence of impairment so are considered to be in default or otherwise credit impaired are in 'stage 3'. Purchased or originated credit-impaired financial assets ('POCI') are treated differently as set out below.

Credit impaired (stage 3)

The group determines that a financial instrument is credit impaired and in stage 3 by considering relevant objective evidence, primarily whether:

- contractual payments of either principal or interest are past due for more than 90 days;
- there are other indications that the borrower is unlikely to pay, such as when a concession has been granted to the borrower for economic or legal reasons relating to the borrower's financial condition; and
- the loan is otherwise considered to be in default.

If such unlikeliness to pay is not identified at an earlier stage, it is deemed to occur when an exposure is 90 days past due, even where regulatory rules permit default to be defined based on 180 days past due. Therefore the definitions of credit impaired and default are aligned as far as possible so that stage 3 represents all loans that are considered defaulted or otherwise credit impaired.

Interest income is recognised by applying the effective interest rate to the amortised cost amount, i.e. gross carrying amount less ECL allowance.

Write-off

Financial assets (and the related impairment allowances) are normally written off, either partially or in full, when there is no realistic prospect of recovery. Where loans are secured, this is generally after receipt of any proceeds from the realisation of security. In circumstances where the net realisable value of any collateral has been determined and there is no reasonable expectation of further recovery, write-off may be earlier.

Renegotiation

Loans are identified as renegotiated and classified as credit impaired when we modify the contractual payment terms due to significant credit distress of the borrower. Renegotiated loans remain classified as credit impaired until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows and retain the designation of renegotiated until maturity or derecognition.

A loan that is renegotiated is derecognised if the existing agreement is cancelled and a new agreement is made on substantially different terms or if the terms of an existing agreement are modified such that the renegotiated loan is a substantially different financial instrument. Any new loans that arise following derecognition events in these circumstances are considered to be POCI and will continue to be disclosed as renegotiated loans.

Other than originated credit-impaired loans, all other modified loans could be transferred out of stage 3 if they no longer exhibit any evidence of being credit impaired and, in the case of renegotiated loans, there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, over the minimum observation period, and there are no other indicators of impairment. These loans could be transferred to stage 1 or 2 based on the mechanism as described below by comparing the risk of a default occurring at the reporting date (based on the modified contractual terms) and the risk of a default occurring at initial recognition (based on the original, unmodified contractual terms). Any amount written off as a result of the modification of contractual terms would not be reversed.

Loan modifications that are not credit impaired

Loan modifications that are not identified as renegotiated are considered to be commercial restructuring. Where a commercial restructuring results in a modification (whether legalised through an amendment to the existing terms or the issuance of a new loan contract) such that HSBC's rights to the cash flows under the original contract have expired, the old loan is derecognised and the new loan is recognised at fair value. The rights to cash flows are generally considered to have expired if the commercial restructure is at market rates and no payment-related concession has been provided.

Significant increase in credit risk (stage 2)

An assessment of whether credit risk has increased significantly since initial recognition is performed at each reporting period by considering the change in the risk of default occurring over the remaining life of the financial instrument. The assessment explicitly or implicitly compares the risk of default occurring at the reporting date compared with that at initial recognition, taking into account reasonable and supportable information, including information about past events, current conditions and future economic conditions. The assessment is unbiased, probability-weighted, and to the extent relevant, uses forward-looking information consistent with that used in the measurement of ECL. The analysis of credit risk is multifactor. The determination of whether a specific factor is relevant and its weight compared with other factors depends on the type of product, the characteristics of the financial instrument and the borrower, and the geographical region. Therefore, it is not possible to provide a single set of criteria that will determine what is considered to be a significant increase in credit risk and these criteria will differ for different types of lending, particularly between retail and wholesale. However, unless identified at an earlier stage, all financial assets are deemed to have suffered a significant increase in credit risk when 30 days past due. In addition, wholesale loans that are individually assessed, typically corporate and commercial customers, and included on a watch or worry list, are included in stage 2.

For wholesale portfolios, the quantitative comparison assesses default risk using a lifetime probability of default which encompasses a wide range of information including the obligor's customer risk rating ('CRR'), macroeconomic condition forecasts and credit transition probabilities. For origination CRRs up to 3.3, significant increase in credit risk is measured by comparing the average PD for the remaining term estimated at origination with the equivalent estimation at reporting date. The quantitative measure of significance varies depending on the credit quality at origination as follows:

Origination CRR	Significance trigger - PD to increase by
0.1-1.2	15bps
2.1-3.3	30bps

For CRRs greater than 3.3 that are not impaired, a significant increase in credit risk is considered to have occurred when the origination PD has doubled. The significance of changes in PD was informed by expert credit risk judgement, referenced to historical credit migrations and to relative changes in external market rates.

For loans originated prior to the implementation of IFRS 9, the origination PD does not include adjustments to reflect expectations of future macroeconomic conditions since these are not available without the use of hindsight. In the absence of this data, origination PD must be approximated assuming through-the-cycle ('TTC') PDs and TTC migration probabilities, consistent with the instrument's underlying modelling approach and the CRR at origination. For these loans, the quantitative comparison is supplemented with additional CRR deterioration-based thresholds, as set out in the table below:

Origination CRR	Additional significance criteria – Number of CRR grade notches deterioration required to identify as significant credit deterioration (stage 2) (> or equal to)
0.1	5 notches
1.1–4.2	4 notches
4.3–5.1	3 notches
5.2–7.1	2 notches
7.2–8.2	1 notch
8.3	0 notch

Further information about the 23-grade scale used for CRR can be found on page 27.

For certain portfolios of debt securities where external market ratings are available and credit ratings are not used in credit risk management, the debt securities will be in stage 2 if their credit risk increases to the extent they are no longer considered investment grade. Investment grade is where the financial instrument has a low risk of incurring losses, the structure has a strong capacity to meet its contractual cash flow obligations in the near term and adverse changes in economic and business conditions in the longer term may, but will not necessarily, reduce the ability of the borrower to fulfil their contractual cash flow obligations.

For retail portfolios, default risk is assessed using a reporting date 12-month PD derived from credit scores, which incorporates all available information about the customer. This PD is adjusted for the effect of macroeconomic forecasts for periods longer than 12 months and is considered to be a reasonable approximation of a lifetime PD measure. Retail exposures are first segmented into homogeneous portfolios, generally by country, product and brand. Within each portfolio, the stage 2 accounts are defined as accounts with an adjusted 12-month PD greater than the average 12-month PD of loans in that portfolio 12 months before they become 30 days past due. The expert credit risk judgement is that no prior increase in credit risk is significant. This portfolio-specific threshold identifies loans with a PD higher than would be expected from loans that are performing as originally expected, and higher than what would have been acceptable at origination. It therefore approximates a comparison of origination to reporting date PDs.

Unimpaired and without significant increase in credit risk – (stage 1)

ECL resulting from default events that are possible within the next 12 months ('12-month ECL') are recognised for financial instruments that remain in stage 1.

Purchased or originated credit impaired

Financial assets that are purchased or originated at a deep discount that reflects the incurred credit losses are considered to be POCI. This population includes the recognition of a new financial instrument following a renegotiation where concessions have been granted for economic or contractual reasons relating to the borrower's financial difficulty that otherwise would not have been considered. The amount of change-in-lifetime ECL is recognised in profit or loss until the POCI is derecognised, even if the lifetime ECL are less than the amount of ECL included in the estimated cash flows on initial recognition.

Movement between stages

Financial assets can be transferred between the different categories (other than POCI) depending on their relative increase in credit risk since initial recognition. Financial instruments are transferred out of stage 2 if their credit risk is no longer considered to be significantly increased since initial recognition based on the assessments described above. Except for renegotiated loans, financial instruments are transferred out of stage 3 when they no longer exhibit any evidence of credit impairment as described above. Renegotiated loans that are not POCI will continue to be in stage 3 until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, observed over a minimum one-year period and there are no other indicators of impairment. For loans that are assessed for impairment on a portfolio basis, the evidence typically comprises a history of payment performance against the original or revised terms, as appropriate to the circumstances. For loans that are assessed for impairment on an individual basis, all available evidence is assessed on a case-by-case basis.

Measurement of ECL

The assessment of credit risk and the estimation of ECL are unbiased and probability-weighted, and incorporate all available information that is relevant to the assessment including information about past events, current conditions and reasonable and supportable forecasts of future events and economic conditions at the reporting date. In addition, the estimation of ECL should take into account the time value of money.

In general, HSBC calculates ECL using three main components, a probability of default, a loss given default ('LGD') and the exposure at default ('EAD').

The 12-month ECL is calculated by multiplying the 12-month PD, LGD and EAD. Lifetime ECL is calculated using the lifetime PD instead. The 12-month and lifetime PDs represent the probability of default occurring over the next 12 months and the remaining maturity of the instrument respectively.

The EAD represents the expected balance at default, taking into account the repayment of principal and interest from the balance sheet date to the default event together with any expected drawdowns of committed facilities. The LGD represents expected losses on the EAD given the event of default, taking into account, among other attributes, the mitigating effect of collateral value at the time it is expected to be realised and the time value of money.

HSBC leverages the Basel II IRB framework where possible, with recalibration to meet the differing IFRS 9 requirements as set out in the following table:

Model	Regulatory capital	IFRS 9
PD	• Through the cycle (represents long-run average PD throughout a full economic cycle) • The definition of default includes a backstop of 90+ days past due, although this has been modified to 180+ days past due for some portfolios, particularly UK and US mortgages	• Point in time (based on current conditions, adjusted to take into account estimates of future conditions that will impact PD) • Default backstop of 90+ days past due for all portfolios
EAD	• Cannot be lower than current balance	• Amortisation captured for term products
LGD	• Downturn LGD (consistent losses expected to be suffered during a severe but plausible economic downturn) • Regulatory floors may apply to mitigate risk of underestimating downturn LGD due to lack of historical data • Discounted using cost of capital • All collection costs included	• Expected LGD (based on estimate of loss given default including the expected impact of future economic conditions such as changes in value of collateral) • No floors • Discounted using the original effective interest rate of the loan • Only costs associated with obtaining/selling collateral included
Other		• Discounted back from point of default to balance sheet date

While 12-month PDs are recalibrated from Basel II models where possible, the lifetime PDs are determined by projecting the 12-month PD using a term structure. For the wholesale methodology, the lifetime PD also takes into account credit migration, i.e. a customer migrating through the CRR bands over its life.

The ECL for wholesale stage 3 is determined on an individual basis using a discounted cash flow ('DCF') methodology. The expected future cash flows are based on the credit risk officer's estimates as at the reporting date, reflecting reasonable and supportable

assumptions and projections of future recoveries and expected future receipts of interest. Collateral is taken into account if it is likely that the recovery of the outstanding amount will include realisation of collateral based on its estimated fair value of collateral at the time of expected realisation, less costs for obtaining and selling the collateral. The cash flows are discounted at a reasonable approximation of the original effective interest rate. For significant cases, cash flows under four different scenarios are probability-weighted by reference to the three economic scenarios applied more generally by HSBC Group and the judgement of the credit risk officer in relation to the likelihood of the workout strategy succeeding or receivership being required. For less significant cases, the effect of different economic scenarios and work-out strategies is approximated and applied as an adjustment to the most likely outcome.

Period over which ECL is measured

Expected credit loss is measured from the initial recognition of the financial asset. The maximum period considered when measuring ECL (be it 12-month or lifetime ECL) is the maximum contractual period over which HSBC is exposed to credit risk. For wholesale overdrafts, credit risk management actions are taken no less frequently than on an annual basis and therefore this period is to the expected date of the next substantive credit review. The date of the substantive credit review also represents the initial recognition of the new facility. However, where the financial instrument includes both a drawn and undrawn commitment and the contractual ability to demand repayment and cancel the undrawn commitment does not serve to limit HSBC's exposure to credit risk to the contractual notice period, the contractual period does not determine the maximum period considered. Instead, ECL is measured over the period HSBC remains exposed to credit risk that is not mitigated by credit risk management actions. This applies to retail overdrafts and credit cards, where the period is the average time taken for stage 2 exposures to default or close as performing accounts, determined on a portfolio basis and ranging from between two and six years. In addition, for these facilities it is not possible to identify the ECL on the loan commitment component separately from the financial asset component. As a result, the total ECL is recognised in the loss allowance for the financial asset unless the total ECL exceeds the gross carrying amount of the financial asset, in which case the ECL is recognised as a provision.

Forward-looking economic inputs

HSBC will in general apply three forward-looking global economic scenarios determined with reference to external forecast distributions representative of our view of forecast economic conditions, the consensus economic scenario approach. This approach is considered sufficient to calculate unbiased expected loss in most economic environments. They represent a most likely outcome (the Central scenario) and two, less likely, 'outer' scenarios on either side of the Central, referred to as the Upside and Downside scenarios. The Central scenario is the basis for the annual operating planning process and, with regulatory modifications, will also be used in enterprise-wide stress tests. The Upside and Downside scenarios are constructed following a standard process supported by a scenario narrative reflecting HSBC Group's current top and emerging risks and by consulting external and internal subject matter experts. The relationship between the outer scenarios and Central scenario will generally be fixed with the Central scenario being assigned a weighting of 80% and the Upside and Downside scenarios 10% each, with the difference between the Central and outer scenarios in terms of economic severity being informed by the spread of external forecast distributions among professional industry forecasts. The outer scenarios are economically plausible, internally consistent states of the world and will not necessarily be as severe as scenarios used in stress testing. The period of forecasts is 5 years for the central scenario. Upside and Downside scenarios use distributional forecasts for the first two years after which they converge to the central forecasts. The central forecast and spread between the Central and outer scenarios is grounded on the expected Gross Domestic Product of the UK and France. This includes consideration of these country's economic factors as well as global economic events, the economic performance of other countries and the impact these can have on the Gross Domestic Product in the UK and France. HSBC runs a global process which ensures that both domestic and international economic factors are considered in creating scenarios for Europe.

In general, the consequences of the assessment of credit risk and the resulting ECL outputs will be probability-weighted using the standard probability weights. This probability weighting may be applied directly or the effect of the probability weighting determined on a periodic basis, at least annually, and then applied as an adjustment to the outcomes resulting from the central economic forecast. The central economic forecast is updated quarterly.

HSBC recognises that the consensus economic scenario approach using three scenarios will be insufficient in certain economic environments. Additional analysis may be requested at management's discretion, including the production of extra scenarios. If conditions warrant, this could result in alternative scenarios and probability weightings being applied in arriving at the ECL.

Critical accounting estimates and judgements

In determining ECL, management is required to exercise judgement in defining what is considered to be a significant increase in credit risk and in making assumptions and estimates to incorporate relevant information about past events, current conditions and forecasts of economic conditions. Judgement has been applied in determining the lifetime and point of initial recognition of revolving facilities.

The PD, LGD and EAD models which support these determinations are reviewed regularly in light of differences between loss estimates and actual loss experience, but given that IFRS 9 requirements have only just been applied, there has been little time available to make these comparisons. Therefore, the underlying models and their calibration, including how they react to forward-looking economic conditions, remain subject to review and refinement. This is particularly relevant for lifetime PDs, which have not been previously used in regulatory modelling and for the incorporation of 'Upside scenarios' which have not generally been subject to experience gained through stress testing.

The exercise of judgement in making estimations requires the use of assumptions which are highly subjective and very sensitive to the risk factors, in particular to changes in economic and credit conditions. Many of the factors have a high degree of interdependency and there is no single factor to which loan impairment allowances as a whole are sensitive. The sections marked as audited on pages 42 to 44 'Measurement uncertainty and sensitivity analysis of ECL estimates' set out the assumptions underlying the Central scenario and information about how scenarios are developed in relation to HSBC Group's top and emerging risks and its judgements, informed by consensus forecasts of professional industry forecasters. The sensitivity of ECL to different economic scenarios is illustrated by recalculating the ECL for selected portfolios as if 100% weighting had been assigned to each scenario.

(j) Insurance contracts

A contract is classified as an insurance contract where the group accepts significant insurance risk from another party by agreeing to compensate that party on the occurrence of a specified uncertain future event. An insurance contract may also transfer financial risk, but is accounted for as an insurance contract if the insurance risk is significant. In addition, the group issues investment contracts with discretionary participation features ('DPF') which are also accounted for as insurance contracts as required by IFRS 4 'Insurance Contracts'.

Net insurance premium income

Premiums for life insurance contracts are accounted for when receivable, except in unit-linked insurance contracts where premiums are accounted for when liabilities are established.

Reinsurance premiums are accounted for in the same accounting period as the premiums for the direct insurance contracts to which they relate.

Net insurance claims and benefits paid and movements in liabilities to policyholders

Gross insurance claims for life insurance contracts reflect the total cost of claims arising during the year, including claim handling costs and any policyholder bonuses allocated in anticipation of a bonus declaration.

Maturity claims are recognised when due for payment. Surrenders are recognised when paid or at an earlier date on which, following notification, the policy ceases to be included within the calculation of the related insurance liabilities. Death claims are recognised when notified.

Reinsurance recoveries are accounted for in the same period as the related claim.

Liabilities under insurance contracts

Liabilities under non-linked life insurance contracts are calculated by each life insurance operation based on local actuarial principles. Liabilities under unit-linked life insurance contracts are at least equivalent to the surrender or transfer value, which is calculated by reference to the value of the relevant underlying funds or indices.

Future profit participation on insurance contracts with DPF

Where contracts provide discretionary profit participation benefits to policyholders, liabilities for these contracts include provisions for the future discretionary benefits to policyholders. These provisions reflect the actual performance of the investment portfolio to date and management's expectation of the future performance of the assets backing the contracts, as well as other experience factors such as mortality, lapses and operational efficiency, where appropriate. The benefits to policyholders may be determined by the contractual terms, regulation or past distribution policy.

Investment contracts with DPF

While investment contracts with DPF are financial instruments, they continue to be treated as insurance contracts as required by IFRS 4. The group therefore recognises the premiums for these contracts as revenue and recognises as an expense the resulting increase in the carrying amount of the liability.

In the case of net unrealised investment gains on these contracts, whose discretionary benefits principally reflect the actual performance of the investment portfolio, the corresponding increase in the liabilities is recognised in either the income statement or other comprehensive income, following the treatment of the unrealised gains on the relevant assets. In the case of net unrealised losses, a deferred participating asset is recognised only to the extent that its recoverability is highly probable. Movements in the liabilities arising from realised gains and losses on relevant assets are recognised in the income statement.

Present value of in-force long-term insurance business

The group recognises the value placed on insurance contracts, and investment contracts with DPF, that are classified as long-term and in-force at the balance sheet date, as an asset. The asset represents the present value of the equity holders' interest in the issuing insurance companies' profits expected to emerge from these contracts written at the balance sheet date. The present value of in-force long-term insurance business ('PVIF') is determined by discounting those expected future profits using appropriate assumptions in assessing factors such as future mortality, lapse rates and levels of expenses, and a risk discount rate that reflects the risk premium attributable to the respective contracts. The PVIF incorporates allowances for both non-market risk and the value of financial options and guarantees. The PVIF asset is presented gross of attributable tax in the balance sheet and movements in the PVIF asset are included in 'Other operating income' on a gross of tax basis.

(k) Employee compensation and benefits

Share-based payments

The group enters into both equity-settled and cash-settled share-based payment arrangements with its employees as compensation for the provision of their services. The vesting period for these schemes may commence before the legal grant date if the employees have started to render services in respect of the award before the legal grant date, where there is a shared understanding of the terms and conditions of the arrangement. Expenses are recognised when the employee starts to render service to which the award relates.

Cancellations result from the failure to meet a non-vesting condition during the vesting period, and are treated as an acceleration of vesting recognised immediately in the income statement. Failure to meet a vesting condition by the employee is not treated as a cancellation, and the amount of expense recognised for the award is adjusted to reflect the number of awards expected to vest.

Post-employment benefit plans

The group operates a number of pension schemes including defined benefit, defined contribution and post-employment benefit schemes.

Payments to defined contribution schemes are charged as an expense as the employees render service.

Defined benefit pension obligations are calculated using the projected unit credit method. The net charge to the income statement mainly comprises the service cost and the net interest on the net defined benefit asset or liability, and is presented in operating expenses.

Remeasurements of the net defined benefit asset or liability, which comprise actuarial gains and losses, return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest), are recognised immediately in other comprehensive income. The net defined benefit asset or liability represents the present value of defined benefit obligations reduced by the fair value of plan assets, after applying the asset ceiling test, where the net defined benefit surplus is limited to the present value of available refunds and reductions in future contributions to the plan.

The cost of obligations arising from other post-employment plans are accounted for on the same basis as defined benefit pension plans.

(l) Tax

Income tax comprises current tax and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised in other comprehensive income or directly in equity, in which case the tax is recognised in the same statement in which the related item appears.

Current tax is the tax expected to be payable on the taxable profit for the year and on any adjustment to tax payable in respect of previous years. The group provides for potential current tax liabilities that may arise on the basis of the amounts expected to be paid to

the tax authorities. Payments associated with any incremental base erosion and anti-abuse tax are reflected in tax expense in the period incurred.

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the balance sheet, and the amounts attributed to such assets and liabilities for tax purposes. Deferred tax is calculated using the tax rates expected to apply in the periods as the assets will be realised or the liabilities settled.

Current and deferred tax are calculated based on tax rates and laws enacted, or substantively enacted, by the balance sheet date.

(m) Provisions, contingent liabilities and guarantees

Provisions

Provisions are recognised when it is probable that an outflow of economic benefits will be required to settle a present legal or constructive obligation that has arisen as a result of past events and for which a reliable estimate can be made.

Critical accounting estimates and judgements

Judgement is involved in determining whether a present obligation exists and in estimating the probability, timing and amount of any outflows. Professional expert advice is taken on the assessment of litigation, property (including onerous contracts) and similar obligations. Provisions for legal proceedings and regulatory matters typically require a higher degree of judgement than other types of provisions. When matters are at an early stage, accounting judgements can be difficult because of the high degree of uncertainty associated with determining whether a present obligation exists, and estimating the probability and amount of any outflows that may arise. As matters progress, management and legal advisers evaluate on an ongoing basis whether provisions should be recognised, revising previous judgements and estimates as appropriate. At more advanced stages, it is typically easier to make judgements and estimates around a better defined set of possible outcomes. However, the amount provisioned can remain very sensitive to the assumptions used. There could be a wide range of possible outcomes for any pending legal proceedings, investigations or inquiries. As a result, it is often not practicable to quantify a range of possible outcomes for individual matters. It is also not practicable to meaningfully quantify ranges of potential outcomes in aggregate for these types of provisions because of the diverse nature and circumstances of such matters and the wide range of uncertainties involved. Provisions for customer remediation also require significant levels of estimation and judgement. The amounts of provisions recognised depend on a number of different assumptions, such as, the volume of inbound complaints, the projected period of inbound complaint volumes, the decay rate of complaint volumes, the population identified as systemically mis-sold and the number of policies per customer complaint.

Contingent liabilities, contractual commitments and guarantees

Contingent liabilities

Contingent liabilities, which include certain guarantees and letters of credit pledged as collateral security, and contingent liabilities related to legal proceedings or regulatory matters, are not recognised in the financial statements but are disclosed unless the probability of settlement is remote.

Financial guarantee contracts

Liabilities under financial guarantee contracts that are not classified as insurance contracts are recorded initially at their fair value, which is generally the fee received or present value of the fee receivable.

The bank has issued financial guarantees and similar contracts to other group entities. The group elects to account for certain guarantees as insurance contracts in the bank's financial statements, in which case they are measured and recognised as insurance liabilities. This election is made on a contract by contract basis, and is irrevocable.

(n) Accounting policies applied to financial instruments prior to 1 January 2018

Financial instruments measured at amortised cost

Loans and advances to banks and customers, held-to-maturity investments and most financial liabilities are measured at amortised cost. The carrying value of these financial assets at initial recognition includes any directly attributable transactions costs. If the initial fair value is lower than the cash amount advanced, such as in the case of some leveraged finance and syndicated lending activities, the difference is deferred and recognised over the life of the loan (as described in sub-section (c) above) through the recognition of interest income, unless the loan becomes impaired. HSBC may commit to underwriting loans on fixed contractual terms for specified periods of time. When the loan arising from the lending commitment is expected to be held for trading, the commitment to lend is recorded as a derivative. When HSBC intends to hold the loan, a provision on the loan commitment is only recorded where it is probable that HSBC will incur a loss.

Impairment of loans and advances

Losses for impaired loans are recognised when there is objective evidence that impairment of a loan or portfolio of loans has occurred. Losses which may arise from future events are not recognised.

Individually assessed loans and advances

The factors considered in determining whether a loan is individually significant for the purposes of assessing impairment include the size of the loan, the number of loans in the portfolio, the importance of the individual loan relationship and how this is managed. Loans that are determined to be individually significant will be individually assessed for impairment, except when volumes of defaults and losses are sufficient to justify treatment under a collective methodology.

Loans considered as individually significant are typically to corporate and commercial customers, are for larger amounts and are managed on an individual basis. For these loans, HSBC considers on a case-by-case basis at each balance sheet date whether there is any objective evidence that a loan is impaired.

The determination of the realisable value of security is based on the most recently updated market value at the time the impairment assessment is performed. The value is not adjusted for expected future changes in market prices, though adjustments are made to reflect local conditions such as forced sale discounts.

Impairment losses are calculated by discounting the expected future cash flows of a loan, which include expected future receipts of contractual interest, at the loan's original effective interest rate or an approximation thereof, and comparing the resultant present value with the loan's current carrying amount.

Collectively assessed loans and advances

Impairment is assessed collectively to cover losses which have been incurred but have not yet been identified on loans subject to individual assessment or for homogeneous groups of loans that are not considered individually significant, which are generally retail lending portfolios.

Incurred but not yet identified impairment

Individually assessed loans for which no evidence of impairment has been specifically identified on an individual basis are grouped together according to their credit risk characteristics for a collective impairment assessment. This assessment captures impairment losses that HSBC has incurred as a result of events occurring before the balance sheet date that HSBC is not able to identify on an individual loan basis, and that can be reliably estimated. When information becomes available that identifies losses on individual loans within a group, those loans are removed from the group and assessed individually.

Homogeneous groups of loans and advances

Statistical methods are used to determine collective impairment losses for homogeneous groups of loans not considered individually significant. The methods used to calculate collective allowances are set out below:

- When appropriate empirical information is available, HSBC utilises roll-rate methodology, which employs statistical analyses of historical data and experience of delinquency and default to reliably estimate the amount of the loans that will eventually be written off as a result of events occurring before the balance sheet date. Individual loans are grouped using ranges of past due days, and statistical estimates are made of the likelihood that loans in each range will progress through the various stages of delinquency and become irrecoverable. Additionally, individual loans are segmented based on their credit characteristics, such as industry sector, loan grade or product. In applying this methodology, adjustments are made to estimate the periods of time between a loss event occurring, for example because of a missed payment, and its confirmation through write-off (known as the loss identification period). Current economic conditions are also evaluated when calculating the appropriate level of allowance required to cover inherent loss. In certain highly developed markets, models also take into account behavioural and account management trends as revealed in, for example bankruptcy and rescheduling statistics.
- When the portfolio size is small or when information is insufficient or not reliable enough to adopt a roll-rate methodology, HSBC adopts a basic formulaic approach based on historical loss rate experience, or a discounted cash flow model. Where a basic formulaic approach is undertaken, the period between a loss event occurring and its identification is estimated by local management, and is typically between six and 12 months.

Write-off of loans and advances

Loans and the related impairment allowance accounts are normally written off, either partially or in full, when there is no realistic prospect of recovery. Where loans are secured, this is generally after receipt of any proceeds from the realisation of security. In circumstances where the net realisable value of any collateral has been determined and there is no reasonable expectation of further recovery, write-off may be earlier.

Reversals of impairment

If the amount of an impairment loss decreases in a subsequent period, and the decrease can be related objectively to an event occurring after the impairment was recognised, the excess is written back by reducing the loan impairment allowance account accordingly. The write-back is recognised in the income statement.

Assets acquired in exchange for loans

When non-financial assets acquired in exchange for loans as part of an orderly realisation are held for sale, these assets are recorded as 'Assets held for sale'.

Renegotiated loans

Loans subject to collective impairment assessment whose terms have been renegotiated are no longer considered past due, but are treated as up-to-date loans for measurement purposes once a minimum number of required payments has been received. Where collectively assessed loan portfolios include significant levels of renegotiated loans, these loans are segregated from other parts of the loan portfolio for the purposes of collective impairment assessment to reflect their risk profile. Loans subject to individual impairment assessment, whose terms have been renegotiated, are subject to ongoing review to determine whether they remain impaired. The carrying amounts of loans that have been classified as renegotiated retain this classification until maturity or derecognition.

A loan that is renegotiated is derecognised if the existing agreement is cancelled and a new agreement made on substantially different terms or if the terms of an existing agreement are modified such that the renegotiated loan is substantially a different financial instrument. Any new loans that arise following derecognition events will continue to be disclosed as renegotiated loans and are assessed for impairment as above.

Non-trading reverse repurchase, repurchase and similar agreements

When debt securities are sold subject to a commitment to repurchase them at a predetermined price ('repos'), they remain on the balance sheet and a liability is recorded in respect of the consideration received. Securities purchased under commitments to resell ('reverse repos') are not recognised on the balance sheet and an asset is recorded in respect of the initial consideration paid. Non-trading repos and reverse repos are measured at amortised cost. The difference between the sale and repurchase price or between the purchase and resale price is treated as interest and recognised in net interest income over the life of the agreement.

Contracts that are economically equivalent to reverse repurchase or repurchase agreements (such as sales or purchases of debt securities entered into together with total return swaps with the same counterparty) are accounted for similarly to, and presented together with, reverse repurchase or repurchase agreements.

Financial instruments measured at fair value

Available-for-sale financial assets

Available-for-sale financial assets are recognised on the trade date when HSBC enters into contractual arrangements to purchase them, and are normally derecognised when they are either sold or redeemed. They are subsequently remeasured at fair value, and changes therein are recognised in other comprehensive income until the assets are either sold or become impaired. Upon disposal, the cumulative gains or losses in other comprehensive income are recognised in the income statement as 'Gains less losses from financial investments'.

Impairment of available-for-sale financial assets

Available-for-sale financial assets are assessed at each balance sheet date for objective evidence of impairment. Impairment losses are recognised in the income statement within 'Loan impairment charges and other credit risk provisions' for debt instruments and within 'Gains less losses from financial investments' for equities.

Available-for-sale debt securities

In assessing objective evidence of impairment at the reporting date, HSBC considers all available evidence, including observable data or information about events specifically relating to the securities which may result in a shortfall in the recovery of future cash flows. A subsequent decline in the fair value of the instrument is recognised in the income statement when there is objective evidence of impairment as a result of decreases in the estimated future cash flows. Where there is no further objective evidence of impairment, the decline in the fair value of the financial asset is recognised in other comprehensive income. If the fair value of a debt security increases in a subsequent period, and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, or the instrument is no longer impaired, the impairment loss is reversed through the income statement.

Available-for-sale equity securities

A significant or prolonged decline in the fair value of the equity below its cost is objective evidence of impairment. In assessing whether it is significant, the decline in fair value is evaluated against the original cost of the asset at initial recognition. In assessing whether it is prolonged, the decline is evaluated against the continuous period in which the fair value of the asset has been below its original cost at initial recognition.

All subsequent increases in the fair value of the instrument are treated as a revaluation and are recognised in other comprehensive income. Subsequent decreases in the fair value of the available-for-sale equity security are recognised in the income statement to the extent that further cumulative impairment losses have been incurred. Impairment losses recognised on the equity security are not reversed through the income statement.

Financial instruments designated at fair value

Financial instruments, other than those held for trading, are classified in this category if they meet one or more of the criteria set out below, and are so designated irrevocably at inception:

- the use of the designation removes or significantly reduces an accounting mismatch;
- when a group of financial assets, liabilities or both is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy; and
- where financial instruments contain one or more non-closely related embedded derivatives.

Designated financial assets are recognised when HSBC enters into contracts with counterparties, which is generally on trade date, and are normally derecognised when the rights to the cash flows expire or are transferred. Designated financial liabilities are recognised when HSBC enters into contracts with counterparties, which is generally on settlement date, and are normally derecognised when extinguished. Subsequent changes in fair values are recognised in the income statement in 'Net income/(expense) from financial instruments designated at fair value'. Under this criterion, the main classes of financial instruments designated by HSBC are:

Long-term debt issues

The interest and/or foreign exchange exposure on certain fixed rate debt securities issued has been matched with the interest and/or foreign exchange exposure on certain swaps as part of a documented risk management strategy.

Financial assets and financial liabilities under unit-linked and non-linked investment contracts.

A contract under which HSBC does not accept significant insurance risk from another party is not classified as an insurance contract, other than investment contracts with discretionary participation features ('DPF'), but is accounted for as a financial liability. See Note 1.2(j) for investment contracts with DPF and contracts where HSBC accepts significant insurance risk. Customer liabilities under linked and certain non-linked investment contracts issued by insurance subsidiaries and the corresponding financial assets are designated at fair value. Liabilities are at least equivalent to the surrender or transfer value which is calculated by reference to the value of the relevant underlying funds or indices. Premiums receivable and amounts withdrawn are accounted for as increases or decreases in the liability recorded in respect of investment contracts. The incremental costs directly related to the acquisition of new investment contracts or renewing existing investment contracts are deferred and amortised over the period during which the investment management services are provided.

2 Net fee income

Net fee income by global business

	2018						2017
	Retail Banking and Wealth Management	**Commercial Banking**	**Global Banking and Markets**	**Global Private Banking**	**Corporate Centre**	**Total**	Total
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	£m
Account services	**203**	**214**	**179**	**13**	**—**	**609**	902
Funds under management	**228**	**26**	**150**	**47**	**—**	**451**	508
Cards	**105**	**39**	**6**	**—**	**—**	**150**	354
Credit facilities	**1**	**157**	**229**	**6**	**—**	**393**	494
Broking income	**16**	**23**	**215**	**28**	**—**	**282**	310
Unit trusts	**9**	**—**	**—**	**2**	**—**	**11**	15
Imports/exports	**—**	**44**	**36**	**—**	**—**	**80**	122
Remittances	**13**	**23**	**50**	**2**	**—**	**88**	177
Underwriting	**—**	**3**	**238**	**3**	**—**	**244**	276
Global custody	**6**	**8**	**106**	**9**	**—**	**129**	122
Insurance agency commission	**40**	**2**	**—**	**9**	**—**	**51**	98
Other	**316**	**230**	**894**	**30**	**(556)**	**914**	967
Fee income	**937**	**769**	**2,103**	**149**	**(556)**	**3,402**	4,345
Less: fee expense	**(339)**	**(56)**	**(1,464)**	**(40)**	**541**	**(1,358)**	(1,356)
Net fee income	**598**	**713**	**639**	**109**	**(15)**	**2,044**	2,989

Net fee income includes £1,875m of fees earned on financial assets that are not at fair value through profit or loss (other than amounts included in determining the effective interest rate) (2017: £2,780m), £365m of fees payable on financial liabilities that are not at fair value through profit of loss (other than amounts included in determining the effective interest rate) (2017: £471m), £613m of fees earned on trust and other fiduciary activities (2017: £677m), and £2m of fees payable relating to trust and other fiduciary activities (2017: £1m). Comparatives for fees earned on trust and other fiduciary activities have been restated to align with current year treatment.

3 Net income/(expense) from financial instruments measured at fair value through profit or loss

	2018	2017
	£m	£m
Net income/(expense) arising on:		
Trading activities	**391**	2,803
Other trading income – hedge ineffectiveness	**(18)**	3
– on cash flow hedges	**(6)**	(8)
– on fair value hedges	**(12)**	11
Fair value movement on non-qualifying hedges	**(13)**	(16)
Other instruments designated and mandatorily measured at fair value and related derivatives	**2,373**	N/A
Net income from financial instruments held for trading or managed on a fair value basis[1]	**2,733**	2,790
Financial assets held to meet liabilities under insurance and investment contracts	**(626)**	639
Liabilities to customers under investment contracts	**22**	(37)
Net income from assets and liabilities of insurance businesses, including related derivatives, measured at fair value through profit or loss	**(604)**	602
Derivatives managed in conjunction with the group's issued debt securities	**(157)**	(176)
Other changes in fair value	**162**	289
Changes in fair value of long-term debt and related derivatives[1]	**5**	113
Changes in fair value of other financial instruments mandatorily measured at fair value through profit or loss	**511**	N/A
Year ended 31 Dec	**2,645**	3,505

1 *The effect of foreign exchange exposure on certain long-term debt instruments has been included in 'Net income from financial instruments held for trading or managed on a fair value basis' from 1 January 2018. Comparative information has been re-presented. The restatement decreased 'Changes in fair value of long-term debt and related derivatives' by £402m with an equivalent increase in 'Net income from financial instruments held for trading or managed on a fair value basis'. For further details, refer to 'Changes to accounting from 1 January 2018' on page 10.*

4 Insurance business

Net insurance premium income

	Non-linked insurance	Linked life insurance	Investment contracts with DPF[1]	Total
	£m	£m	£m	£m
Gross insurance premium income	**202**	**166**	**1,734**	**2,102**
Reinsurers' share of gross insurance premium income	**(94)**	**(3)**	**–**	**(97)**
Year ended 31 Dec 2018	**108**	**163**	**1,734**	**2,005**
Gross insurance premium income	219	106	1,575	1,900
Reinsurers' share of gross insurance premium income	(88)	(3)	–	(91)
Year ended 31 Dec 2017	131	103	1,575	1,809

1 *Discretionary participation features.*

Net insurance claims and benefits paid and movement in liabilities to policyholders

	Non-linked insurance	Linked life insurance	Investment contracts with DPF[1]	Total
	£m	£m	£m	£m
Gross claims and benefits paid and movement in liabilities	**167**	**(40)**	**1,284**	**1,411**
– claims, benefits and surrenders paid	**169**	**90**	**1,407**	**1,666**
– movement in liabilities	**(2)**	**(130)**	**(123)**	**(255)**
Reinsurers' share of claims and benefits paid and movement in liabilities	**(69)**	**136**	**–**	**67**
– claims, benefits and surrenders paid	**(64)**	**(2)**	**–**	**(66)**
– movement in liabilities	**(5)**	**138**	**–**	**133**
Year ended 31 Dec 2018	**98**	**96**	**1,284**	**1,478**
Gross claims and benefits paid and movement in liabilities	132	217	2,257	2,606
– claims, benefits and surrenders paid	145	90	1,556	1,791
– movement in liabilities	(13)	127	701	815
Reinsurers' share of claims and benefits paid and movement in liabilities	(49)	(67)	–	(116)
– claims, benefits and surrenders paid	(61)	(3)	–	(64)
– movement in liabilities	12	(64)	–	(52)
Year ended 31 Dec 2017	83	150	2,257	2,490

1 *Discretionary participation features.*

Liabilities under insurance contracts

	Non-linked insurance	Linked life insurance	Investment contracts with DPF[1]	Total
	£m	£m	£m	£m
Gross liabilities under insurance contracts at 1 Jan 2018	**617**	**1,166**	**19,250**	**21,033**
Claims and benefits paid	**(169)**	**(90)**	**(1,407)**	**(1,666)**
Increase in liabilities to policyholders	**167**	**(40)**	**1,284**	**1,411**
Exchange differences and other movements[2]	**2**	**5**	**(128)**	**(121)**
Gross liabilities under insurance contracts at 31 Dec 2018	**617**	**1,041**	**18,999**	**20,657**
Reinsurers' share of liabilities under insurance contracts	**(129)**	**(50)**	**–**	**(179)**
Net liabilities under insurance contracts at 31 Dec 2018	**488**	**991**	**18,999**	**20,478**
Gross liabilities under insurance contracts at 1 Jan 2017	616	1,030	18,078	19,724
Claims and benefits paid	(145)	(90)	(1,556)	(1,791)
Increase in liabilities to policyholders	132	217	2,257	2,606
Exchange differences and other movements	14	9	471	494
Gross liabilities under insurance contracts at 31 Dec 2017	617	1,166	19,250	21,033
Reinsurers' share of liabilities under insurance contracts	(148)	(188)	–	(336)
Net liabilities under insurance contracts at 31 Dec 2017	469	978	19,250	20,697

1 *Discretionary participation features.*
2 *'Exchange differences and other movements' includes movements in liabilities arising from net unrealised investment gains recognised in other comprehensive income.*

The key factors contributing to the movement in liabilities to policyholders included movement in the market value of assets supporting policyholder liabilities, death claims, surrenders, lapses, liabilities to policyholders created at the initial inception of the policies, the declaration of bonuses and other amounts attributable to policyholders.

5 Operating profit

Operating profit is stated after the following items:

	2018	2017
	£m	£m
Income		
Interest recognised on impaired financial assets	**54**	39
Interest recognised on financial assets measured at amortised cost	**6,178**	N/A
Interest recognised on financial assets measured at fair value through other comprehensive income	**902**	N/A
Expense		
Interest on financial instruments, excluding interest on trading liabilities designated or otherwise mandatorily measured at fair value	**(3,074)**	(2,216)
Payments under lease and sublease agreements	**(76)**	(174)
– minimum lease payments	**(76)**	(171)
– contingent rents and sublease payments	**—**	(3)
Gains/(losses)		
Impairment of available-for-sale equity securities	**N/A**	(26)
Gains recognised on assets held for sale	**6**	65
Change in expected credit losses and other credit impairment charges	**(159)**	N/A
– loans and advances to banks and customers	**(196)**	N/A
– loans commitments and guarantees	**(42)**	N/A
– debt instruments measured at fair value though other comprehensive income	**79**	N/A
Loan impairment charges and other credit risk provisions	**N/A**	(495)
– net impairment charge on loans and advances	**N/A**	(624)
– release of impairment on available-for-sale debt securities	**N/A**	145
– other credit risk provisions	**N/A**	(16)

External net operating income is attributed to countries on the basis of the location of the branch responsible for reporting the results or advancing the funds:

	2018	2017
	£m	£m
External net operating income by country	**9,468**	13,052
– United Kingdom[1]	**6,537**	9,693
– France	**1,532**	1,708
– Germany	**654**	653
– Turkey[2]	**—**	133
– Other countries	**745**	865

1 Impacted by the transfers to HSBC UK Bank plc under the ring-fence implementation. For further information see Note 35 'Discontinued operations'.
2 On 29 June 2017, the Turkish operations transferred to HSBC Middle East Holdings B.V. and HSBC Bank Middle East Limited.

6 Employee compensation and benefits

	2018	2017
	£m	£m
Wages and salaries	**2,035**	2,550
Social security costs	**434**	475
Post-employment benefits	**60**	104
Year ended 31 Dec	**2,529**	3,129

Average number of persons employed by the group during the year

	2018[1,2]	2017[2]
Retail Banking and Wealth Management	**14,699**	24,793
Commercial Banking	**4,943**	6,659
Global Banking and Markets	**4,659**	5,295
Global Private Banking	**541**	677
Corporate Centre	**5,595**	7,918
Year ended 31 Dec	**30,437**	45,342

1 Impacted by the transfers to HSBC UK Bank plc and its subsidiaries under the ring-fence implementation. For further information, see Note 35 'Discontinued operations'.
2 In October 2017, 21,571 employees were transferred from the group to HSBC UK Bank plc, and were seconded back to the group until 30 June 2018.

Share-based payments

The share-based payment income statement charge is recognised in wages and salaries as follows:

	2018	2017
	£m	£m
Restricted share awards	99	104
Savings-related and other share award option plans	4	10
Year ended 31 Dec	**103**	114

HSBC share awards

Award	Policy
Restricted share awards (including annual incentive awards delivered in shares) and Group Performance Share Plan ('GPSP')	• An assessment of performance over the relevant period ending on 31 December is used to determine the amount of the award to be granted. • Deferred awards generally require employees to remain in employment over the vesting period and are not subject to performance conditions after the grant date. • Deferred share awards generally vest over a period of three years and GPSP awards vest after five years. • Vested shares may be subject to a retention requirement post-vesting. GPSP awards are retained until cessation of employment. • Awards granted from 2010 onwards are subject to a malus provision prior to vesting.
International Employee Share Purchase Plan ('ShareMatch')	• The plan was first introduced in Hong Kong in 2013 and now includes employees based in 25 jurisdictions. • Shares are purchased in the market each quarter up to a maximum value of £750, or the equivalent in local currency. • Matching awards are added at a ratio of one free share for every three purchased. • Matching awards vest subject to continued employment and the retention of the purchased shares for a maximum period of two years and nine months.

Movement on HSBC share awards

	2018	2017
	Number	Number
	(000s)	(000s)
Restricted share awards outstanding at 1 Jan	**25,368**	30,513
Transfers to HSBC UK Bank plc and its subsidiaries	(883)	N/A
Additions during the year[1]	20,315	17,287
Released in the year[1]	(20,737)	(21,858)
Forfeited in the year	(668)	(574)
Restricted share awards outstanding at 31 Dec	**23,395**	25,368
Weighted average fair value of awards granted (£)	6.35	5.00

1 Includes a number of share option plans transferred from or to other subsidiaries of HSBC Holdings plc.

HSBC share option plans

Main plans	Policy
Savings-related share option plans ('Sharesave')	• Two plans: the UK Plan and the International Plan. The last grant of options under the International Plan was in 2012. • From 2014, eligible employees can save up to £500 per month with the option to use the savings to acquire shares. • Exercisable within six months following either the third or fifth anniversary of the commencement of a three-year or five-year contract, respectively. • The exercise price is set at a 20% (2017: 20%) discount to the market value immediately preceding the date of invitation.
HSBC Holdings Group share option plan	• Plan ceased in May 2005. • Exercisable between the third and tenth anniversaries of the date of grant.

Calculation of fair values

The fair values of share options are calculated using a Black-Scholes model. The fair value of a share award is based on the share price at the date of the grant.

Movement on HSBC share option plans

	Savings-related share option plans	
	Number	WAEP[1]
	(000s)	£
Outstanding at 1 Jan 2018	**32,567**	**4.51**
Transfers to HSBC UK Bank plc and its subsidiaries	**(25,608)**	**4.50**
Granted during the year[2]	**2,205**	**5.19**
Exercised during the year[2]	**(3,742)**	**4.42**
Expired during the year	**(987)**	**4.99**
Forfeited during the year	**(427)**	**4.54**
Outstanding at 31 Dec 2018	**4,008**	**4.88**
Weighted average remaining contractual life (years)	**2.54**	
Outstanding at 1 Jan 2017	34,365	4.32
Granted during the year[2]	5,510	5.13
Exercised during the year[2]	(4,438)	4.61
Expired during the year	(2,870)	4.41
Outstanding at 31 Dec 2017	32,567	4.51
Weighted average remaining contractual life (years)	2.39	

1 *Weighted average exercise price.*
2 *Includes a number of share option plans transferred from or to other subsidiaries of HSBC Holdings plc.*

Post-employment benefit plans

We operate a number of pension plans throughout Europe for our employees. Some are defined benefit plans, and prior to ring-fencing, the largest was HSBC Bank (UK) Pension Scheme. Pension risk section on page 34 contains details about policies and practices associated with the pensions plans.

The group's balance sheet includes the net surplus or deficit, being the difference between the fair value of plan assets and the discounted value of scheme liabilities at the balance sheet date for each plan. Surpluses are only recognised to the extent that they are recoverable through reduced contributions in the future, or through potential future refunds from the schemes. In assessing whether a surplus is recoverable, the group has considered its current right to obtain a future refund or a reduction in future contributions.

HSBC Bank (UK) Pension Scheme

To meet the requirements of the Banking Reform Act, from 1 July 2018, the main employer of HSBC Bank (UK) Pension Scheme changed from HSBC Bank plc to HSBC UK Bank plc, with additional support from HSBC Holdings plc. At the same time, non-ring fenced entities including HSBC Bank plc exited the section of the plan for ring-fenced entities, and joined a newly created section with segregated assets and liabilities (approximately 0.2% of the total plan).

The plan has a defined benefit section and a defined contribution section. The defined benefit section was closed to future benefit accrual in 2015, with defined benefits earned by employees at that date continuing to be linked to their salary while they remain employed by HSBC. The new segregated section provides HSBC Bank plc employees with their defined contribution pension and, where relevant, defined benefit pension benefits arising from future salary increases above CPI. The plan is overseen by an independent corporate trustee, who has a fiduciary responsibility for the operation of the plan. Its assets are held separately from the assets of HSBC Group.

The first funding valuation of the new segregated section of the plan for HSBC Bank plc non ring-fenced entities is currently being assessed as at 31 December 2018. The assessment will be carried out by Colin G Singer, at Willis Towers Watson Limited, who is a Fellow of the UK Institute and Faculty of Actuaries, using the projected unit credit method.

Income statement charge

	2018	2017
	£m	£m
Defined benefit pension plans	**(33)**	(40)
Defined contribution pension plans	**91**	140
Pension plans	**58**	100
Defined benefit and contribution healthcare plans	**2**	4
Year ended 31 Dec 2018	**60**	104

Cumulative actuarial gains/(losses) recognised in other comprehensive income

	2018	2017
	£m	£m
At 1 Jan	**2,498**	105
Actuarial gains recognised in other comprehensive income for the year	**255**	2,393
At 31 Dec	**2,753**	2,498

Net assets/(liabilities) recognised on the balance sheet in respect of defined benefit plans

	Fair value of plan assets	Present value of defined benefit obligations	Effect of limit on plan surpluses	Total
	£m	£m	£m	£m
Defined benefit pension plans	**496**	**(723)**	**—**	**(227)**
Defined benefit healthcare plans	**—**	**(81)**	**—**	**(81)**
At 31 Dec 2018	**496**	**(804)**	**—**	**(308)**
Total employee benefit liabilities (within 'Accruals, deferred income and other liabilities')				**(332)**
Total employee benefit assets (within 'Prepayments, accrued income and other assets')				**24**
Defined benefit pension plans	28,309	(22,481)	—	5,828
Defined benefit healthcare plans	—	(100)	—	(100)
At 31 Dec 2017	28,309	(22,581)	—	5,728
Total employee benefit liabilities (within 'Accruals, deferred income and other liabilities')				(338)
Total employee benefit assets (within 'Prepayments, accrued income and other assets')				6,066

Defined benefit pension plans

Net asset/(liability) under defined benefit pension plans

	Fair value of plan assets		Present value of defined benefit obligations		Net defined benefit asset/ (liability)	
	HSBC Bank (UK) Pension Plan	Other plans	HSBC Bank (UK) Pension Plan	Other plans	HSBC Bank (UK) Pension Plan	Other plans
	£m	£m	£m	£m	£m	£m
At 1 Jan 2018	**27,940**	**369**	**(21,874)**	**(607)**	**6,066**	**(238)**
Reorganisation resulting from ring-fencing[1]	**(26,948)**	**—**	**20,580**	**—**	**(6,368)**	**—**
Transfer into HSBC Trinkaus & Burkhardt Pension Scheme	**—**	**8**	**—**	**(4)**	**—**	**4**
Service cost			**(7)**	**(19)**	**(7)**	**(19)**
– current service cost			**(8)**	**(22)**	**(8)**	**(22)**
– past service cost and gains from settlements			**1**	**3**	**1**	**3**
Net interest income/(cost) on the net defined benefit asset/(liability)	**359**	**3**	**(279)**	**(8)**	**80**	**(5)**
Remeasurement effects recognised in other comprehensive income	**(826)**	**(15)**	**1,073**	**7**	**247**	**(8)**
– return on plan assets (excluding interest income)	**(826)**	**(15)**			**(826)**	**(15)**
– actuarial gains			**1,073**	**7**	**1,073**	**7**
Exchange differences	**—**	**51**	**—**	**(53)**	**—**	**(2)**
Contributions by the group	**20**	**—**			**20**	**—**
– normal	**20**	**—**			**20**	**—**
Benefits paid	**(444)**	**—**	**444**	**18**	**—**	**18**
Administrative costs and taxes paid by plan	**(21)**	**—**	**7**	**(1)**	**(14)**	**(1)**
At 31 Dec 2018	**80**	**416**	**(56)**	**(667)**	**24**	**(251)**
Present value of defined benefit obligation relating to:						
– active			**(56)**	**(452)**		
– deferred			**—**	**(42)**		
– pensioners			**—**	**(173)**		
At 1 Jan 2017	26,891	430	(23,413)	(679)	3,478	(249)
Service cost			(90)	(20)	(90)	(20)
– current service cost			(10)	(20)	(10)	(20)
– past service cost and gains/(losses) from settlements			(80)	—	(80)	—
Net interest income/(cost) on the net defined benefit asset/(liability)	665	5	(576)	(9)	89	(4)
Remeasurement effects recognised in other comprehensive income	1,076	6	1,299	2	2,375	8
– return on plan assets (excluding interest income)	1,076	6			1,076	6
– actuarial gains			1,299	2	1,299	2
– other changes			—	—	—	—
Exchange differences	—	(44)	—	48	—	4
Contributions by the group	229	4			229	4
– normal	168	4			168	4
– special	61	—			61	—
Benefits paid	(888)	(32)	888	51	—	19
Administrative costs and taxes paid by plan	(33)	—	18	—	(15)	—
At 31 Dec 2017	27,940	369	(21,874)	(607)	6,066	(238)
Present value of defined benefit obligation relating to:						
– active			(4,052)	(422)		
– deferred			(6,468)	(42)		
– pensioners			(11,354)	(143)		

1 *A new section of the HSBC Bank (UK) Pension Scheme was created on 1 July 2018. The HSBC Bank plc non ring-fenced entities were transferred to the new section in respect of the pension benefit arising from future salary increase above CPI for employees.*

Directors' emoluments

The aggregate emoluments of the Directors of the bank, computed in accordance with the Companies Act 2006 as amended by statutory instrument 2008 No.410, were:

	2018	2017
	£000	£000
Fees[1]	1,586	1,830
Salaries and other emoluments[2]	1,276	1,581
Annual incentives[3]	515	810
Long-term incentives[4]	679	1,396
Year ended 31 Dec	**4,056**	5,617

1 *Fees paid to non-executive Directors.*
2 *Salaries and other emoluments include Fixed Pay Allowances.*
3 *Discretionary annual incentives for executive Directors are based on a combination of individual and corporate performance, and are determined by the Remuneration Committee of the bank's parent company, HSBC Holdings plc. Incentive awards made to executive directors are delivered in the form of cash and HSBC Holdings plc shares. The total amount shown is comprised of £257,400 (2017: £404,880) in cash and £257,400 (2017: £404,880) in Restricted Shares, which is the upfront portion of the annual incentive granted in respect of performance year 2018.*
4 *The amount shown is comprised of £135,525 (2017: £441,103) in deferred cash, £223,451 (2017: £700,709) in deferred Restricted Shares, and £319,734 (2017: £253,806) in shares under the Group Performance Share Plan ('GPSP'). These amounts relate to the portion of the awards that will vest following the substantial completion of the vesting condition attached to these awards in 2018. The total vesting period of deferred cash and share awards is no less than three years, with 33% of the award vesting on each of the first and second anniversaries of the date of the award, and the balance vesting on the third anniversary of the date of the award. The deferred share awards are subject to a six-month retention period upon vesting. GPSP awards are subject to a five-year vesting period and a retention requirement until cessation of employment upon vesting. Details of the Plans are contained within the Directors' Remuneration Report of HSBC Holdings plc. The cost of any awards subject to service conditions under the HSBC Share Plan 2011 are recognised through an annual charge based on the fair value of the awards, apportioned over the period of service to which the award relates.*

No Director exercised share options over HSBC Holdings plc ordinary shares during the year.

Awards were made to one Director under long-term incentive plans in respect of qualifying services rendered in 2018 (2017: one Director). During 2018, one Director received shares in respect of awards under long-term incentive plans that vested during the year (2017: one Director).

Retirement benefits are accruing to one Director under money purchase schemes in respect of Directors' qualifying services (2017: one Director). Contributions of £3,778 were made during the year to money purchase arrangements in respect of Directors' qualifying services (2017: £10,000).

In addition, there were payments under retirement benefit agreements with former Directors of £817,163 (2017: £791,152), including payments in respect of unfunded pension obligations to former Directors of £687,227 (2017: £666,214). The provision at 31 December 2018 in respect of unfunded pension obligations to former Directors amounted to £10,956,784 (2017: £11,695,477).

Of these aggregate figures, the following amounts are attributable to the highest paid Director:

	2018	2017
	£000	£000
Salaries and other emoluments	623	1,581
Annual incentives[1]	361	810
Long-term incentives[2]	575	1,396
Year ended 31 Dec	**1,559**	3,787

1 *Awards made to the highest paid Director are delivered in the form of cash and HSBC Holdings plc shares. The amount shown is comprised of £180,277 (2017: £404,880) in cash and £180,277 (2017: £404,880) in Restricted Shares.*
2 *The amount shown is comprised of £108,586 (2017: £441,103) in deferred cash, £178,022 (2017: £700,709) in deferred Restricted Shares and £288,351 (2017: £253,806) in shares under the GPSP. These amounts relate to a portion of the awards that will vest following the substantial completion of the vesting condition attached to these awards in 2018. The total vesting period of deferred cash and share awards is no less than three years, with 33% of the award vesting on each of the first and second anniversaries of the date of the award, and the balance vesting on the third anniversary of the date of the award. The share awards are subject to a six-month retention period upon vesting. GPSP awards are subject to a five-year vesting period and a retention requirement until cessation of employment upon vesting.*

The highest paid Director received shares in respect of qualifying services under a long-term incentive scheme.

Pension contributions of £3,778 were made by the bank in respect of services by the highest paid Director during the year (2017: £10,000).

7 Auditors' remuneration

	2018	2017
	£m	£m
Audit fees payable to PwC	11.8	14.1
Other audit fees payable	0.4	0.5
Year ended 31 Dec	**12.2**	14.6

Fees payable by the group to PwC

	2018	2017
	£m	£m
Audit fees for HSBC Bank plc's statutory audit[1]	6.7	7.7
Fees for other services provided to the group	11.8	13.3
– audit of the group's subsidiaries[2]	5.1	6.4
– audit-related assurance services[3]	2.2	2.5
– other assurance services	4.4	4.0
– other non-audit services[4]	0.1	0.4
Year ended 31 Dec[5]	18.5	21.0

1 Fees payable to PwC for the statutory audit of the consolidated financial statements of the group and the separate financial statements of HSBC Bank plc. They exclude amounts payable for the statutory audit of the bank's subsidiaries which have been included in 'Fees for other services provided to the group'.
2 Including fees payable to PwC for the statutory audit of the bank's subsidiaries.
3 Including services for assurance and other services that relate to statutory and regulatory filings, including comfort letters and interim reviews.
4 Including other permitted services relating to advisory, corporate finance transactions, etc.
5 The 2017 comparatives have been represented to reflect the Financial Reporting Council guidance regarding classifications of non-audit services. The totals remain unchanged for 2017.

Fees payable for non-audit services for HSBC Bank plc are not disclosed separately because such fees are disclosed on a consolidated basis for the group.

8 Tax

Tax expense

	2018	2017
	£m	£m
Current tax	490	599
– for this year	512	642
– adjustments in respect of prior years	(22)	(43)
Deferred tax	(48)	(71)
– origination and reversal of temporary differences	(61)	(18)
– effect of changes in tax rates	13	(15)
– adjustments in respect of prior years	—	(38)
Year ended 31 Dec	442	528
Continued operations	119	198
Discontinued operations	323	330

The group's profits are taxed at different rates depending on the country in which the profits arise. The key applicable corporate tax rates in 2018 include the UK and France. The UK tax rate applying to HSBC Bank plc and its banking subsidiaries was 27.00% (2017: 27.25%), comprising 19% corporation tax plus 8% surcharge on UK banking profits. The decrease from 2017 is due to the reduction in the corporation tax rate from 20% to 19% from 1 April 2017. The 19% rate of corporation tax in the UK will be reduced to 17% on 1 April 2020. The applicable tax rate in France was 34% (2017: 44%) and will be reduced to 26% from 1 January 2022. Other overseas subsidiaries and overseas branches provided for taxation at the appropriate rates in the countries in which they operate. The tax relating to discontinued operations relates to the activities transferred to HSBC Bank UK plc on 1 July 2018.

Tax reconciliation

The tax charged to the income statement differs from the tax expense that would apply if all profits had been taxed at the UK corporation tax rate as follows:

	2018		2017	
	£m	%	£m	%
Profit before tax	1,974		2,370	
Tax expense				
UK corporation tax at 19.00% (2017: 19.25%)	375	19.00	456	19.25
8% surcharge on UK banking profits	94	4.8	108	4.6
Non-deductible customer compensation expense	(2)	(0.1)	129	5.4
Permanent disallowables	38	1.9	99	4.2
Impact of taxing overseas profits at different rates	32	1.6	106	4.5
Local taxes and overseas withholding taxes	52	2.6	31	1.3
Impairment of goodwill	—	—	9	0.3
Non-deductible regulatory settlements	(8)	(0.4)	(153)	(6.5)
Non-taxable income and gains subject to tax at a lower rate	(106)	(5.4)	(129)	(5.4)
Adjustment in respect of prior years	(22)	(1.1)	(81)	(3.4)
Movements in unrecognised deferred tax	(8)	(0.4)	(25)	(1.1)
Change in tax rates	13	0.7	(15)	(0.6)
Other	(16)	(0.8)	(7)	(0.3)
Year ended 31 Dec	442	22.4	528	22.3
Continued operations	119		198	
Discontinued operations	323		330	

The effective tax rate for the year was 22.4 % (2017: 22.3%). This was higher than 2017 mainly due to a lower level of non-taxable regulatory provision releases and other non-taxable income, offset by a reduced level of overseas profits taxed at higher rates and a lower

level of non-deductible expenses.

Accounting for taxes involves some estimation because the tax law is uncertain and the application requires a degree of judgement, which authorities may dispute. Liabilities are recognised based on best estimates of the probable outcome, taking into account external advice where appropriate. We do not expect significant liabilities to arise in excess of the amounts provided. The current tax asset includes an estimate of tax recoverable from HMRC with regards to past dividends received from EU resident companies. The ultimate resolution of this matter involves litigation for which the outcome is uncertain and is unlikely to be resolved in the short-term.

Movement of deferred tax assets and liabilities

The group	Retirement benefits £m	Loan impairment provisions £m	Property, plant and equipment £m	FVOCI/ Available-for-sale investments £m	Goodwill and intangibles £m	Other[1] £m	Total £m
Assets[2]	**34**	**35**	**349**	**—**	**185**	**134**	**737**
Liabilities[2]	**(1,455)**	**(5)**	**—**	**(80)**	**—**	**—**	**(1,540)**
At 1 Jan 2018	**(1,421)**	**30**	**349**	**(80)**	**185**	**134**	**(803)**
IFRS 9 transitional adjustment	**—**	**38**	**(1)**	**153**	**(1)**	**(17)**	**172**
Transfer to HSBC UK Bank plc and its subsidiaries	**1,592**	**(156)**	**(73)**	**1**	**(20)**	**(10)**	**1,334**
Income statement	**8**	**(13)**	**(3)**	**—**	**10**	**46**	**48**
Other comprehensive income	**(87)**	**129**	**—**	**(147)**	**—**	**(135)**	**(240)**
At 31 Dec 2018	**92**	**28**	**272**	**(73)**	**174**	**18**	**511**
Assets[2]	**92**	**32**	**281**	**—**	**174**	**26**	**605**
Liabilities[2]	**—**	**(4)**	**(9)**	**(73)**	**—**	**(8)**	**(94)**
Assets[2]	75	78	297	—	156	428	1,034
Liabilities[2]	(840)	(11)	(7)	(100)	(9)	(444)	(1,411)
At 1 Jan 2017	(765)	67	290	(100)	147	(16)	(377)
Income statement	(61)	(22)	73	(4)	36	49	71
Other comprehensive income	(596)	—	—	27	—	67	(502)
Equity	—	—	—	—	—	11	11
Foreign exchange and other adjustments	1	(15)	(14)	(3)	2	23	(6)
At 31 Dec 2017	(1,421)	30	349	(80)	185	134	(803)
Assets[2]	34	35	349	—	185	134	737
Liabilities[2]	(1,455)	(5)	—	(80)	—	—	(1,540)

1 *Other deferred tax assets and liabilities relate to unused tax losses, share-based payments and cash flow hedges.*
2 *After netting off balances within countries, the balances as disclosed in the accounts are as follows: deferred tax assets £540m (2017: £130m); and deferred tax liabilities £29m (2017: £933m).*

Movement of deferred tax assets and liabilities

The bank	Retirement benefits £m	Property, plant and equipment £m	Goodwill and intangibles £m	Other[1] £m	Total £m
Assets[2]	**—**	**289**	**192**	**81**	**562**
Lliabilities[2]	**(1,489)**	**—**	**—**	**—**	**(1,489)**
At 1 Jan 2018	**(1,489)**	**289**	**192**	**81**	**(927)**
IFRS 9 transitional adjustment	**1**	**—**	**—**	**143**	**144**
Transfer to HSBC UK Bank plc	**1,592**	**(47)**	**(23)**	**(154)**	**1,368**
Income statement	**7**	**13**	**8**	**(2)**	**26**
Other comprehensive income	**(89)**	**—**	**—**	**(76)**	**(165)**
Foreign exchange and other adjustments	**—**	**—**	**—**	**(1)**	**(1)**
At 31 Dec 2018	**22**	**255**	**177**	**(9)**	**445**
Assets[2]	**22**	**257**	**177**	**—**	**456**
Liabilities[2]	**—**	**(2)**	**—**	**(9)**	**(11)**
Assets[2]	—	217	156	94	467
Liabilities[2]	(838)	—	—	(93)	(931)
At 1 Jan 2017	(838)	217	156	1	(464)
Income statement	(57)	72	35	79	129
Other comprehensive income	(594)	—	—	—	(594)
Equity	—	—	—	—	—
Foreign exchange and other adjustments	—	—	1	1	2
At 31 Dec 2017	(1,489)	289	192	81	(927)
Assets[2]	—	289	192	81	562
Liabilities[2]	(1,489)	—	—	—	(1,489)

1 *Other deferred tax assets and liabilities relate to fair value of own debt, loan impairment allowances, unused tax losses, share-based payments and cash flow hedges.*
2 *After netting off balances within countries, the balances as disclosed in the accounts are as follows: deferred tax assets £447m (2017: £5m) and deferred tax liabilities £2m (2017: £932m).*

Unrecognised deferred tax

The group

The amount of temporary differences, unused tax losses and tax credits for which no deferred tax asset is recognised in the balance sheet was £870m (2017: £765m). These amounts consist of unused tax losses and tax credits arising in the US branch of £694m (2017: £513m) and unused temporary differences and tax losses in Europe of £176m (2017: £251m). The majority of the unrecognised losses in the group expire after 10 years.

The bank

The amount of temporary differences, unused tax losses and tax credits for which no deferred tax asset is recognised in the balance sheet was £825m (2017: £707m). These amounts include unused tax losses and tax credits arising in the US branch of £694m (2017: £513m) and unused temporary differences and tax losses in Europe of £131m (2017: £251m). The unrecognised losses in the bank expire after 10 years.

There are no unrecognised deferred tax liabilities arising from the group's investments in subsidiaries and branches.

9 Dividends

Dividends to shareholders of the parent company

	2018		2017	
	£ per share	**£m**	£ per share	£m
Dividends paid on ordinary shares				
Second interim dividend in respect of the previous year	**0.73**	**583**	0.52	415
First interim dividend in respect of the current year	**0.30**	**234**	0.23	186
Total	**1.03**	**817**	0.75	601
Dividends on preference shares classified as equity				
Dividend on HSBC Bank plc non-cumulative third dollar preference shares	**1.47**	**51**	1.43	50
Total	**1.47**	**51**	1.43	50

A second interim dividend for 2018 of £406m to the shareholder of the parent company was declared by the Directors after 31 December 2018 (Note 36).

In addition to the second interim dividend above, a special dividend of £674m was declared after 31 December 2018 on the ordinary share capital of HSBC Bank plc in respect of 2018 and will be payable on the 26 February 2019.

The total dividend declared on ordinary shares in respect of 2018 was £1,314m (2017: £769m).

Transfer of the ring-fenced bank

On the 22 June, the Directors declared a dividend for 2018 of £12bn to the shareholder of the parent company with respect to ring-fencing. The dividend was distributed on 1 July 2018 on completion of ring-fencing. This dividend did not form part of the regular dividend policy.

Total coupons on capital securities classified as equity

		2018	2017
	First call date	**£m**	£m
Undated Subordinated additional Tier 1 instruments			
– £1,096m[1]	Dec 2019	**31**	59
– £1,100m[1]	Dec 2024	**31**	61
– €1,900m	Dec 2020	**102**	100
– €235m	Jan 2022	**12**	1
		176	221

1 *With effect from 1 July 2018 under the ring-fencing transfer scheme, all rights and obligations in respect of the existing £1,096m Undated Subordinated Additional Tier 1 Instrument issued 2014 (Callable December 2019 onwards) and £1,100m Undated Subordinated Additional Tier 1 Instrument issued 2014 (Callable December 2024 onwards) issued by HSBC Bank plc were transferred to HSBC UK Bank plc.*

10 Trading assets

	The group		The bank	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Treasury and other eligible bills	**2,411**	1,948	**1,104**	1,379
Debt securities[1, 2]	**41,108**	37,536	**26,144**	22,333
Equity securities	**35,257**	63,131	**33,695**	60,384
Trading securities	**78,776**	102,615	**60,943**	84,096
Loans and advances to banks[3, 4]	**7,857**	20,590	**7,148**	17,744
Loans and advances to customers[3, 4]	**8,787**	22,520	**9,674**	22,254
At 31 Dec	**95,420**	145,725	**77,765**	124,094

1 *Included within the above figures for the group are debt securities issued by banks and other financial institutions of £9,564m (2017: £8,659m), of which £1,486m (2017: £551m) are guaranteed by various governments.*
2 *Included within the above figures for the bank are debt securities issued by banks and other financial institutions of £6,951m (2017: £6,272m), of which £985m (2017: nil) are guaranteed by governments.*
3 *Loans and advances to banks and customers include reverse repos, stock borrowing and other amounts.*
4 *Settlement accounts, cash collateral and margin receivables included within 'Loans and advances to banks' and 'Loans and advances to customers' (the group: £26,447m; the bank: £22,772m) were reclassified from 'Trading assets' to 'Prepayments, accrued income and other assets' on 1 January 2018, and comparative data was not restated. This reclassification was in accordance with IFRS 9. Refer to Note 34 'Effects of reclassifications upon adoption of IFRS 9' for further details.*

11 Fair values of financial instruments carried at fair value

Control framework

Fair values are subject to a control framework designed to ensure that they are either determined or validated by a function independent of the risk taker.

For all financial instruments where fair values are determined by reference to externally quoted prices or observable pricing inputs to models, independent price determination or validation is utilised. In inactive markets, the group will source alternative market information to validate the financial instrument's fair value, with greater weight given to information that is considered to be more relevant and reliable. The factors that are considered in this regard are, *inter alia*:

- the extent to which prices may be expected to represent genuine traded or tradable prices;
- the degree of similarity between financial instruments;
- the degree of consistency between different sources;
- the process followed by the pricing provider to derive the data;
- the elapsed time between the date to which the market data relates and the balance sheet date; and
- the manner in which the data was sourced.

For fair values determined using valuation models, the control framework may include, as applicable, development or validation by independent support functions of: (i) the logic within valuation models; (ii) the inputs to these models; (iii) any adjustments required outside the valuation models; and (iv) where possible, model outputs. Valuation models are subject to a process of due diligence and calibration before becoming operational and are calibrated against external market data on an ongoing basis.

Financial liabilities measured at fair value

In certain circumstances, the group records its own debt in issue at fair value, based on quoted prices in an active market for the specific instrument. When quoted market prices are unavailable, the own debt in issue is valued using valuation techniques, the inputs for which are based either on quoted prices in an inactive market for the instrument or are estimated by comparison with quoted prices in an active market for similar instruments. In both cases, the fair value includes the effect of applying the credit spread that is appropriate to the group's liabilities.

Structured notes issued and certain other hybrid instruments are included within trading liabilities and are measured at fair value. The spread applied to these instruments is derived from the spreads at which the group issues structured notes.

Fair value hierarchy

Fair values of financial assets and liabilities are determined according to the following hierarchy:

- Level 1 – valuation technique using quoted market price: financial instruments with quoted prices for identical instruments in active markets that HSBC can access at the measurement date.
- Level 2 – valuation technique using observable inputs: financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.
- Level 3 – valuation technique with significant unobservable inputs: financial instruments valued using valuation techniques where one or more significant inputs are unobservable.

Financial instruments carried at fair value and bases of valuation

	2018				2017			
	Level 1	**Level 2**	**Level 3**	**Total**	Level 1	Level 2	Level 3	Total
The group	**£m**	**£m**	**£m**	**£m**	£m	£m	£m	£m
Recurring fair value measurements at 31 Dec								
Assets								
Trading assets	**69,774**	**22,094**	**3,552**	**95,420**	92,032	51,409	2,284	145,725
Financial assets designated and otherwise mandatorily measured at fair value through profit or loss	**10,128**	**5,590**	**2,081**	**17,799**	N/A	N/A	N/A	N/A
Derivatives	**1,101**	**141,341**	**2,080**	**144,522**	234	141,337	1,764	143,335
Financial assets designated at fair value	**N/A**	**N/A**	**N/A**	**N/A**	8,936	276	54	9,266
Financial investments	**40,237**	**6,232**	**790**	**47,259**	46,967	9,598	1,435	58,000
Liabilities								
Trading liabilities	**35,964**	**13,504**	**46**	**49,514**	31,396	74,096	1,004	106,496
Financial liabilities designated at fair value	**5,337**	**30,595**	**990**	**36,922**	3,082	15,167	—	18,249
Derivatives	**1,420**	**137,049**	**1,463**	**139,932**	597	138,140	1,333	140,070

Financial instruments carried at fair value and bases of valuation

	2018				2017			
	Level 1	**Level 2**	**Level 3**	**Total**	Level 1	Level 2	Level 3	Total
The bank	**£m**	**£m**	**£m**	**£m**	£m	£m	£m	£m
Recurring fair value measurements at 31 Dec								
Assets								
Trading assets	**53,104**	**21,075**	**3,586**	**77,765**	74,535	47,200	2,359	124,094
Financial assets designated and otherwise mandatorily measured at fair value through profit or loss	**24**	**5,051**	**670**	**5,745**	N/A	N/A	N/A	N/A
Derivatives	**849**	**136,247**	**2,133**	**139,229**	69	133,359	1,808	135,236
Financial assets designated at fair value	**N/A**	**N/A**	**N/A**	**N/A**	—	—	—	—
Financial investments	**24,511**	**2,116**	**72**	**26,699**	27,493	2,817	1,072	31,382
Liabilities								
Trading liabilities	**15,128**	**12,154**	**19**	**27,301**	10,529	66,042	732	77,303
Financial liabilities designated at fair value	**—**	**22,203**	**728**	**22,931**	—	11,006	—	11,006
Derivatives	**1,237**	**132,351**	**1,719**	**135,307**	425	131,003	1,607	133,035

Transfers between Level 1 and Level 2 fair values

	Assets				**Liabilities**		
	Financial investments	**Trading assets**	**Designated and otherwise mandatorily measured at fair value through profit or loss[2]**	**Derivatives**	**Trading liabilities**	**Designated at fair value**	**Derivatives**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
At 31 Dec 2018							
Transfers from Level 1 to Level 2	**—**	**183**	**—**	**—**	**33**	**—**	**—**
Transfers from Level 2 to Level 1[1]	**—**	**1,625**	**—**	**(96)**	**1,275**	**—**	**(103)**

	Assets				Liabilities		
	Available-for-sale	Held for trading	Designated at fair value	Derivatives	Held for trading	Designated at fair value	Derivatives
	£m	£m	£m	£m	£m	£m	£m
At 31 Dec 2017							
Transfers from Level 1 to Level 2	714	29	—	—	11	—	—
Transfers from Level 2 to Level 1	—	84	—	—	28	—	—

1 *Liquid corporate bonds of £1,547m in trading assets and £1,220m in trading liabilities were transferred from Level 2 to Level 1 during the period.*
2 *The group adopted IFRS 9 on 1 January 2018 resulting in the reclassification of certain financial assets and liabilities. The comparatives for 'financial assets designated and otherwise mandatorily measured at fair value through profit or loss' refer to prior period 'financial assets designated at fair value'. Refer to Note 34 'Effects of reclassifications upon adoption of IFRS 9' for further details.*

Transfers between levels of the fair value hierarchy are deemed to occur at the end of each quarterly reporting period. Transfers into and out of levels of the fair value hierarchy are normally attributable to observability of valuation inputs and price transparency. In the current year the majority of the transfer relates to the reclassification of certain positions where improved data is now available.

Fair value adjustments

Fair value adjustments are adopted when the group determines there are additional factors considered by market participants that are not incorporated within the valuation model. Movements in the level of fair value adjustments do not necessarily result in the recognition of profits or losses within the income statement, such as when models are enhanced and fair value adjustments may no longer be required.

Bid-offer

IFRS 13 'Fair value measurement' requires use of the price within the bid-offer spread that is most representative of fair value. Valuation models will typically generate mid-market values. The bid-offer adjustment reflects the extent to which bid-offer costs would be incurred

if substantially all residual net portfolio market risks were closed using available hedging instruments or by disposing of or unwinding the position.

Uncertainty

Certain model inputs may be less readily determinable from market data, and/or the choice of model itself may be more subjective. In these circumstances, an adjustment may be necessary to reflect the likelihood that market participants would adopt more conservative values for uncertain parameters and/or model assumptions than those used in the valuation model.

Credit and debit valuation adjustments

The CVA is an adjustment to the valuation of over-the-counter ('OTC') derivative contracts to reflect the possibility that the counterparty may default, and that the group may not receive the full market value of the transactions.

The DVA is an adjustment to the valuation of OTC derivative contracts to reflect the possibility that HSBC may default, and that it may not pay the full market value of the transactions.

HSBC calculates a separate CVA and DVA for each legal entity, and for each counterparty to which the entity has exposure. With the exception of central clearing parties, all third-party counterparties are included in the CVA and DVA calculations, and these adjustments are not netted across Group entities.

HSBC calculates the CVA by applying the probability of default ('PD') of the counterparty, conditional on the non-default of HSBC, to HSBC's expected positive exposure to the counterparty and multiplying the result by the loss expected in the event of default.

Conversely, HSBC calculates the DVA by applying the PD of HSBC, conditional on the non-default of the counterparty, to the expected positive exposure of the counterparty to HSBC and multiplying the result by the proportional loss expected in the event of default. Both calculations are performed over the life of the potential exposure.

For most products, HSBC uses a simulation methodology, which incorporates a range of potential exposures over the life of the portfolio, to calculate the expected positive exposure to a counterparty. The simulation methodology includes credit mitigants, such as counterparty netting agreements and collateral agreements with the counterparty.

The methodologies do not, in general, account for 'wrong-way risk', which arises when the underlying value of the derivative prior to any CVA is positively correlated to the PD of the counterparty. When there is significant wrong-way risk, a trade-specific approach is applied to reflect this risk in the valuation.

Funding fair value adjustment

The FFVA is calculated by applying future market funding spreads to the expected future funding exposure of any uncollateralised component of the OTC derivative portfolio. The expected future funding exposure is calculated by a simulation methodology, where available, and is adjusted for events that may terminate the exposure, such as the default of HSBC or the counterparty. The FFVA and DVA are calculated independently.

Model limitation

Models used for portfolio valuation purposes may be based upon a simplified set of assumptions that do not capture all current and future material market characteristics. In these circumstances, model limitation adjustments are adopted.

Inception profit (Day 1 P&L reserves)

Inception profit adjustments are adopted when the fair value estimated by a valuation model is based on one or more significant unobservable inputs. The accounting for inception profit adjustments is discussed in Note 1.

Fair value valuation bases

Financial instruments measured at fair value using a valuation technique with significant unobservable inputs – Level 3

	Assets					Liabilities			
	Financial Investments	Held for trading	Designated and otherwise mandatorily measured at fair value through profit or loss	Derivatives	Total	Held for trading	Designated at fair value	Derivatives	Total
The group	£m	£m	£m	£m	£m	£m	£m	£m	£m
Private equity including strategic investments	62	10	1,673	—	1,745	10	—	—	10
Asset-backed securities	723	730	24	—	1,477	—	—	—	—
Structured notes	—	2	—	—	2	36	990	—	1,026
Derivatives	—	—	—	2,080	2,080	—	—	1,463	1,463
Other portfolios	5	2,810	384	–	3,199	–	–	—	—
At 31 Dec 2018	**790**	**3,552**	**2,081**	**2,080**	**8,503**	**46**	**990**	**1,463**	**2,499**

	Assets					Liabilities			
	Available-for-sale	Held for trading	Designated at fair value	Derivatives	Total	Held for trading	Designated at fair value	Derivatives	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Private equity including strategic investments	547	15	54	—	616	14	—	—	14
Asset-backed securities	879	888	—	—	1,767	—	—	—	—
Structured notes	—	2	—	—	2	990	—	—	990
Derivatives	—	—	—	1,764	1,764	—	—	1,333	1,333
Other portfolios	9	1,379	—	—	1,388	—	—	—	—
At 31 Dec 2017	1,435	2,284	54	1,764	5,537	1,004	—	1,333	2,337

Financial instruments measured at fair value using a valuation technique with significant unobservable inputs – Level 3 (continued)

	Assets					Liabilities			
	Financial Investments	**Held for trading**	**Designated and otherwise mandatorily measured at fair value through profit or loss**	**Derivatives**	**Total**	**Held for trading**	**Designated at fair value**	**Derivatives**	**Total**
The bank	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Private equity including strategic investments	**53**	**1**	**444**	**–**	**498**	**–**	**–**	**–**	**–**
Asset-backed securities	**19**	**776**	**226**	**–**	**1,021**	**–**	**–**	**–**	**–**
Structured notes	**–**	**–**	**–**	**–**	**–**	**19**	**728**	**–**	**747**
Derivatives	**–**	**–**	**–**	**2,133**	**2,133**	**–**	**–**	**1,713**	**1,713**
Other portfolios	**–**	**2,809**	**–**	**–**	**2,809**	**–**	**–**	**6**	**6**
At 31 Dec 2018	**72**	**3,586**	**670**	**2,133**	**6,461**	**19**	**728**	**1,719**	**2,466**

	Assets					Liabilities			
	Available-for-sale	Held for trading	Designated at fair value	Derivatives	Total	Held for trading	Designated at fair value	Derivatives	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Private equity including strategic investments	347	—	—	—	347	—	—	—	—
Asset-backed securities	725	980	—	—	1,705	—	—	—	—
Structured notes	—	—	—	—	—	732	—	—	732
Derivatives	—	—	—	1,808	1,808	—	—	1,607	1,607
Other portfolios	—	1,379	—	—	1,379	—	—	—	—
At 31 Dec 2017	1,072	2,359	—	1,808	5,239	732	—	1,607	2,339

Level 3 instruments are present in both ongoing and legacy businesses. Loans held for securitisation, derivatives with monolines, certain 'other derivatives' and predominantly all Level 3 ABSs are legacy positions. HSBC has the capability to hold these positions.

Private equity including strategic investments

The investment's fair value is estimated: on the basis of an analysis of the investee's financial position and results, risk profile, prospects and other factors; by reference to market valuations for similar entities quoted in an active market; or the price at which similar companies have changed ownership.

Asset-backed securities

While quoted market prices are generally used to determine the fair value of these securities, valuation models are used to substantiate the reliability of the limited market data available and to identify whether any adjustments to quoted market prices are required. For certain ABSs, such as residential mortgage-backed securities, the valuation uses an industry standard model with assumptions relating to prepayment speeds, default rates and loss severity based on collateral type, and performance, as appropriate. The valuations output is benchmarked for consistency against observable data for securities of a similar nature.

Structured notes

The fair value of Level 3 structured notes is derived from the fair value of the underlying debt security, and the fair value of the embedded derivative is determined as described in the paragraph below on derivatives. These structured notes comprise principally equity-linked notes, issued by HSBC, which provide the counterparty with a return linked to the performance of equity securities and other portfolios. Examples of the unobservable parameters include long-dated equity volatilities and correlations between equity prices, and interest and foreign exchange rates.

Derivatives

OTC derivative valuation models calculate the present value of expected future cash flows, based upon 'no-arbitrage' principles. For many vanilla derivative products, the modelling approaches used are standard across the industry. For more complex derivative products, there may be some differences in market practice. Inputs to valuation models are determined from observable market data, wherever possible, including prices available from exchanges, dealers, brokers or providers of consensus pricing. Certain inputs may not be observable in the market directly, but can be determined from observable prices through model calibration procedures or estimated from historical data or other sources.

Reconciliation of fair value measurements in Level 3 of the fair value hierarchy

Movement in Level 3 financial instruments

	Assets				Liabilities		
	Financial Investments	**Trading assets**	**Designated and otherwise mandatorily measured at fair value through profit or loss**	**Derivatives**	**Trading liabilities**	**Designated at fair value**	**Derivatives**
The group	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
At 1 Jan 2018	**943**	**2,284**	**1,794**	**1,764**	**67**	**937**	**1,333**
Total gains/(losses) recognised in profit or loss	**(1)**	**118**	**307**	**586**	**(2)**	**(111)**	**181**
– net income from financial instruments held for trading or managed on a fair value basis	**—**	**118**	**—**	**586**	**(2)**	**—**	**181**
– changes in fair value of other financial instruments mandatorily measured at fair value through profit or loss	**—**	**—**	**307**	**—**	**—**	**(111)**	**—**
– gains less losses from financial investments at fair value through other comprehensive income	**(1)**	**—**	**—**	**—**	**—**	**—**	**—**
Total gains/(losses) recognised in other comprehensive income ('OCI')	**61**	**145**	**—**	**(4)**	**—**	**3**	**1**
– financial investments: fair value gains/(losses)	**25**	**—**	**—**	**—**	**—**	**—**	**—**
– exchange differences	**36**	**145**	**—**	**(4)**	**—**	**3**	**1**
Purchases	**25**	**3,059**	**524**	**6**	**3**	**57**	**79**
New issuances	**—**	**701**	**—**	**6**	**4**	**1,287**	**26**
Sales	**(35)**	**(991)**	**(240)**	**—**	**(9)**	**—**	**(11)**
Settlements	**(93)**	**(1,463)**	**(282)**	**(123)**	**(1)**	**(812)**	**59**
Transfers out	**(347)**	**(1,114)**	**(71)**	**(257)**	**(16)**	**(371)**	**(354)**
Transfers in	**237**	**813**	**49**	**102**	**—**	**—**	**149**
At 31 Dec 2018	**790**	**3,552**	**2,081**	**2,080**	**46**	**990**	**1,463**
Unrealised gains/(losses) recognised in profit or loss relating to assets and liabilities held at 31 Dec 2018	**—**	**(5)**	**89**	**302**	**4**	**56**	**245**
– trading income/(expense) excluding net interest income	**—**	**(5)**	**—**	**302**	**4**	**—**	**245**
– net income/(expense) from other financial instruments designated at fair value	**—**	**—**	**89**	**—**	**—**	**56**	**—**

	Assets				Liabilities		
	Available-for-sale	Held for trading	Designated at fair value	Derivatives	Held for trading	Designated at fair value	Derivatives
	£m	£m	£m	£m	£m	£m	£m
At 1 Jan 2017	982	2,721	21	2,151	762	5	1,877
Total gains/(losses) recognised in profit or loss	(24)	(171)	(3)	36	52	(5)	433
– trading income/(expense) excluding net interest income	—	(171)	—	36	52	—	433
– gains less losses from financial investments	(24)	—	(3)	—	—	(5)	—
Total gains/(losses) recognised in other comprehensive income ('OCI')[1]	108	(121)	1	(26)	8	—	(30)
– available-for-sale investments: fair value gains/(losses)	146	—	—	—	—	—	—
– cash flow hedges: fair value gains/(losses)	—	—	—	(18)	—	—	(28)
– exchange differences	(38)	(121)	1	(8)	8	—	(2)
Purchases	112	1,026	36	2	4	—	—
New issuances	—	—	—	—	776	—	—
Sales	(131)	(1,464)	—	(6)	(9)	—	(12)
Settlements	(46)	(230)	—	(12)	(459)	—	(272)
Transfers out	(269)	(101)	(1)	(595)	(144)	—	(814)
Transfers in	703	624	—	214	14	—	151
At 31 Dec 2017	1,435	2,284	54	1,764	1,004	—	1,333
Unrealised gains/(losses) recognised in profit or loss relating to assets and liabilities held at 31 Dec 2017	17	22	4	76	156	—	173
– trading income/(expense) excluding net interest income	—	22	—	76	156	—	173
– net income from other financial instruments designated at fair value	—	—	4	—	—	—	—
– loan impairment charges and other credit risk provisions	17	—	—	—	—	—	—

1 *Included in 'Available-for-sale investments: fair value gains/(losses)' and 'Exchange differences' in the consolidated statement of comprehensive income.*

Movement in Level 3 financial instruments (continued)

The bank	Assets				Liabilities		
	Financial Investments	Trading Assets	Designated and otherwise mandatorily measured at fair value through profit or loss	Derivatives	Trading Liabilities	Designated at fair value	Derivatives
	£m	£m	£m	£m	£m	£m	£m
At 1 Jan 2018	**140**	**2,362**	**980**	**1,808**	**32**	**700**	**1,605**
Total gains/(losses) recognised in profit or loss	**(1)**	**117**	**98**	**610**	**(2)**	**(87)**	**187**
– net income from financial instruments held for trading or managed on a fair value basis	**—**	**117**	**—**	**610**	**(2)**	**—**	**187**
– changes in fair value of other financial instruments mandatorily measured at fair value through profit or loss	**—**	**—**	**98**	**—**	**—**	**(87)**	**—**
– gains less losses from financial investments at fair value through other comprehensive income	**(1)**	**—**	**—**	**—**	**—**	**—**	**—**
Total gains/(losses) recognised in other comprehensive income ('OCI')	**1**	**144**	**16**	**—**	**—**	**—**	**—**
– exchange differences	**1**	**144**	**16**	**—**	**—**	**—**	**—**
Purchases	**23**	**3,126**	**18**	**—**	**—**	**—**	**76**
New issuances	**—**	**701**	**—**	**6**	**—**	**1,273**	**39**
Sales	**(12)**	**(1,101)**	**(278)**	**—**	**—**	**—**	**(11)**
Settlements	**(10)**	**(1,462)**	**(164)**	**(130)**	**6**	**(797)**	**52**
Transfers out	**(73)**	**(1,114)**	**—**	**(265)**	**(17)**	**(361)**	**(367)**
Transfers in	**4**	**813**	**—**	**104**	**—**	**—**	**138**
At 31 Dec 2018	**72**	**3,586**	**670**	**2,133**	**19**	**728**	**1,719**
Unrealised gains/(losses) recognised in profit or loss relating to assets and liabilities held at 31 Dec 2018	**—**	**(5)**	**6**	**255**	**(4)**	**48**	**(246)**
– trading income/(expense) excluding net interest income	**—**	**(5)**	**—**	**255**	**(4)**	**—**	**(246)**
– net income/(expense) from other financial instruments designated at fair value	**—**	**—**	**6**	**—**	**—**	**48**	**—**

	Assets				Liabilities		
	Available-for-sale	Held for trading	Designated at fair value	Derivatives	Held for trading	Designated at fair value	Derivatives
	£m	£m	£m	£m	£m	£m	£m
At 1 Jan 2017[1]	1,426	2,722	—	2,242	499	—	2,115
Total gains/(losses) recognised in profit or loss	—	(139)	—	33	28	—	427
– trading income/(expense) excluding net interest income	—	(139)	—	33	28	—	427
– gains less losses from financial investments	—	—	—	—	—	—	—
Total gains/(losses) recognised in other comprehensive income ('OCI')[2]	189	(122)	—	(42)	—	—	(30)
– available-for-sale investments: fair value gains/(losses)	197	—	—	—	—	—	—
– cash flow hedges: fair value gains/(losses)	—	—	—	(25)	—	—	(28)
– exchange differences	(8)	(122)	—	(17)	—	—	(2)
Purchases	846	1,097	—	1	—	—	15
New issuances	—	—	—	—	756	—	—
Sales	(1,131)	(1,491)	—	(6)	(6)	—	(9)
Settlements	(224)	(222)	—	(3)	(416)	—	(244)
Transfers out	(51)	(106)	—	(649)	(129)	—	(847)
Transfers in	17	620	—	232	—	—	180
At 31 Dec 2017	1,072	2,359	—	1,808	732	—	1,607
Unrealised gains/(losses) recognised in profit or loss relating to assets and liabilities held at 31 Dec 2017	—	22	—	(38)	130	—	177
– trading income/(expense) excluding net	—	22	—	(38)	130	—	177

1 *The bank had no level 3 assets or liabilities designated at fair value in 2017.*
2 *Included in 'Available-for-sale investments: fair value gains/(losses)' and 'Exchange differences' in the consolidated statement of comprehensive income.*

Effect of changes in significant unobservable assumptions to reasonably possible alternatives

Sensitivity of Level 3 fair values to reasonably possible alternative assumptions

	2018				2017			
	Reflected in profit or loss		Reflected in OCI		Reflected in profit or loss		Reflected in OCI	
	Favourable changes	Un-favourable changes	Favourable changes	Un-favourable changes	Favourable changes	Un-favourable changes	Favourable changes	Un-favourable changes
The group	£m	£m	£m	£m	£m	£m	£m	£m
Derivatives, trading assets and trading liabilities[1]	**155**	**(147)**	**—**	**—**	150	(141)	—	—
Designated and otherwise mandatorily measured at fair value through profit or loss	**177**	**(124)**	**3**	**(1)**	3	(3)	—	—
Financial investments	**7**	**(9)**	**17**	**(17)**	53	(77)	2	(2)
At 31 Dec	**339**	**(280)**	**20**	**(18)**	206	(221)	2	(2)
The bank								
Derivatives, trading assets and trading liabilities[1]	**136**	**(127)**	**—**	**—**	136	(127)	—	—
Designated and otherwise mandatorily measured at fair value through profit or loss	**53**	**(51)**	**—**	**—**	—	—	—	—
Financial investments	**6**	**(6)**	**—**	**—**	43	(40)	—	—
At 31 Dec	**195**	**(184)**	**—**	**—**	179	(167)	—	—

1 *Derivatives, trading assets and trading liabilities are presented as one category to reflect the manner in which these instruments are risk managed.*

Sensitivity of Level 3 fair values to reasonably possible alternative assumptions by instrument type

	2018				2017			
	Reflected in profit or loss		Reflected in OCI		Reflected in profit or loss		Reflected in OCI	
	Favourable changes	Un-favourable changes	Favourable changes	Un-favourable changes	Favourable changes	Un-favourable changes	Favourable changes	Un-favourable changes
	£m	£m	£m	£m	£m	£m	£m	£m
Private equity including strategic investments	**173**	**(119)**	**—**	**—**	55	(53)	2	(2)
Asset-backed securities	**38**	**(18)**	**20**	**(18)**	34	(40)	—	—
Structured notes	**10**	**(10)**	**—**	**—**	6	(6)	—	—
Derivatives	**74**	**(74)**	**—**	**—**	82	(84)	—	—
Other derivatives	**—**	**—**	**—**	**—**	—	—	—	—
Other portfolios	**44**	**(59)**	**—**	**—**	29	(38)	—	—
At 31 Dec	**339**	**(280)**	**20**	**(18)**	206	(221)	2	(2)

The sensitivity analysis aims to measure a range of fair values consistent with the application of a 95% confidence interval. Methodologies take account of the nature of the valuation technique employed, as well as the availability and reliability of observable proxy and historical data.

When the fair value of a financial instrument is affected by more than one unobservable assumption, the above table reflects the most favourable or the most unfavourable change from varying the assumptions individually.

Key unobservable inputs to Level 3 financial instruments

Quantitative information about significant unobservable inputs in Level 3 valuations

	Fair value				2018				2017			
	Assets	Liabilities	Valuation techniques	Key unobservable inputs	Full range of inputs		Core range of inputs[1]		Full range of inputs		Core range of inputs[1]	
	£m	£m			Lower	Higher	Lower	Higher	Lower	Higher	Lower	Higher
Private equity including strategic investments	1,745	10	See page 123	See page 123	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Asset-backed securities	1,477	–										
– CLO/CDO[2]	146	–	Market proxy	Bid quotes	–	100	88	100	–	101	13	57
– Other ABSs	1,331	–	Market proxy	Bid quotes	–	100	68	99	–	103	35	99
Structured notes	2	1,026										
– equity-linked notes	–	929	Model-Option model	Equity volatility	8%	79%	13%	43%	7%	57%	11%	24%
	–	–	Model-Option model	Equity correlation	31%	88%	40%	77%	34%	91%	41%	60%
– fund-linked notes	–	65	Model-Option model	Fund volatility	7%	21%	7%	21%	6%	15%	6%	15%
– FX-linked notes	–	19	Model-Option model	FX volatility	8%	27%	8%	25%	4%	20%	5%	17%
– other	2	13										
Derivatives	2,080	1,463										
Interest rate derivatives:	1,172	694										
– securitisation swaps	183	548	Model-Discounted cash flow	Prepayment rate	6%	7%	6%	7%	20%	90%	20%	90%
– long-dated swaptions	796	22	Model-Option model	IR volatility	13%	39%	18%	31%	8%	41%	16%	34%
– other	193	124										
FX derivatives:	342	379										
– FX options	342	379	Model-Option model	FX Volatility	3%	27%	6%	18%	1%	26%	6%	15%
Equity derivatives:	545	343										
– long-dated single stock options	121	157	Model-Option model	Equity volatility	5%	83%	13%	46%	8%	49%	12%	36%
– other	424	186										
Credit derivatives:	21	47										
– other	21	47										
Other portfolios	3,199	–										
– structured certificates	949	–	Model-Discounted cash flow	Credit volatility	2%	4%	2%	4%	2%	4%	2%	4%
– other	2,250	–										
At 31 Dec	8,503	2,499										

1 *The core range of inputs is the estimated range within which 90% of the inputs fall.*
2 *Collateralised loan obligation/collateralised debt obligation.*

Private equity including strategic investments

Given the bespoke nature of the analysis in respect of each holding, it is not practical to quote a range of key unobservable inputs.

Prepayment rates

Prepayment rates are a measure of the anticipated future speed at which a loan portfolio will be repaid in advance of the due date. They vary according to the nature of the loan portfolio and expectations of future market conditions, and may be estimated using a variety of evidence, such as prepayment rates implied from proxy observable security prices, current or historical prepayment rates and macroeconomic modelling.

Market proxy

Market proxy pricing may be used for an instrument when specific market pricing is not available, but there is evidence from instruments with common characteristics. In some cases, it might be possible to identify a specific proxy, but more generally evidence across a wider range of instruments will be used to understand the factors that influence current market pricing and the manner of that influence.

Volatility

Volatility is a measure of the anticipated future variability of a market price. It varies by underlying reference market price, and by strike and maturity of the option.

Certain volatilities, typically those of a longer-dated nature, are unobservable and estimated from observable data. The range of unobservable volatilities reflects the wide variation in volatility inputs by reference market price. The core range is significantly narrower than the full range because these examples with extreme volatilities occur relatively rarely within the HSBC portfolio.

Correlation

Correlation is a measure of the inter-relationship between two market prices, and is expressed as a number between minus one and one. It is used to value more complex instruments where the payout is dependent upon more than one market price. There is a wide range of instruments for which correlation is an input, and consequently a wide range of both same-asset correlations and cross-asset correlations is used. In general, the range of same-asset correlations will be narrower than the range of cross-asset correlations.

Unobservable correlations may be estimated based upon a range of evidence, including consensus pricing services, HSBC trade prices, proxy correlations and examination of historical price relationships. The range of unobservable correlations quoted in the table reflects the wide variation in correlation inputs by market price pair.

Credit spread

Credit spread is the premium over a benchmark interest rate required by the market to accept lower credit quality. In a discounted cash flow model, the credit spread increases the discount factors applied to future cash flows, thereby reducing the value of an asset. Credit spreads may be implied from market prices and may not be observable in more illiquid markets.

Inter-relationships between key unobservable inputs

Key unobservable inputs to Level 3 financial instruments may not be independent of each other. As described above, market variables may be correlated. This correlation typically reflects the manner in which different markets tend to react to macroeconomic or other events. Furthermore, the effect of changing market variables on the HSBC portfolio will depend on HSBC's net risk position in respect of each variable.

12 Fair values of financial instruments not carried at fair value

Fair values of financial instruments not carried at fair value and bases of valuation

		Fair value			
	Carrying amount	Quoted market price Level 1	Observable inputs Level 2	Significant unobservable inputs Level 3	Total
The group	**£m**	**£m**	**£m**	**£m**	**£m**
At 31 Dec 2018					
Assets					
Loans and advances to banks	**13,628**	**–**	**11,970**	**1,662**	**13,632**
Loans and advances to customers	**111,964**	**–**	**3**	**112,662**	**112,665**
Reverse repurchase agreements – non-trading	**80,102**	**–**	**80,102**	**–**	**80,102**
Financial investments – at amortised cost	**13**	**–**	**8**	**5**	**13**
Liabilities					
Deposits by banks	**24,532**	**–**	**24,514**	**–**	**24,514**
Customer accounts	**180,836**	**–**	**180,719**	**119**	**180,838**
Repurchase agreements – non-trading	**46,583**	**–**	**46,582**	**–**	**46,582**
Debt securities in issue	**22,721**	**–**	**22,721**	**–**	**22,721**
Subordinated liabilities	**13,770**	**–**	**13,999**	**–**	**13,999**
At 31 Dec 2017					
Assets					
Loans and advances to banks	14,149	–	13,302	847	14,149
Loans and advances to customers	280,402	–	1,245	280,518	281,763
Reverse repurchase agreements – non-trading	45,808	–	45,808	–	45,808
Liabilities					
Deposits by banks	29,349	–	29,328	–	29,328
Customer accounts	381,546	–	380,646	897	381,543
Repurchase agreements – non-trading	37,775	–	37,775	–	37,775
Debt securities in issue	13,286	–	13,296	–	13,296
Subordinated liabilities	16,494	–	16,982	–	16,982

Fair values of financial instruments not carried at fair value and bases of valuation (continued)

		Fair value			
	Carrying amount	Quoted market price Level 1	Observable inputs Level 2	Significant unobservable inputs Level 3	Total
The bank	**£m**	**£m**	**£m**	**£m**	**£m**
At 31 Dec 2018					
Assets					
Loans and advances to banks	**12,686**	**–**	**11,556**	**1,130**	**12,686**
Loans and advances to customers	**58,783**	**–**	**5**	**59,425**	**59,430**
Reverse repurchase agreements – non-trading	**56,495**	**–**	**56,494**	**–**	**56,494**
Financial investments – at amortised cost	**–**	**–**	**–**	**–**	**–**
Liabilities					
Deposits by banks	**18,148**	**–**	**18,147**	**–**	**18,147**
Customer accounts	**125,871**	**–**	**125,871**	**–**	**125,871**
Repurchase agreements – non-trading	**35,693**	**–**	**35,693**	**–**	**35,693**
Debt securities in issue	**19,085**	**–**	**19,085**	**–**	**19,085**
Subordinated liabilities	**13,323**	**–**	**13,535**	**–**	**13,535**
At 31 Dec 2017					
Assets					
Loans and advances to banks	15,160	–	15,122	38	15,160
Loans and advances to customers	220,450	–	1,125	220,420	221,545
Reverse repurchase agreements – non-trading	36,627	–	36,627	–	36,627
Liabilities					
Deposits by banks	24,626	–	24,626	–	24,626
Customer accounts	320,026	–	320,026	–	320,026
Repurchase agreements – non-trading	35,220	–	35,220	–	35,220
Debt securities in issue	6,108	–	6,108	–	6,108
Subordinated liabilities	15,930	–	16,392	–	16,392

Other financial instruments not carried at fair value are typically short-term in nature and reprice to current market rates frequently. Accordingly, their carrying amount is a reasonable approximation of fair value. They include cash and balances at central banks and items in the course of collection from and transmission to other banks, all of which are measured at amortised cost.

Valuation

Fair value is an estimate of the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It does not reflect the economic benefits and costs that HSBC expects to flow from an instrument's cash flow over its expected future life. Our valuation methodologies and assumptions in determining fair values for which no observable market prices are available may differ from those of other companies.

Loans and advances to banks and customers

To determine the fair value of loans and advances to banks and customers, loans are segregated, as far as possible, into portfolios of similar characteristics. Fair values are based on observable market transactions, when available. When they are unavailable, fair values are estimated using valuation models incorporating a range of input assumptions. These assumptions may include: value estimates from third-party brokers reflecting over-the-counter trading activity; forward-looking discounted cash flow models, taking account of expected customer prepayment rates, using assumptions that HSBC believes are consistent with those that would be used by market participants in valuing such loans; new business rates estimates for similar loans; and trading inputs from other market participants including observed primary and secondary trades. From time to time, we may engage a third-party valuation specialist to measure the fair value of a pool of loans.

The fair value of loans reflects expected credit losses at the balance sheet date and estimates of market participants' expectations of credit losses over the life of the loans, and the fair value effect of repricing between origination and the balance sheet date. For credit impaired loans, fair value is estimated by discounting the future cash flows over the time period they are expected to be recovered.

Financial investments

The fair values of listed financial investments are determined using bid market prices. The fair values of unlisted financial investments are determined using valuation techniques that incorporate the prices and future earnings streams of equivalent quoted securities.

Deposits by banks and customer accounts

The fair values of on-demand deposits are approximated by their carrying value. For deposits with longer-term maturities, fair values are estimated using discounted cash flows, applying current rates offered for deposits of similar remaining maturities.

Debt securities in issue and subordinated liabilities

Fair values are determined using quoted market prices at the balance sheet date where available, or by reference to quoted market prices for similar instruments.

Repurchase and reverse repurchase agreements – non-trading

Fair values approximate carrying amounts as balances are generally short dated.

13 Financial assets designated and otherwise mandatorily measured at fair value through profit or loss

	2018			2017		
	Designated at fair value	**Mandatorily measured at fair value**	**Total**	Designated at fair value	Mandatorily measured at fair value	Total
	£m	**£m**	**£m**	£m	£m	£m
Securities	**—**	**12,515**	**12,515**	9,260	N/A	9,260
– debt securities	**—**	**2,992**	**2,992**	1,034	N/A	1,034
– equity securities	**—**	**9,523**	**9,523**	8,226	N/A	8,226
Loans and advances to banks and customers	**—**	**5,141**	**5,141**	6	N/A	6
Other	**—**	**143**	**143**	—	N/A	—
At 31 Dec	**—**	**17,799**	**17,799**	9,266	N/A	9,266

14 Derivatives

Notional contract amounts and fair values of derivatives by product contract type

	Notional contract amount		Fair value – Assets			Fair value – Liabilities		
	Trading	**Hedging**	**Trading**	**Hedging**	**Total**	**Trading**	**Hedging**	**Total**
The group	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Foreign exchange	**4,341,381**	**4,227**	**50,881**	**109**	**50,990**	**(48,088)**	**(155)**	**(48,243)**
Interest rate	**13,252,292**	**38,617**	**107,028**	**497**	**107,525**	**(104,490)**	**(812)**	**(105,302)**
Equities	**984,963**	**—**	**9,131**	**—**	**9,131**	**(9,181)**	**—**	**(9,181)**
Credit	**304,263**	**—**	**2,893**	**—**	**2,893**	**(3,190)**	**—**	**(3,190)**
Commodity and other	**47,470**	**—**	**675**	**—**	**675**	**(708)**	**—**	**(708)**
Offset (Note 28)					**(26,692)**			**26,692**
At 31 Dec 2018	**18,930,369**	**42,844**	**170,608**	**606**	**144,522**	**(165,657)**	**(967)**	**(139,932)**
Foreign exchange	3,172,038	2,334	41,100	39	41,139	(38,709)	(135)	(38,844)
Interest rate	9,973,858	60,496	156,780	571	157,351	(152,079)	(1,390)	(153,469)
Equities	448,156	—	7,393	—	7,393	(9,795)	—	(9,795)
Credit	306,855	—	3,566	—	3,566	(4,087)	—	(4,087)
Commodity and other	38,939	—	622	—	622	(611)	—	(611)
Offset (Note 28)					(66,736)			66,736
At 31 Dec 2017	13,939,846	62,830	209,461	610	143,335	(205,281)	(1,525)	(140,070)

The notional contract amounts of derivatives held for trading purposes and derivatives designated in hedge accounting relationships indicate the nominal value of transactions outstanding at the balance sheet date; they do not represent amounts at risk.

Derivative assets and liabilities decreased during 2018, driven by the adoption of Settled to Market accounting for cleared derivatives, yield curve movements and changes in foreign exchange rates.

	Notional contract amount		Fair value – Assets			Fair value – Liabilities		
	Trading	**Hedging**	**Trading**	**Hedging**	**Total**	**Trading**	**Hedging**	**Total**
The bank	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Foreign exchange	**4,338,438**	**4,215**	**50,638**	**109**	**50,747**	**(47,976)**	**(155)**	**(48,131)**
Interest rate	**11,462,267**	**25,685**	**90,831**	**494**	**91,325**	**(88,976)**	**(670)**	**(89,646)**
Equities	**979,037**	**—**	**8,976**	**—**	**8,976**	**(9,031)**	**—**	**(9,031)**
Credit	**304,093**	**—**	**2,901**	**—**	**2,901**	**(3,185)**	**—**	**(3,185)**
Commodity and other	**47,463**	**—**	**675**	**—**	**675**	**(709)**	**—**	**(709)**
Offset					**(15,395)**			**15,395**
At 31 Dec 2018	**17,131,298**	**29,900**	**154,021**	**603**	**139,229**	**(149,877)**	**(825)**	**(135,307)**
Foreign exchange	3,202,826	1,153	40,818	29	40,847	(38,603)	(108)	(38,711)
Interest rate	8,627,923	51,387	137,241	552	137,793	(133,750)	(1,142)	(134,892)
Equities	437,029	—	7,367	—	7,367	(9,690)	—	(9,690)
Credit	306,633	—	3,569	—	3,569	(4,088)	—	(4,088)
Commodity and other	39,389	—	620	—	620	(614)	—	(614)
Offset					(54,960)			54,960
At 31 Dec 2017	12,613,800	52,540	189,615	581	135,236	(186,745)	(1,250)	(133,035)

Use of derivatives

We undertake derivatives activity for three primary purposes: to create risk management solutions for clients, to manage the portfolio risks arising from client business, and to manage and hedge our own risks.

Trading derivatives

Most of the group's derivative transactions relate to sales and trading activities. Sales activities include the structuring and marketing of derivative products to customers to enable them to take, transfer, modify or reduce current or expected risks. Trading activities include market-making and risk management. Market-making entails quoting bid and offer prices to other market participants for the purpose of

generating revenues based on spread and volume. Risk management activity is undertaken to manage the risk arising from client transactions, with the principal purpose of retaining client margin. Other derivatives classified as held for trading include non-qualifying hedging derivatives.

Substantially all of the group's derivatives entered into with subsidiaries are managed in conjunction with financial liabilities designated at fair value.

Derivatives valued using models with unobservable inputs

The difference between the fair value at initial recognition (the transaction price) and the value that would have been derived had the valuation techniques used for subsequent measurement been applied at initial recognition, less subsequent releases, is in the following table:

Unamortised balance of derivatives valued using models with significant unobservable inputs

	The group		The bank	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Unamortised balance at 1 Jan	**72**	72	**69**	69
Deferral on new transactions	**88**	126	**88**	126
Recognised in the income statement during the year:	**(87)**	(123)	**(87)**	(123)
– amortisation	**(59)**	(60)	**(59)**	(60)
– maturity, termination or offsetting derivative	**(28)**	(63)	**(28)**	(63)
Exchange differences and other	**(15)**	(3)	**(15)**	(3)
Unamortised balance at 31 Dec[1]	**58**	72	**55**	69

1 *This amount is yet to be recognised in the consolidated income statement.*

Hedge accounting derivatives

The group applies hedge accounting to manage the following risks: interest rate and foreign exchange. The Report of the Directors–Risk presents more details on how these risks arise and how they are managed by the group.

Fair value hedges

The group enters into fixed-for-floating-interest-rate swaps to manage the exposure to changes in fair value due to movements in market interest rates on certain fixed rate financial instruments which are not measured at fair value through profit or loss, including debt securities held and issued.

Hedging instrument by hedged risk

	Hedging instrument				
		Carrying amount			
The group	**Notional amount[1]**	**Assets**	**Liabilities**	**Balance sheet presentation**	**Change in fair value[2]**
Hedged risk	**£m**	**£m**	**£m**		**£m**
Interest rate[3]	**29,142**	**433**	**(787)**	**Derivatives**	**161**
At 31 Dec 2018	**29,142**	**433**	**(787)**		**161**

1 *The notional contract amounts of derivatives designated in qualifying hedge accounting relationships indicate the nominal value of transactions outstanding at the balance sheet date; they do not represent amounts at risk.*
2 *Used in effectiveness testing; comprising the full fair value change of the hedging instrument not excluding any component.*
3 *The hedged risk 'interest rate' includes inflation risk.*

Hedged item by hedged risk

	Hedged item						Ineffectiveness	
	Carrying amount		Accumulated fair value hedge adjustments included in carrying amount[2]					
The group	**Assets**	**Liabilities**	**Assets**	**Liabilities**	**Balance sheet presentation**	**Change in fair value[1]**	**Recognised in profit and loss**	**Profit and loss presentation**
Hedged risk	**£m**	**£m**	**£m**	**£m**		**£m**	**£m**	
Interest rate[3]	**16,242**		**55**		**Financial assets at fair value through other comprehensive**	**(132)**	**(12)**	**Net income from financial instruments held for trading or managed on a fair value basis**
	997		**(3)**		**Loans and advances to customers**	**(3)**		
		570		**97**	**Debt securities in issue**	**(16)**		
		10,048		**35**	**Deposits by banks[4]**	**(23)**		
At 31 Dec 2018	**17,239**	**10,618**	**52**	**132**		**(174)**	**(12)**	

1 *Used in effectiveness assessment; comprising amount attributable to the designated hedged risk that can be a risk component.*
2 *The accumulated amounts of fair value adjustments remaining in the statement of financial position for hedged items that have ceased to be adjusted for hedging gains and losses were £(58)m for 'Financial assets at fair value through other comprehensive income' and £34m for 'Debt securities in issue'.*
3 *The hedged risk 'interest rate' includes inflation risk.*
4 *The notional amount of non-dynamic fair value hedges was £9,953m, of which the weighted-average maturity is February 2023 and the weighted average swap rate is 0.45%. £6,276m of these hedges are internal to HSBC Group and composed by internal funding between HSBC Holdings and the group.*

Hedging instrument by hedged risk

The bank	Hedging instrument				
		Carrying amount			
	Notional amount[1]	Assets	Liabilities	Balance sheet presentation	Change in fair value[2]
Hedged risk	£m	£m	£m	£m	£m
Interest rate[3]	20,438	481	(656)	Derivatives	94
At 31 Dec 2018	**20,438**	**481**	**(656)**		**94**

1 The notional contract amounts of derivatives designated in qualifying hedge accounting relationships indicate the nominal value of transactions outstanding at the balance sheet date; they do not represent amounts at risk.
2 Used in effectiveness testing; comprising the full fair value change of the hedging instrument not excluding any component.
3 The hedged risk 'interest rate' includes inflation risk.

Hedged item by hedged risk

The bank	Hedged item						Ineffectiveness	
	Carrying amount		Accumulated fair value hedge adjustments included in carrying amount[2]					
	Assets	Liabilities	Assets	Liabilities	Balance sheet presentation	Change in fair value[1]	Recognised in profit and loss	Profit and loss presentation
Hedged risk	£m	£m	£m	£m		£m	£m	
Interest rate[3]	12,490		55		Financial assets at fair value through other comprehensive income	(77)	(12)	Net income from financial instruments held for trading or managed on a fair value basis
	73		(3)		Loans and advances to customers	(2)		
		570		97	Debt securities in issue	(16)		
		6,305		—	Deposits by banks[4]	(11)		
At 31 Dec 2018	**12,563**	**6,875**	**52**	**97**		**(106)**	**(12)**	

1 Used in effectiveness assessment; comprising amount attributable to the designated hedged risk that can be a risk component.
2 The accumulated amounts of fair value adjustments remaining in the statement of financial position for hedged items that have ceased to be adjusted for hedging gains and losses were £(58)m for 'Financial assets at fair value through other comprehensive income' and £34m for 'Debt securities in issue'.
3 The hedged risk 'interest rate' includes inflation risk.
4 The notional amount of non-dynamic fair value hedges was £6,276m, of which the weighted-average maturity is August 2024 and the weighted average swap rate is 0.87%. Those hedges are internal to HSBC Group and composed by internal funding between HSBC Holdings and the group.

Sources of hedge ineffectiveness may arise from basis risk including, but not limited to the discount rates used for calculating the fair value of derivatives, hedges using instruments with a non-zero fair value and notional, and timing differences between the hedged items and hedging instruments.

For some debt securities held, the group manages interest rate risk in a dynamic risk management strategy. The assets in scope of this strategy are high quality fixed-rate debt securities, which may be sold to meet liquidity and funding requirements.

The interest rate risk of the group's fixed rate debt securities issued is managed in a non-dynamic risk management strategy.

Cash flow hedges

The group's cash flow hedging instruments consist principally of interest rate swaps and cross-currency swaps that are used to manage the variability in future interest cash flows of non-trading financial assets and liabilities, arising due to changes in market interest rates and foreign-currency basis.

The group applies macro cash flow hedging for interest-rate risk exposures on portfolios of replenishing current and forecasted issuances of non-trading assets and liabilities that bear interest at variable rates, including rolling such instruments. The amounts and timing of future cash flows, representing both principal and interest flows, are projected for each portfolio of financial assets and liabilities on the basis of their contractual terms and other relevant factors, including estimates of prepayments and defaults. The aggregate cash flows representing both principal balances and interest cash flows across all portfolios are used to determine the effectiveness and ineffectiveness. Macro cash flow hedges are considered to be dynamic hedges.

The group also hedges the variability in future cash-flows on foreign-denominated financial assets and liabilities arising due to changes in foreign exchange market rates with cross-currency swaps; these are considered dynamic hedges.

Hedging instrument by hedged risk

	Hedging instrument					Hedged item	Ineffectiveness	
		Carrying amount						
	Notional amount[1]	Assets	Liabilities	Balance sheet presentation	Change in fair value[2]	Change in fair value[3]	Recognised in profit and loss	Profit and loss presentation
Hedged risk	£m	£m	£m		£m	£m	£m	
Foreign exchange	**4,215**	**109**	**(155)**	**Derivatives**	**(121)**	**(121)**	**–**	**Net income from financial instruments held for trading or managed on a fair value basis**
Interest rate	**9,475**	**64**	**(25)**		**(44)**	**(38)**	**(6)**	
At 31 Dec 2018	**13,690**	**173**	**(180)**		**(165)**	**(159)**	**(6)**	

1 The notional contract amounts of derivatives designated in qualifying hedge accounting relationships indicate the nominal value of transactions outstanding at the balance sheet date; they do not represent amounts at risk.
2 Used in effectiveness testing; comprising the full fair value change of the hedging instrument not excluding any component.
3 Used in effectiveness assessment; comprising amount attributable to the designated hedged risk that can be a risk component.

Sources of hedge ineffectiveness may arise from basis risk including, but not limited to timing differences between the hedged items and hedging instruments, and hedges using instruments with a non-zero fair value.

Reconciliation of equity and analysis of other comprehensive income by risk type

	Interest rate	Foreign exchange
	£m	£m
Cash flow hedging reserve at 1 Jan 2018	**(42)**	**4**
Fair value losses	**(38)**	**(121)**
Fair value losses reclassified from cash flow hedge reserve to income statement in respect of:		
– hedged items that have affected profit or loss	**44**	**113**
Income taxes	**(14)**	**–**
Transfer to HSBC UK Bank plc and its subsidiaries	**26**	**3**
Cash flow hedging reserve at 31 Dec 2018	**(24)**	**(1)**

15 Financial investments

Carrying amount of financial investments

	The group		The bank	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Financial investments measured at fair value through other comprehensive income	**47,259**	N/A	**26,699**	N/A
– treasury and other eligible bills	**3,123**	N/A	**2,135**	N/A
– debt securities	**43,973**	N/A	**24,511**	N/A
– equity securities	**87**	N/A	**53**	N/A
– other instruments[1]	**76**	N/A	**–**	N/A
Debt instruments measured at amortised cost	**13**	N/A	**–**	N/A
– treasury and other eligible bills	**8**	N/A	**–**	N/A
– debt securities	**5**	N/A	**–**	N/A
Available-for-sale securities at fair value	**N/A**	58,000	**N/A**	31,382
– treasury and other eligible bills	**N/A**	3,043	**N/A**	2,292
– debt securities	**N/A**	54,295	**N/A**	28,683
– equity securities	**N/A**	662	**N/A**	407
At 31 Dec[2]	**47,272**	58,000	**26,699**	31,382

1 'Other instruments' are comprised of loans and advances.
2 Categories of financial instruments are disclosed under IFRS 9 at 31 December 2018. These are not directly comparable with 31 December 2017, where the instruments were categorised in accordance with IAS 39.

For the group, £13m (2017: £7,241m), and for the bank, £nil (2017: £4,819m), of the debt securities issued by banks and other financial institutions are guaranteed by various governments.

Equity instruments measured at fair value through other comprehensive income

	Instruments held at year end	
	Fair value	Dividends recognised
Type of equity instruments	£m	£m
Business facilitation	**75**	**1**
Investments required by central institutions	**9**	**7**
Others	**3**	**–**
At 31 Dec 2018	**87**	**8**

Net gains/losses on equity instruments measured at fair value through other comprehensive income during 2018 amounted to £1m.

16 Assets pledged, collateral received and assets transferred

Assets pledged

Financial assets pledged as collateral

	The group		The bank	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Treasury bills and other eligible securities	**1,317**	745	**—**	—
Loans and advances to banks	**29**	7,084	**—**	4,914
Loans and advances to customers	**22,148**	32,528	**—**	9,863
Debt securities	**37,250**	48,247	**26,555**	30,322
Equity securities	**18,644**	24,562	**18,561**	24,473
Other[1]	**21,810**	226	**18,530**	39
Assets pledged at 31 Dec	**101,198**	113,392	**63,646**	69,611

1 *Settlement accounts, cash collateral and margin receivables included within 'Loans and advances to banks' and 'Loans and advances to customers' were reclassified from 'Trading assets' to 'Other assets' on 1 January 2018. Comparative data has not been restated.*

Financial assets pledged as collateral which the counterparty has the right to sell or repledge

	The group		The bank	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Trading assets	**43,505**	41,593	**36,945**	32,036
Financial investments	**1,637**	7,198	**236**	2,833
At 31 Dec	**45,142**	48,791	**37,181**	34,869

Assets pledged as collateral include all assets categorised as encumbered in the disclosure on page 63.

The amount of assets pledged to secure liabilities may be greater than the book value of assets utilised as collateral. For example, in the case of securitisations and covered bonds, the amount of liabilities issued, plus mandatory over-collateralisation, is less than the book value of the pool of assets available for use as collateral. This is also the case where assets are placed with a custodian or a settlement agent that has a floating charge over all the assets placed to secure any liabilities under settlement accounts.

These transactions are conducted under terms that are usual and customary to collateralised transactions including, where relevant, standard securities lending and borrowing, repurchase agreements and derivative margining. The group places both cash and non-cash collateral in relation to derivative transactions.

Collateral received

The fair value of assets accepted as collateral, relating primarily to standard securities lending, reverse repurchase agreements and derivative margining, that the group is permitted to sell or repledge in the absence of default was £250,277m (2017: £173,386m) (the bank: 2018: £201,548m; 2017: £136,570m). The fair value of any such collateral sold or repledged was £202,782m (2017: £130,430m) (the bank: 2018: £152,454m; 2017: £98,215m). The group is obliged to return equivalent securities. These transactions are conducted under terms that are usual and customary to standard securities lending, reverse repurchase agreements and derivative margining.

Assets transferred

The assets pledged include transfers to third parties that do not qualify for derecognition, notably secured borrowings such as debt securities held by counterparties as collateral under repurchase agreements and equity securities lent under securities lending agreements, as well as swaps of equity and debt securities. For secured borrowings, the transferred asset collateral continues to be recognised in full and a related liability, reflecting the group's obligation to repurchase the assets for a fixed price at a future date is also recognised on the balance sheet. Where securities are swapped, the transferred asset continues to be recognised in full. There is no associated liability as the non-cash collateral received is not recognised on the balance sheet. The group is unable to use, sell or pledge the transferred assets for the duration of these transactions, and remains exposed to interest rate risk and credit risk on these pledged assets. The counterparty's recourse is not limited to the transferred assets.

Transferred financial assets not qualifying for full derecognition and associated financial liabilities

	Carrying amount of:		**Fair value of:**		
	Transferred assets	**Associated liabilities**	**Transferred assets**	**Associated liabilities**	**Net position**
The group	**£m**	**£m**	**£m**	**£m**	**£m**
At 31 Dec 2018					
Repurchase agreements	**19,375**	**19,396**	**—**	**—**	**—**
Securities lending agreements	**25,765**	**2,865**	**—**	**—**	**—**
At 31 Dec 2017					
Repurchase agreements	24,323	23,004	—	—	—
Securities lending agreements	24,562	2,385	—	—	—

Transferred financial assets not qualifying for full derecognition and associated financial liabilities (continued)

	Carrying amount of:		Fair value of:		
	Transferred assets	Associated liabilities	Transferred assets	Associated liabilities	Net position
The bank	**£m**	**£m**	**£m**	**£m**	**£m**
At 31 Dec 2018					
Repurchase agreements	**8,976**	**8,976**	**–**	**–**	**–**
Securities lending agreements	**28,205**	**2,794**	**–**	**–**	**–**
At 31 Dec 2017					
Repurchase agreements	10,401	8,979	–	–	–
Securities lending agreements	24,473	2,338	–	–	–

17 Interests in associates

Principal associates of the group and the bank

Business Growth Fund Group PLC ('BGF') is a principal associate of the group. BGF is an independent company, established in 2011 to provide investment to growing small and medium sized British businesses. BGF is backed by five of the UK's main banking groups: Barclays, HSBC, Lloyds, RBS and Standard Chartered. At 31 December 2018, the group had a 24.5% interest in the equity capital of BGF.

Interests in joint ventures

On the 1 July 2018, the group transferred its shareholding in Vaultex through the court approved ring-fencing transfer scheme as provided for in Part VII of the FSMA to HSBC UK.

A list of all associates is set out on page 164.

18 Investments in subsidiaries

Principal subsidiary undertakings of HSBC Bank plc

	At 31 Dec 2018		
	Country of incorporation or registration	HSBC Bank plc's interest in equity capital	Share class
		%	
HSBC Investment Bank Holdings Limited	**England and Wales**	**100.00**	**Ordinary £1**
HSBC Asset Finance (UK) Limited	**England and Wales**	**100.00**	**Ordinary £1**
HSBC Life (UK) Limited	**England and Wales**	**100.00**	**Ordinary £1**
HSBC France	**France**	**99.99**	**€5 Actions**
HSBC Trinkaus & Burkhardt AG	**Germany**	**80.67**	**Stückaktien**
HSBC Bank Malta p.l.c	**Malta**	**70.03**	**Ordinary €0.30**

All the above prepare their financial statements up to 31 December.

Transfer of the ring-fenced bank entities

On 1 July 2018, the bank transferred its shareholding in a number of entities, most notably HSBC Equipment Finance (UK) Limited, HSBC Invoice Finance (UK) Limited, HSBC Private Bank (UK) Limited, HSBC Trust Company (UK) Limited and Marks and Spencer Financial Services plc. These transfers were made through the court approved ring-fencing transfer scheme as provided for in Part VII of the Financial Services and Markets Act 2000 ('FSMA'). The group transferred £211.9bn of total assets, including goodwill and £212.0bn of total liabilities, resulting in a £9.9bn reduction in the group's equity. The bank transferred £212.0bn of total assets and £204.6bn of total liabilities, resulting in a £7.4bn reduction in the bank's equity. From that date the results of these entities are excluded from the group's results. For further information refer to Note 35 'Discontinued operations'.

Details of all group subsidiaries, as required under Section 409 of the Companies Act 2006, are set out in Note 37. The principal countries of operation are the same as the countries of incorporation.

Impairment testing of investments in subsidiaries

At each reporting period end, HSBC Bank plc reviews investments in subsidiaries for indicators of impairment. An impairment is recognised when the carrying amount exceeds the recoverable amount for that investment.

The recoverable amount is the higher of the investment's fair value less costs of disposal and its value in use. The value in use is calculated by discounting management's cash flow projections for the investment.

- The cash flow projections for each investment are based on the latest approved plans and a long-term growth rate is used to extrapolate the cash flows in perpetuity.
- The growth rate reflects GDP and inflation for the country within which the investment operates and is based on the long-term average growth rates.
- The rate used to discount the cash flows is based on the cost of capital assigned to each investment, which is derived using a capital asset pricing model ('CAPM'). CAPM depends on a number of inputs reflecting financial and economic variables, including the risk-free rate and a premium to reflect the inherent risk of the business being evaluated. These variables are based on the market's assessment of the economic variables and management's judgement. The discount rates for each investment are refined to reflect the rates of inflation for the countries within which the investment operates. In addition, for the purposes of testing investments for impairment, management supplements this process by comparing the discount rates derived using the internally generated CAPM, with cost of capital rates produced by external sources for businesses operating in similar markets.

No impairment was recognised in 2018. An impairment of £29m was recognised as a result of the impairment test performed in 2017, this related to an investment in HSBC Polska.

19 Structured entities

The group is mainly involved with both consolidated and unconsolidated structured entities through the securitisation of financial assets, conduits and investment funds, established either by the group or a third party.

Consolidated structured entities

Total assets of the group's consolidated structured entities, split by entity type

	Conduits	Securitisations	Group managed funds	Other	Total
	£m	£m	£m	£m	£m
At 31 Dec 2018	**7,218**	**232**	**3,378**	**2,912**	**13,740**
At 31 Dec 2017	9,551	330	3,210	3,500	16,591

Conduits

The group has established and manages two types of conduits: securities investment conduits ('SICs') and multi-seller conduits.

Securities investment conduits

The SICs purchase highly rated ABSs to facilitate tailored investment opportunities.

- At 31 December 2018, Solitaire, the group's principal SIC held £1.8bn of ABSs (2017: £2.4bn). These are included within the disclosures of ABSs on page 55. It is currently funded entirely by commercial paper ('CP') issued to the group. Although the group continues to provide a liquidity facility, Solitaire has no need to draw on it as long as the group purchases its issued CP, which the group intends to do for the foreseeable future. At 31 December 2018, the group held £2.7bn of CP (2017: £3.4bn).
- Mazarin's clean up redemption conditions were triggered in September 2018. The group's primary exposure to Mazarin is represented by the amortised cost of the debt required to support the non-cash assets of the vehicle. At 31 December 2018, this amounted to £0.3bn (2017: £0.7bn). First loss protection is provided through the capital notes issued by this vehicle, which are held substantially by third parties.
- Barion and Malachite's clean up redemption conditions were triggered in March and August 2018 respectively, resulting in the full redemption of these vehicles.

Multi-seller conduit

The group's multi-seller conduit was established to provide access to flexible market-based sources of finance for its clients. Currently, the group bears risk equal to transaction-specific facility offered to the multi-seller conduit, amounting to £9.7bn at 31 December 2018 (2017: £9.4bn). First loss protection is provided by the originator of the assets, and not by the group, through transaction-specific credit enhancements. A layer of secondary loss protection is provided by the group in the form of programme-wide enhancement facilities.

Securitisations

The group uses structured entities to securitise customer loans and advances it originates in order to diversify its sources of funding for asset origination and capital efficiency purposes. The loans and advances are transferred by the group to the structured entities for cash or synthetically through credit default swaps, and the structured entities issue debt securities to investors.

Group managed funds

The group has established a number of money market and non-money market funds. Where it is deemed to be acting as principal rather than agent in its role as investment manager, the group controls these funds.

Other

The group has entered into a number of transactions in the normal course of business, which include asset and structured finance transactions where it has control of the structured entity. In addition, the group is deemed to control a number of third-party managed funds through its involvement as a principal in the funds.

Unconsolidated structured entities

The term 'unconsolidated structured entities' refers to all structured entities not controlled by the group. The group enters into transactions with unconsolidated structured entities in the normal course of business to facilitate customer transactions and for specific investment opportunities.

Nature and risks associated with the group's interests in unconsolidated structured entities

	Securitisations	Group managed funds	Non-group managed funds	Other	Total
Total asset values of the entities (£m)					
0 – 400	**6**	**81**	**884**	**37**	**1,008**
400 – 1,500	**3**	**6**	**505**	**3**	**517**
1,500 – 4,000	**—**	**—**	**229**	**—**	**229**
4,000 – 20,000	**—**	**—**	**74**	**1**	**75**
20,000+	**—**	**—**	**5**	**—**	**5**
Number of entities at 31 Dec 2018	**9**	**87**	**1,697**	**41**	**1,834**
	£m	**£m**	**£m**	**£m**	**£m**
Total assets in relation to the group's interests in the unconsolidated structured entities	**1,160**	**2,038**	**4,788**	**1,788**	**9,774**
– trading assets	**—**	**1**	**281**	**1,051**	**1,333**
– financial assets designated and otherwise mandatorily measured at fair value	**—**	**2,032**	**3,944**	**—**	**5,976**
– loans and advances to customers	**1,160**	**—**	**211**	**536**	**1,907**
– financial investments	**—**	**5**	**352**	**201**	**558**
Total liabilities in relation to the group's interests in the unconsolidated structured entities	**—**	**8**	**—**	**—**	**8**
Other off-balance sheet commitments	**608**	**5**	**1,666**	**—**	**2,279**
The group's maximum exposure at 31 Dec 2018	**1,768**	**2,035**	**6,454**	**1,788**	**12,045**
Total asset values of the entities (£m)					
0 – 400	11	82	1,327	190	1,610
400 – 1,500	1	6	512	3	522
1,500 – 4,000	—	—	229	—	229
4,000 – 20,000	—	—	80	2	82
20,000+	—	—	4	—	4
Number of entities at 31 Dec 2017	12	88	2,152	195	2,447
	£m	£m	£m	£m	£m
Total assets in relation to the group's interests in the unconsolidated structured entities	1,016	1,286	4,286	2,033	8,621
– trading assets	—	—	126	1,895	2,021
– financial assets designated at fair value	—	1,277	3,843	—	5,120
– loans and advances to customers	1,016	—	—	23	1,039
– financial investments	—	9	317	115	441
Total liabilities in relation to group's interests in the unconsolidated structured entities	—	6	2	—	8
Other off-balance sheet commitments	—	—	33	—	33
The group's maximum exposure at 31 Dec 2017	1,016	1,280	4,317	2,033	8,646

The maximum exposure to loss from the group's interests in unconsolidated structured entities represents the maximum loss it could incur as a result of its involvement with these entities regardless of the probability of the loss being incurred.

- For commitments, guarantees and written credit default swaps, the maximum exposure to loss is the notional amount of potential future losses.
- For retained and purchased investments in and loans to unconsolidated structured entities, the maximum exposure to loss is the carrying value of these interests at the balance sheet reporting date.

The maximum exposure to loss is stated gross of the effects of hedging and collateral arrangements entered into to mitigate the group's exposure to loss.

Securitisations

The group has interests in unconsolidated securitisation vehicles through holding notes issued by these entities. In addition, the group has investments in ABSs issued by third-party structured entities, as set out on page 55.

Group managed funds

The group establishes and manages money market funds and non-money market investment funds to provide customers with investment opportunities. The group, as fund manager, may be entitled to receive management and performance fees based on the assets under management. The group may also retain units in these funds.

Non-group managed funds

The group purchases and holds units of third-party managed funds in order to facilitate business and meet customer needs.

Other

The group has established structured entities in the normal course of business, such as structured credit transactions for customers, to provide finance to public and private sector infrastructure projects, and for asset and structured finance transactions.

In addition to the interests disclosed above, the group enters into derivative contracts, reverse repos and stock borrowing transactions with structured entities. These interests arise in the normal course of business for the facilitation of third-party transactions and risk management solutions.

Group sponsored structured entities

The amount of assets transferred to and income received from such sponsored entities during 2018 and 2017 was not significant.

20 Goodwill and intangible assets

	The group		The bank	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Goodwill[1,2]	**1,323**	4,559	**84**	369
Present value of in-force long-term insurance business	**651**	572	**—**	—
Other intangible assets[2,3]	**652**	805	**416**	679
At 31 Dec	**2,626**	5,936	**500**	1,048

1 *Impacted by the transfers to HSBC UK Bank plc under the ring-fence implementation. For further information, see Note 35 'Discontinued operations'.*
2 *For 2018, the amortisation and impairment of intangible assets totalled £171m for the group (£nil for goodwill and £171m for other intangibles).*
3 *Included within the group's other intangible assets is internally generated software with a net carrying value of £572m (2017: £736m).*

Movement analysis of goodwill

	The group		The bank	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
At 1 Jan	**4,559**	4,487	**369**	356
Transfer to HSBC UK Bank plc and its subsidiaries	**(3,285)**	—	**(223)**	—
Exchange differences	**45**	149	**—**	(6)
Other	**4**	(77)	**(62)**	19
At 31 Dec	**1,323**	4,559	**84**	369

Impairment testing

The group's impairment test in respect of goodwill allocated to each cash-generating unit ('CGU') is performed at 1 July each year, with a review for indicators of impairment at 30 June and 31 December. At 31 December 2018, we reviewed the inputs used in our most recent impairment test in the light of current economic and market conditions. This review did not identify any indicators of impairment.

As a result, no impairment tests have been performed at 31 December 2018. The annual test performed at 1 July remains the latest impairment test and the disclosures given are at 1 July.

The testing at 1 July took into account the transfer of the ring-fenced bank activities to HSBC UK Bank plc. The carrying values of the CGUs at 1 July were established using risk-weighted assets ('RWAs') attributed to each of the group's CGU at 1 July, and compared to their recoverable amounts. The same RWAs were used to calculate the goodwill transferred to the ring-fenced bank at 1 July. The testing resulted in no impairment of goodwill, but did highlight that the Commercial Banking CGU had become sensitive.

Basis of the recoverable amount

The recoverable amount of all CGUs to which goodwill has been allocated was equal to its value in use ('VIU') at each respective testing date for 2017 and 2018.

For each CGU, the VIU is calculated by discounting management's cash flow projections for the CGU.

Key assumptions in VIU calculation

	Annual impairment test 2018			Annual impairment test 2017		
	Goodwill at 1 Jul 2018	**Discount rate**	**Nominal growth rate beyond initial cash flow projections**	Goodwill at 1 Jul 2017	Discount rate	Nominal growth rate beyond initial cash flow projections
Cash-generating unit	**£m**	**%**	**%**	£m	%	%
RBWM	**386**	**8.3**	**3.5**	2,062	8.9	3.7
CMB	**569**	**9.3**	**3.5**	1,798	9.9	3.7
GPB	**308**	**9.4**	**3.5**	665	9.7	3.6
Total	**1,263**			4,525		

Management's judgement in estimating the cash flows of a CGU: the cash flow projections for each CGU are based on the latest plans presented to the Board. For the goodwill impairment test conducted at 1 July 2018, management's cash flow for the group post ring-fencing projections until the end of 2022 were used.

Nominal long-term growth rate: the long-term growth rate is used to extrapolate the cash flows in perpetuity. The growth rate reflects GDP and inflation for the countries within which the CGU operates or derives revenue from. The rates are based on 20-year forecast growth rates, as they represent an objective estimate of likely future trends.

Discount rate: the rate used to discount the cash flows is based on the cost of capital assigned to each CGU, which is derived using a capital asset pricing model ('CAPM'). CAPM depends on a number of inputs reflecting financial and economic variables, including the risk-free rate and a premium to reflect the inherent risk of the business being evaluated. These variables are based on the market's assessment of the economic variables and management's judgement. The discount rates for each CGU are refined to reflect the rates of inflation for the countries within which the CGU operates. In addition, for the purposes of testing goodwill for impairment, management supplements this process by comparing the discount rates derived using the internally generated CAPM, with cost of capital rates produced by external sources for businesses operating in similar markets. In all periods, internal rates were adjusted to reflect the uncertainty of the cash flows used in the test.

Sensitivities of key assumptions in calculating VIU

At 1 July 2018, the Commercial Banking CGU was sensitive to reasonably possible changes in the key assumptions supporting the recoverable amount.

In making an estimate of reasonably possible changes to assumptions, management considers the available evidence in respect of each input to the model. These include the external range of observable discount rates, historical performance against forecast, and risks attaching to the key assumptions underlying cash flow projections.

The following table presents a summary of the key assumptions underlying the most sensitive inputs to the model for Commercial Banking, the key risks attaching to each, and details of a reasonably possible change to assumptions where, in the opinion of management, these could result in an impairment.

Reasonably possible changes in key assumptions

	Input	Key assumptions	Associated risks	Reasonably possible change
Cash-generating unit				
Commercial Banking	Cash flow projections	• Level of interest rates and yield curves. • Competitors' positions within the market. • Level and change in unemployment rates.	• Uncertain regulatory environment. • Customer remediation and regulatory actions.	• Cash flow projections decrease by 10%.
	Discount rate	• Discount rate used is a reasonable estimate of a suitable market rate for the profile of the business.	• External evidence arises to suggest that the rate used is not appropriate to the business.	• Discount rate increases by 100 basis points.
	Long-term growth rates	• Business growth will reflect GDP growth rates in the long term.	• Growth does not match GDP or there is a fall in GDP forecasts.	• Real GDP growth does not occur or is not reflected in performance.

Sensitivity of VIU to reasonably possible changes in key assumptions and changes to current assumptions to achieve nil headroom

			Increase/(decrease)		
Cash-generating unit	**Carrying amount**	**Value in use**	**Discount rate**	**Cash flows**	**Long-term growth**
At 1 July 2018	**£m**	**£m**	**bps**	**%**	**bps**
Commercial Banking	**5,413**	**6,093**	**73**	**(11.2)**	**(88)**

Whilst there are no indicators of impairment at 31 December 2018, CMB's recoverable amount exceeds the carrying amount by only £680m and sensitivity is high. The reasonably possible changes in assumption detailed above would result in an impairment. Thus there is a risk of impairment in the future should business performance or economic factors diverge from forecasts.

Present value of in-force long-term insurance business

When calculating the present value of in-force ('PVIF') insurance business, expected cash flows are projected after adjusting for a variety of assumptions made by each insurance operation to reflect local market conditions and management's judgement of future trends, and uncertainty in the underlying assumptions is reflected by applying margins (as opposed to a cost of capital methodology). Variations in actual experience and changes to assumptions can contribute to volatility in the results of the insurance business.

Actuarial Control Committees of each key insurance entity meet on a quarterly basis to review and approve PVIF assumptions. All changes to non-economic assumptions, economic assumptions that are not observable and model methodology must be approved by the Actuarial Control Committee.

Movements in PVIF

	2018	2017
	£m	£m
PVIF at 1 Jan	**572**	577
Change in PVIF of long-term insurance business	**74**	(23)
– value of new business written during the year	**32**	29
– expected return[1]	**(65)**	(65)
– assumption changes and experience variances[2] (see below)	**113**	33
– other adjustments	**(6)**	(20)
Exchange differences	**5**	18
PVIF at 31 Dec	**651**	572

1 *'Expected return' represents the unwinding of the discount rate and reversal of expected cash flows for the period.*
2 *Represents the effect of changes in assumptions on expected future profits and the difference between assumptions used in the previous PVIF calculation and actual experience observed during the year to the extent that this affects future profits. The gain of £113m (2017: £33m) was driven by modelling methodology updates in France and changes to product management in France and the UK.*

Key assumptions used in the computation of PVIF for main life insurance operations

Economic assumptions are set in a way that is consistent with observable market values. The valuation of PVIF is sensitive to observed market movements and the impact of such changes is included in the sensitivities presented below.

	2018		2017	
	UK	**France[1]**	UK	France[1]
	%	**%**	%	%
Weighted average risk-free rate	**1.19**	**1.52**	1.15	1.50
Weighted average risk discount rate	**1.69**	**2.35**	1.65	2.20
Expense inflation	**3.49**	**1.70**	4.55	1.48

1 *For 2018, the calculation of France's PVIF assumes a risk discount rate of 2.35% (2017: 2.20%) plus a risk margin of £85m (2017: £59m).*

Sensitivity to changes in economic assumptions

The group sets the risk discount rate applied to the PVIF calculation by starting from a risk-free rate curve and adding explicit allowances for risks not reflected in the best estimate cash flow modelling. Where the insurance operations provide options and guarantees to policyholders the cost of these options and guarantees is an explicit reduction to PVIF, unless it is already allowed for as an explicit addition to the technical provisions required by regulators. See page 67 for further details of these guarantees and the impact of changes in economic assumptions on our insurance manufacturing subsidiaries.

Sensitivity to changes in non-economic assumptions

Policyholder liabilities and PVIF are determined by reference to non-economic assumptions including mortality and/or morbidity, lapse rates and expense rates. See page 68 for further details on the impact of changes in non-economic assumptions on our insurance manufacturing operations.

21 Prepayments, accrued income and other assets

	The group		The bank	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Prepayments and accrued income	**1,683**	2,047	**863**	1,131
Settlement accounts[1]	**7,047**	N/A	**5,638**	N/A
Cash collateral and margin receivables[1]	**21,823**	N/A	**18,502**	N/A
Assets held for sale	**37**	461	**1**	6
Bullion	**2,995**	2,608	**2,994**	2,606
Endorsements and acceptances	**115**	210	**81**	171
Reinsurers' share of liabilities under insurance contracts (Note 4)	**179**	336	**–**	–
Employee benefit assets (Note 6)	**24**	6,066	**24**	6,066
Other accounts	**2,475**	2,276	**2,263**	1,945
Property, plant and equipment	**1,119**	2,022	**122**	933
At 31 Dec	**37,497**	16,026	**30,488**	12,858

1 *Settlement accounts, cash collateral and margin receivables included in 'Trading assets' (the group: £26,447m; the bank: £22,772m), 'Loans and advances to banks' (the group: £573m; the bank: £424m) and 'Loans and advances to customers' (the group: £394m; the bank: £265m) at 31 December 2017 were reclassified to 'Settlements accounts' and 'Cash collateral and margin receivables' at 1 January 2018 in accordance with IFRS 9. Comparative data was not restated. This reclassification was in accordance with IFRS 9. Refer to Note 34 'Effects of reclassifications upon adoption of IFRS 9' for further details. In addition, intragroup trade receivables have been reclassified from 'Loans and advances to banks' and 'Loans and advances to customers' to 'Cash collateral and margin receivables'.*

Prepayments, accrued income and other assets include £32,826m (2017: £4,738m) of financial assets, the majority of which are measured at amortised cost.

Assets held for sale

	The group		The bank	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Property, plant and equipment	**36**	15	**–**	6
Assets of disposal groups held for sale	**1**	446	**1**	–
Assets classified as held for sale at 31 Dec	**37**	461	**1**	6

22 Trading liabilities

	The group		The bank	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Deposits by banks[1, 2]	**3,942**	33,092	**3,853**	30,811
Customer accounts[1, 2]	**6,627**	20,594	**6,385**	18,826
Other debt securities in issue[3]	**1,095**	19,374	**50**	15,155
Other liabilities – net short positions in securities	**37,850**	33,436	**17,013**	12,511
At 31 Dec[4]	**49,514**	106,496	**27,301**	77,303

1 *'Deposits by banks' and 'Customer accounts' include repos, stock lending and other amounts.*
2 *Settlement accounts, cash collateral and margin payables included within 'Deposits by banks' and 'Customer accounts' (the group: £30,755m; the bank: £26,999m) were reclassified from 'Trading liabilities' to 'Accruals, deferred income and other liabilities' on 1 January 2018. This reclassification is to better reflect the nature of these balances and ensure consistency of presentation. Comparative data was not restated as the reclassification is not significant in the context of other changes to the balance sheet resulting from the adoption of IFRS 9. Refer to Note 34 'Effects of reclassifications upon adoption of IFRS 9' for further details.*
3 *'Other debt securities in issue' comprises structured notes issued by the group for which market risks are actively managed as part of trading portfolios.*
4 *We have considered market practices for the presentation of certain financial liabilities which contain both deposit and derivative components and were previously included in 'Trading liabilities'. Such liabilities amounted to £17,958m (the group) and £15,161m (the bank) at 31 December 2017. These liabilities are classified as 'Financial liabilities designated at fair value' from 1 January 2018. Comparative information has not been restated. Refer to Note 34 'Effects of reclassifications upon adoption of IFRS 9' for further details.*

23 Financial liabilities designated at fair value

	The group		The bank	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Deposits by banks and customer accounts	**169**	108	**93**	—
Liabilities to customers under investment contracts	**611**	547	**—**	—
Debt securities in issue[1]	**33,643**	13,343	**20,339**	6,755
Subordinated liabilities (Note 26)	**2,177**	3,912	**2,499**	4,251
Preferred securities (Note 26)	**322**	339	**—**	—
At 31 Dec	**36,922**	18,249	**22,931**	11,006

1 *We have considered market practices for the presentation of certain financial liabilities which contain both deposit and derivative components and were previously included in 'Trading liabilities'. Such liabilities amounted to £17,958m (the group) and £15,161m (the bank) at 31 December 2017. These liabilities are classified as 'Debt securities in issue' from 1 January 2018. Comparative information has not been restated. Refer to Note 34 'Effects of reclassifications upon adoption of IFRS 9' for further details.*

The group

The carrying amount of financial liabilities designated at fair value was £9,438m less than the contractual amount at maturity (2017: £1,095m more). The cumulative amount of change in fair value attributable to changes in credit risk was £(201)m (2017: loss of £312m).

The bank

The carrying amount of financial liabilities designated at fair value was £9,636m less than the contractual amount at maturity (2017: £826m higher). The cumulative amount of change in fair value attributable to changes in credit risk was £(113)m (2017: loss of £204m).

24 Accruals, deferred income and other liabilities

	The group		**The bank**	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Accruals and deferred income	**2,333**	2,342	**1,336**	1,371
Settlement accounts[1]	**5,814**	N/A	**5,443**	N/A
Cash collateral and margin payables[1]	**29,747**	N/A	**26,642**	N/A
Endorsements and acceptances	**115**	208	**82**	171
Employee benefit liabilities (Note 6)	**332**	338	**95**	123
Liabilities of disposal groups held for sale	**—**	454	**—**	—
Amount due to investors in funds consolidated by the group	**598**	636	**—**	—
Share-based payment liability to HSBC Holdings	**155**	146	**128**	128
Other liabilities	**1,942**	2,491	**1,424**	1,574
At 31 Dec	**41,036**	6,615	**35,150**	3,367

1 *Settlement accounts, cash collateral and margin payables included in 'Trading liabilities' (the group: £30,755m; the bank: £26,999m), 'Deposits by banks' (the group: £570m; the bank: £516m) and 'Customer accounts' (the group: £548m; the bank: £344m) were reclassified to 'Settlement accounts' and 'Cash collateral and margin payables' on 1 January 2018. This reclassification is to better reflect the nature of these balances and ensure consistency of presentation. Comparative data was not restated as the reclassification is not significant in the context of other changes to the balance sheet resulting from the adoption of IFRS 9. Refer to Note 34 'Effects of reclassifications upon adoption of IFRS 9' for further details. In addition, intragroup trade payables have been reclassified from 'Deposits from banks' and 'Customer accounts' to 'Cash collateral and margin payables'.*

For the group, accruals, deferred income and other liabilities include £40,327m (2017: £5,728m), and for the bank £34,740m(2017: £2,861m) of financial liabilities, the majority of which are measured at amortised cost.

25 Provisions

The group	Restructuring costs	Legal proceedings and regulatory matters	Customer remediation	Other provisions[2]	Total
	£m	£m	£m	£m	£m
Provisions (excluding contractual commitments)					
At 31 Dec 2017	**94**	**406**	**1,065**	**176**	**1,741**
Additions	**2**	**65**	**91**	**86**	**244**
Amounts utilised	**(34)**	**(138)**	**(337)**	**(66)**	**(575)**
Unused amounts reversed	**(29)**	**(107)**	**(47)**	**(73)**	**(256)**
Unwinding of discounts	**—**	**—**	**—**	**4**	**4**
Transfer to HSBC UK Bank plc and its subsidiaries	**(2)**	**(2)**	**(742)**	**(5)**	**(751)**
Exchange and other movements	**—**	**7**	**5**	**(1)**	**11**
At 31 Dec 2018	**31**	**231**	**35**	**121**	**418**
Contractual commitments[1]					
At 31 Dec 2017					**55**
Impact on transition to IFRS 9					**104**
Transfer to HSBC UK Bank plc					**(72)**
Net change in expected credit loss provision and other movements					**33**
At 31 Dec 2018					**120**
Total Provisions					
At 31 Dec 2017					**1,796**
At 31 Dec 2018					**538**

	Restructuring costs	Legal proceedings and regulatory matters	Customer remediation	Contractual commitments[1]	Other provisions[2]	Total
	£m	£m	£m	£m	£m	£m
At 1 Jan 2017	253	1,095	897	53	133	2,431
Additions	45	116	625	34	127	947
Amounts utilised	(127)	(85)	(412)	(1)	(37)	(662)
Unused amounts reversed	(54)	(653)	(39)	(26)	(50)	(822)
Exchange and other movements	(23)	(67)	(6)	(5)	3	(98)
At 31 Dec 2017	94	406	1,065	55	176	1,796

1 The contractual commitments provision at 31 December 2017 represented IAS 37 provisions on off-balance sheet loan commitments and guarantees, for which expected credit losses are provided following transition to IFRS 9 on 1 January 2018. It further includes provisions in respect of insurance contracts.
2 Other provisions includes £48m (2017: £106m) of vacant space provisions of which there were unwinding of discounts of £3m (2017: £5m).

The bank	Restructuring costs	Legal proceedings and regulatory matters	Customer remediation	Other provisions[2]	Total
	£m	£m	£m	£m	£m
Provisions (excluding contractual commitments)					
At 31 Dec 2017	**37**	**355**	**850**	**119**	**1,361**
Additions	**—**	**60**	**57**	**39**	**156**
Amounts utilised	**(9)**	**(115)**	**(226)**	**(36)**	**(386)**
Unused amounts reversed	**(27)**	**(92)**	**(46)**	**(49)**	**(214)**
Unwinding of discounts	**1**	**—**	**—**	**3**	**4**
Transfer to HSBC UK Bank plc	**(2)**	**—**	**(615)**	**(5)**	**(622)**
Exchange and other movements	**—**	**6**	**4**	**(1)**	**9**
At 31 Dec 2018	**—**	**214**	**24**	**70**	**308**
Contractual commitments[1]					
At 31 Dec 2017					**33**
Impact on transition to IFRS 9					**97**
Transfer to HSBC UK Bank plc					**(71)**
Net change in expected credit loss provision and other movements					**33**
At 31 Dec 2018					**92**
Total Provisions					
At 31 Dec 2017					**1,394**
At 31 Dec 2018					**400**

	Restructuring costs	Legal proceedings and regulatory matters	Customer remediation	Contractual commitments[1]	Other provisions[2]	Total
	£m	£m	£m	£m	£m	£m
At 1 Jan 2017	154	980	650	29	72	1,885
Additions	36	99	556	27	83	801
Amounts utilised	(107)	(15)	(315)	(1)	(11)	(449)
Unused amounts reversed	(46)	(649)	(34)	(21)	(35)	(785)
Exchange and other movements	—	(60)	(7)	(1)	10	(58)
At 31 Dec 2017	37	355	850	33	119	1,394

1 *The contractual commitments provision at 31 December 2017 represented IAS 37 provisions on off-balance sheet loan commitments and guarantees, for which expected credit losses are provided following transition to IFRS 9 on 1 January 2018. It further includes provisions in respect of insurance contracts.*
2 *Other provisions includes £48m (2017: £106m) of vacant space provisions of which there were unwinding of discounts of £3m (2017: £5m).*

Legal proceedings and regulatory matters

Further details of legal proceedings and regulatory matters are set out in Note 32. Legal proceedings include civil court, arbitration or tribunal proceedings brought against HSBC companies (whether by way of claim or counterclaim), or civil disputes that may, if not settled, result in court, arbitration or tribunal proceedings. Regulatory matters refer to investigations, reviews and other actions carried out by, or in response to the actions of, regulatory or law enforcement agencies in connection with alleged wrongdoing.

Customer remediation

Provisions include £35m (2017: £1.1bn) in respect of customer redress programmes. The majority of the provisions relating to the Payment Protection Insurance were transferred to HSBC UK Bank plc under the ring-fence implementation. At 31 December 2018 HSBC Bank plc holds £5m in provisions in respect to Payment Protection Insurance claims for Channel Island and Isle of Man customers.

Contractual commitments

Refer to Note 34 for further information on the impact of IFRS 9 on undrawn loan commitments and financial guarantees, presented in ‘Contractual commitments’. This provision results from the adoption of IFRS 9 and has no comparatives. Further analysis of the movement in the expected credit loss provision is disclosed within the 'Reconciliation of impairment allowances under IAS 39 and provisions under IAS 37 to expected credit losses under IFRS 9' table on page 45.

26 Subordinated liabilities

Subordinated liabilities

	The group		The bank	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
At amortised cost	**13,770**	16,494	**13,323**	15,930
– subordinated liabilities	**13,070**	15,794	**13,323**	15,930
– preferred securities	**700**	700	**—**	—
Designated at fair value (Note 23)	**2,499**	4,251	**2,499**	4,251
– subordinated liabilities	**2,177**	3,912	**2,499**	4,251
– preferred securities	**322**	339	**—**	—
At 31 Dec	**16,269**	20,745	**15,822**	20,181

Subordinated liabilities rank behind senior obligations and consist of capital instruments and other instruments. Capital instruments generally count towards the capital base of the group and may be called and redeemed by the group subject to prior notification to the PRA and, where relevant, the consent of the local banking regulator. If not redeemed at the first call date, coupons payable may step up or become floating rate based on interbank rates. On capital instruments other than floating rate notes, interest is payable at fixed rates of up to 7.65%.

The balance sheet amounts disclosed below are presented on an IFRS basis and do not reflect the amount that the instruments contribute to regulatory capital due to the inclusion of issuance costs, regulatory amortisation and regulatory eligibility limits prescribed in the grandfathering provisions under CRD IV.

Subordinated liabilities of the group

		Footnotes	Carrying amount 2018 £m	2017 £m
Capital instruments				
Additional tier 1 instruments guaranteed by the bank				
£300m	5.862% Non-cumulative Step-up Perpetual Preferred Securities	1	**322**	339
£700m	5.844% Non-cumulative Step-up Perpetual Preferred Securities	2	**700**	700
Tier 2 instruments				
$450m	Subordinated Floating Rate Notes 2021		**352**	333
$750m	3.43% Subordinated Loan 2022	10	**585**	568
£350m	5% Callable Subordinated Notes 2023	4	**—**	367
£300m	6.5% Subordinated Notes 2023		**300**	299
€650m	Floating Rate Subordinated Loan 2023	5	**—**	577
€1,500m	Floating Rate Subordinated Loan 2023	10	**1,345**	1,331
$2,000m	3.5404% Subordinated Loan 2023	10	**1,566**	1,480
€1,500m	Floating Rate Subordinated Loan 2024	3	**1,345**	—
€2,000m	1.728% Subordinated Loan 2024	3	**1,794**	—
€2,000m	1.125% Subordinated Loan 2024	10	**1,794**	1,775
$300m	7.65% Subordinated Notes 2025		**235**	277
$1,400m	Floating Rate Subordinated Loan 2025	5	**—**	1,036
$1,300m	Floating Rate Subordinated Loan 2026	5	**—**	962
€300m	Floating Rate Subordinated Loan 2027		**269**	266
$750m	4.186% Subordinated Loan 2027	10	**598**	583
€1,250m	1.4648% Subordinated Loan 2027	10	**1,121**	1,109
€260m	Floating Rate Subordinated Loan 2029	11	**233**	231
£200m	Floating Rate Subordinated Loan 2028	7	**200**	—
€300m	Floating Rate Subordinated Loan 2028	8	**269**	—
£350m	5.375% Callable Subordinated Step-up Notes 2030	9	**401**	432
£500m	5.375% Subordinated Notes 2033		**593**	675
£225m	6.25% Subordinated Notes 2041		**224**	224
£600m	4.75% Subordinated Notes 2046		**594**	594
$750m	Undated Floating Rate Primary Capital Notes		**587**	555
$500m	Undated Floating Rate Primary Capital Notes		**392**	370
$300m	Undated Floating Rate Primary Capital Notes (Series 3)		**235**	222
Other Tier 2 instruments each less than £100m			**215**	322
Other instruments				
Subordinated loan instruments not eligible for inclusion in regulatory capital				
€1,500m	Floating Rate Subordinated Loan 2021	3	**—**	1,331
€2,000m	0.6633% Subordinated Loan 2022	3	**—**	1,775
£1,000m	2.6% Subordinated Loan 2026	6	**—**	1,012
£1,000m	2.948% Subordinated Loan 2028	6	**—**	1,000
At 31 Dec			**16,269**	20,745

1 In April 2020, the distribution rate changes to six month sterling LIBOR plus 1.85%.
2 In November 2031, the distribution rate changes to six month sterling LIBOR plus 1.76%.
3 In December 2018, the bank repaid the €1,500m Floating Rate Subordinated Loan 2021 and the €2,000m 0.6633% Subordinated Loan 2022 from HSBC Holdings plc and received the €1,500m Floating Rate Subordinated Loan 2024 and the €2,000m 1.728% Subordinated Loan 2024 from HSBC UK Holdings plc.
4 In March 2018 the bank repaid the £350m 5% Callable Subordinated Notes 2023.
5 In June 2018, the bank repaid the €650m Floating Rate Subordinated Loan 2023, the US$1,400m Floating Rate Subordinated Loan 2025 and the US$1,300m Floating Rate Subordinated Loan 2026 from HSBC Holdings plc.
6 In October 2018, the bank repaid the £1,000m 2.6% Subordinated Loan 2026 and the £1,000m 2.948% Subordinated Loan 2028 from HSBC Holdings plc.
7 In May 2018, the bank received the £200m Floating Rate Subordinated Loan 2028 from HSBC UK Holdings plc.
8 In June 2018, the bank received the €300m Floating Rate Subordinated Loan 2028 from HSBC UK Holdings plc.
9 In November 2025, the interest rate changes to three month sterling LIBOR plus 1.50%.
10 These instruments were issued in 2017 in preparation to meet the Minimum Requirement for Own Funds and Eligible Liabilities (MREL) and did not previously qualify as regulatory capital. However, they were converted to qualify as Tier 2 regulatory capital in Q4 2018.
11 This instrument was issued by HSBC France to HSBC Holdings plc in 2014. Starting in Q4 2018, it now qualifies as a Tier 2 regulatory capital instrument for HSBC France and HSBC Bank plc.
Footnotes 1, 2, 4 and 9 all relate to instruments that are redeemable at the option of the issuer on the date of the change in the distribution or interest rate, and on subsequent rate reset and payment dates in some cases, subject to prior notification to the PRA.

27 Maturity analysis of assets, liabilities and off-balance sheet commitments

Contractual maturity of financial liabilities

The balances in the table below do not agree directly with those in our consolidated balance sheet as the table incorporates, on an undiscounted basis, all cash flows relating to principal and future coupon payments (except for trading liabilities and derivatives not treated as hedging derivatives).

Undiscounted cash flows payable in relation to hedging derivative liabilities are classified according to their contractual maturities. Trading liabilities and derivatives not treated as hedging derivatives are included in the 'On demand' time bucket and not by contractual maturity.

In addition, loans and other credit-related commitments, financial guarantees are generally not recognised on our balance sheet. The undiscounted cash flows potentially payable under financial guarantees are classified on the basis of the earliest date they can be called.

Cash flows payable under financial liabilities by remaining contractual maturities

The group	On demand £m	Due within 3 months £m	Due between 3 and 12 months £m	Due between 1 and 5 years £m	Due after 5 years £m	Total £m
Deposits by banks	**12,708**	**5,097**	**880**	**5,456**	**436**	**24,577**
Customer accounts	**149,093**	**25,396**	**6,141**	**214**	**66**	**180,910**
Repurchase agreements – non-trading	**—**	**45,804**	**847**	**—**	**—**	**46,651**
Trading liabilities[1]	**49,514**	**—**	**—**	**—**	**—**	**49,514**
Financial liabilities designated at fair value[1]	**123**	**1,130**	**2,822**	**22,285**	**29,909**	**56,269**
Derivatives	**139,021**	**44**	**242**	**518**	**340**	**140,165**
Debt securities in issue	**—**	**8,417**	**11,018**	**2,785**	**842**	**23,062**
Subordinated liabilities	**—**	**115**	**205**	**4,798**	**11,057**	**16,175**
Other financial liabilities	**37,545**	**1,644**	**534**	**96**	**773**	**40,592**
	388,004	**87,647**	**22,689**	**36,152**	**43,423**	**577,915**
Loan and other credit-related commitments	**148,600**	**289**	**6**	**—**	**—**	**148,895**
Financial guarantees[2]	**6,054**	**—**	**—**	**—**	**—**	**6,054**
At 31 Dec 2018	**542,658**	**87,936**	**22,695**	**36,152**	**43,423**	**732,864**
Deposits by banks	16,922	5,215	1,336	5,372	578	29,423
Customer accounts	326,674	43,742	9,143	1,347	793	381,699
Repurchase agreements – non-trading	10,257	26,012	1,503	—	—	37,772
Trading liabilities	106,496	—	—	—	—	106,496
Financial liabilities designated at fair value	510	476	3,793	9,318	5,148	19,245
Derivatives	138,555	113	256	928	428	140,280
Debt securities in issue	5	4,469	6,864	1,656	468	13,462
Subordinated liabilities	2	47	86	3,962	13,540	17,637
Other financial liabilities	3,964	1,495	446	101	832	6,838
	603,385	81,569	23,427	22,684	21,787	752,852
Loan and other credit-related commitments[3]	139,916	31,915	2,305	632	3	174,771
Financial guarantees[2,4]	8,301	—	—	—	—	8,301
At 31 Dec 2017	751,602	113,484	25,732	23,316	21,790	935,924

1 *Structured liabilities have moved from 'Trading liabilities' to 'Financial liabilities designated at fair value'. Comparatives have not been restated. See Note 34 for further details.*
2 *Excludes performance guarantee contracts to which the impairment requirements in IFRS 9 are not applied.*
3 *31 December 2017 balances have been restated to include £32.5bn of loan commitments (unsettled reverse repurchase agreements) not previously identified for disclosure.*
4 *The undiscounted cash flows potentially payable under financial guarantees are classified on the basis of the earliest date they can be called. Application of this policy throughout the group was improved in 2018, and therefore comparative information has been represented.*

Cash flows payable under financial liabilities by remaining contractual maturities (continued)

The bank	On demand £m	Due within 3 months £m	Due between 3 and 12 months £m	Due between 1 and 5 years £m	Due after 5 years £m	Total £m
Deposits by banks	**11,327**	**5,105**	**1,476**	**276**	**—**	**18,184**
Customer accounts	**103,631**	**20,403**	**1,870**	**29**	**—**	**125,933**
Repurchase agreements - non-trading	**—**	**35,087**	**676**	**—**	**—**	**35,763**
Trading liabilities[1]	**27,301**	**—**	**—**	**—**	**—**	**27,301**
Financial liabilities designated at fair value[1]	**5**	**1,108**	**2,613**	**13,817**	**24,220**	**41,763**
Derivatives	**134,511**	**37**	**194**	**482**	**309**	**135,533**
Debt securities in issue	**—**	**6,952**	**9,028**	**2,848**	**601**	**19,429**
Subordinated liabilities	**—**	**91**	**239**	**4,799**	**11,177**	**16,306**
Other financial liabilities	**33,166**	**1,528**	**89**	**—**	**—**	**34,783**
	309,941	**70,311**	**16,185**	**22,251**	**36,307**	**454,995**
Loan and other credit-related commitments	**65,669**	**269**	**—**	**—**	**—**	**65,938**
Financial guarantees[2]	**5,578**	**—**	**—**	**—**	**—**	**5,578**
At 31 Dec 2018	**381,188**	**70,580**	**16,185**	**22,251**	**36,307**	**526,511**
Deposits by banks	16,613	3,233	4,359	370	54	24,629
Customer accounts	275,845	38,670	4,878	891	359	320,643
Repurchase agreements - non-trading	10,232	23,655	1,330	—	—	35,217
Trading liabilities	77,303	—	—	—	—	77,303
Financial liabilities designated at fair value	22	476	2,598	5,524	3,299	11,919
Derivatives	131,790	108	196	807	404	133,305
Debt securities in issue	5	1,453	4,019	226	582	6,285
Subordinated liabilities	—	46	40	3,780	13,176	17,042
Other financial liabilities	2,676	666	97	10	—	3,449
	514,486	68,307	17,517	11,608	17,874	629,792
Loan and other credit-related commitments	98,319	476	982	34	3	99,814
Financial guarantees[3]	6,711	—	—	—	—	6,711
At 31 Dec 2017	619,516	68,783	18,499	11,642	17,877	736,317

1 *Structured liabilities have moved from 'Trading liabilities' to 'Financial liabilities designated at fair value'. Comparatives have not been restated. See Note 34 for further details.*
2 *Excludes performance guarantee contracts to which the impairment requirements in IFRS 9 are not applied.*
3 *The undiscounted cash flows potentially payable under financial guarantees are classified on the basis of the earliest date they can be called. Application of this policy throughout the group was improved in 2018, and therefore comparative information has been represented.*

Maturity analysis of financial assets and financial liabilities

The following table provides an analysis of financial assets and liabilities by residual contractual maturity at the balance sheet date. These balances are included in the maturity analysis as follows:

- Financial assets and liabilities with no contractual maturity (such as equity securities) are included in the 'Due after more than one year' time bucket. Undated or perpetual instruments are classified based on the contractual notice period which the counterparty of the instrument is entitled to give. Where there is no contractual notice period, undated or perpetual contracts are included in the 'Due after more than one year' time bucket;
- Financial instruments included within assets and liabilities of disposal groups held for sale are classified on the basis of the contractual maturity of the underlying instruments and not on the basis of the disposal transaction;
- Liabilities under investment contracts are classified in accordance with their contractual maturity. Undated investment contracts are included in the 'Due after more than one year' time bucket, however, such contracts are subject to surrender and transfer options by the policyholders.

Maturity analysis of financial assets and financial liabilities

	2018			2017		
	Due within 1 year	**Due after more than 1 year**	**Total**	Due within 1 year	Due after more than 1 year	Total
The group	**£m**	**£m**	**£m**	£m	£m	£m
Assets						
Financial assets designated or otherwise mandatorily measured at fair value	**5,171**	**12,628**	**17,799**	N/A	N/A	N/A
Financial assets designated at fair value	**N/A**	**N/A**	**N/A**	67	9,199	9,266
Loans and advances to banks	**9,805**	**3,823**	**13,628**	10,697	3,452	14,149
Loans and advances to customers	**55,481**	**56,483**	**111,964**	93,239	187,163	280,402
Reverse repurchase agreement – non-trading	**79,739**	**363**	**80,102**	45,383	425	45,808
Financial investments	**9,677**	**37,595**	**47,272**	10,832	47,168	58,000
Other financial assets	**32,481**	**345**	**32,826**	2,475	306	2,781
At 31 Dec	**192,354**	**111,237**	**303,591**	162,693	247,713	410,406
Liabilities						
Deposits by banks	**18,612**	**5,920**	**24,532**	23,434	5,915	29,349
Customer accounts	**180,544**	**292**	**180,836**	379,463	2,083	381,546
Repurchase agreements – non-trading	**46,583**	**—**	**46,583**	37,775	—	37,775
Financial liabilities designated at fair value	**3,857**	**33,065**	**36,922**	3,768	14,481	18,249
Debt securities in issue	**19,552**	**3,169**	**22,721**	11,188	2,098	13,286
Other financial liabilities	**39,108**	**880**	**39,988**	2,900	703	3,603
Subordinated liabilities	**25**	**13,745**	**13,770**	40	16,454	16,494
At 31 Dec	**308,281**	**57,071**	**365,352**	458,568	41,734	500,302
The bank						
Assets						
Financial assets designated or otherwise mandatorily measured at fair value	**4,799**	**946**	**5,745**	N/A	N/A	N/A
Loans and advances to banks	**8,948**	**3,738**	**12,686**	9,379	5,781	15,160
Loans and advances to customers	**39,844**	**18,939**	**58,783**	74,941	145,509	220,450
Reverse repurchase agreement – non-trading	**56,357**	**138**	**56,495**	36,201	426	36,627
Financial investments	**5,506**	**21,193**	**26,699**	6,023	25,359	31,382
Other financial assets	**27,210**	**11**	**27,221**	2,090	2	2,092
31 Dec	**142,664**	**44,965**	**187,629**	128,634	177,077	305,711
Liabilities						
Deposits by banks	**17,882**	**266**	**18,148**	24,202	424	24,626
Customer accounts	**125,843**	**28**	**125,871**	319,369	657	320,026
Repurchase agreements – non-trading	**35,693**	**—**	**35,693**	35,220	—	35,220
Financial liabilities designated at fair value	**3,516**	**19,415**	**22,931**	2,435	8,571	11,006
Debt securities in issue	**15,859**	**3,226**	**19,085**	5,457	651	6,108
Other financial liabilities	**34,485**	**—**	**34,485**	1,636	—	1,636
Subordinated liabilities	**—**	**13,323**	**13,323**	—	15,930	15,930
31 Dec	**233,278**	**36,258**	**269,536**	388,319	26,233	414,552

28 Offsetting of financial assets and financial liabilities

The ‘Amounts not set off in the balance sheet’ include transactions where:

- The counterparty has an offsetting exposure with the group and a master netting or similar arrangement is in place with a right of set off only in the event of default, insolvency or bankruptcy, or the offset criteria are not otherwise satisfied.
- In the case of derivatives and reverse repurchase/repurchase, stock borrowing/lending and similar agreements, cash and non-cash collateral has been received/pledged.

For risk management purposes, the net amounts of loans and advances to customers are subject to limits, which are monitored and the relevant customer agreements are subject to review and updated, as necessary, to ensure that the legal right of offset remains appropriate.

	Amounts subject to enforceable netting arrangements								
				Amounts not set off in the balance sheet					
	Gross amounts	Amounts offset	Net amounts in the balance sheet	Financial instruments	Non-cash collateral	Cash collateral	Net amount	Amounts not subject to enforceable netting arrangements[5]	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Financial assets									
Derivatives (Note 14)[1]	**169,923**	**(26,692)**	**143,231**	**(104,948)**	**(6,816)**	**(29,081)**	**2,386**	**1,291**	**144,522**
Reverse repos, stock borrowing and similar agreements classified as[2]:									
– trading assets	**12,661**	**(619)**	**12,042**	**(975)**	**(11,068)**	**—**	**(1)**	**597**	**12,639**
– non-trading assets	**184,887**	**(107,441)**	**77,446**	**(17,084)**	**(60,288)**	**(73)**	**1**	**2,674**	**80,120**
Loans and advances to customers[3]	**24,698**	**(7,744)**	**16,954**	**(12,040)**	**—**	**—**	**4,914**	**—**	**16,954**
At 31 Dec 2018	**392,169**	**(142,496)**	**249,673**	**(135,047)**	**(78,172)**	**(29,154)**	**7,300**	**4,562**	**254,235**
Derivatives (Note 14)[1]	208,031	(66,736)	141,295	(105,613)	(7,524)	(26,037)	2,121	2,040	143,335
Reverse repos, stock borrowing and similar agreements classified as[2]:									
– trading assets	10,298	—	10,298	(319)	(9,979)	—	—	878	11,176
– non-trading assets	100,249	(59,103)	41,146	(2,748)	(38,368)	(30)	—	4,662	45,808
Loans and advances to customers[3]	30,499	(7,716)	22,783	(19,073)	—	(134)	3,576	—	22,783
31 Dec 2017	349,077	(133,555)	215,522	(127,753)	(55,871)	(26,201)	5,697	7,580	223,102
Financial liabilities									
Derivatives (Note 14)[1]	**164,194**	**(26,692)**	**137,502**	**(104,948)**	**(10,685)**	**(20,914)**	**955**	**2,430**	**139,932**
Repos, stock lending and similar agreements classified as[2]:									
– trading liabilities	**10,706**	**(619)**	**10,087**	**(975)**	**(9,113)**	**—**	**(1)**	**101**	**10,188**
– non-trading liabilities	**153,926**	**(107,441)**	**46,485**	**(17,084)**	**(29,271)**	**(129)**	**1**	**98**	**46,583**
Customer accounts[4]	**23,364**	**(7,744)**	**15,620**	**(12,040)**	**—**	**—**	**3,580**	**8**	**15,628**
At 31 Dec 2018	**352,190**	**(142,496)**	**209,694**	**(135,047)**	**(49,069)**	**(21,043)**	**4,535**	**2,637**	**212,331**
Derivatives (Note 14)[1]	205,836	(66,736)	139,100	(105,614)	(10,164)	(18,283)	5,039	970	140,070
Repos, stock lending and similar agreements classified as[2]:									
– trading liabilities	22,291	—	22,291	(319)	(21,972)	—	—	47	22,338
– non-trading liabilities	93,940	(59,103)	34,837	(2,747)	(31,912)	(178)	—	2,938	37,775
Customer accounts[4]	30,382	(7,716)	22,666	(19,073)	—	(139)	3,454	117	22,783
31 Dec 2017	352,449	(133,555)	218,894	(127,753)	(64,048)	(18,600)	8,493	4,072	222,966

1 *At 31 December 2018, the amount of cash margin received that had been offset against the gross derivatives assets was £2,354m (2017: £3,247m). The amount of cash margin paid that had been offset against the gross derivatives liabilities was £4,269m (2017: £3,428m).*
2 *For the amount of repos, reverse repos, stock lending, stock borrowing and similar agreements recognised on the balance sheet within 'Trading assets' £95,420m (2017: £145,725m) and 'Trading liabilities' £49,514m (2017: £106,496m), see the 'Funding sources and uses' table on page 62.*
3 *At 31 December 2018, the total amount of 'Loans and advances to customers' recognised on the balance sheet was £111,964m (2017: £280,402m) of which £16,954m (2017: £22,783m) was subject to offsetting.*
4 *At 31 December 2018, the total amount of 'Customer accounts' recognised on the balance sheet was £180,836m (2017: £381,546m) of which £15,620m (2017: £22,666m) was subject to offsetting.*
5 *These exposures continue to be secured by financial collateral, but we may not have sought or been able to obtain a legal opinion evidencing enforceability of the right of offset.*

29 Called up share capital and other equity instruments

Issued and fully paid

HSBC Bank plc £1.00 ordinary shares

	2018		2017	
	Number	£m	Number	£m
At 1 Jan	**796,969,110**	**797**	796,969,110	797
Re-designation of the £1.00 preferred ordinary share	**1**	**—**	—	—
At 31 Dec	**796,969,111**	**797**	796,969,110	797

HSBC Bank plc £1.00 preferred ordinary shares

	2018		2017	
	Number	£000	Number	£000
At 1 Jan	**1**	**—**	1	—
Shares re-designated into ordinary shares	**(1)**	**—**	—	—
At 31 Dec	**—**	**—**	1	—

At the Board's General Meeting held on 23 November 2018, a resolution was passed to amend the rights of the one preferred ordinary share of £1.00 in the capital of HSBC Bank plc, so it has the same rights, is subject to the same restrictions, and ranks *pari passu* in all respects with the ordinary shares of £1.00. This resulted in the preferred ordinary share to be re-designated as an ordinary share.

HSBC Bank plc $0.01 non-cumulative third dollar preference shares

	2018		2017	
	Number	**£000**	Number	£000
At 1 Jan and 31 Dec	**35,000,000**	**172**	35,000,000	172

The bank has no obligation to redeem the preference shares but may redeem them in part or in whole at any time, subject to prior notification to the Prudential Regulation Authority. Dividends on the preference shares in issue are paid annually at the sole and absolute discretion of the Board of Directors. The Board of Directors will not declare a dividend on the preference shares in issue if payment of the dividend would cause the bank not to meet the capital adequacy requirements of the Prudential Regulation Authority or the profit of the bank, available for distribution as dividends, is not sufficient to enable the bank to pay in full both dividends on the preference shares in issue and dividends on any other shares that are scheduled to be paid on the same date and have an equal right to dividends or if payment of the dividend is prohibited by the rights attached to any class of shares in the capital of the bank, excluding ordinary shares.

The preference shares in issue carry no rights to conversion into ordinary shares of the bank. Holders of the preference shares in issue will be able to attend any general meetings of shareholders of the bank and to vote on any resolution proposed to vary or abrogate any of the rights attaching to the preference shares or any resolution proposed to reduce the paid up capital of the preference shares. If the dividend payable on the preference shares in issue has not been paid in full for the most recent dividend period or any resolution is proposed for the winding-up of the bank or the sale of its entire business then, in such circumstances, holders of preference shares will be entitled to vote on all matters put to general meetings. In the case of unpaid dividends the holders of preference shares in issue will be entitled to attend and vote at any general meetings until such time as dividends on the preference shares have been paid in full, or a sum set aside for such payment in full, in respect of one dividend period. All shares in issue are fully paid.

Other equity instruments

HSBC Bank plc additional tier 1 instruments

		2018	2017
		£m	£m
£1,096m	Undated Subordinated Additional Tier 1 instrument issued 2014 (Callable December 2019 onwards)	**—**	1,096
£1,100m	Undated Subordinated Additional Tier 1 instrument issued 2014 (Callable December 2024 onwards)	**—**	1,100
£555m	Undated Subordinated Resettable Additional Tier 1 instrument 2018 (Callable March 2023 onwards)	**555**	—
€1,900m	Undated Subordinated Resettable Additional Tier 1 instrument issued 2015 (Callable December 2020 onwards)	**1,388**	1,388
€235m	Undated Subordinated Resettable Additional Tier 1 instrument issued 2016 (Callable January 2022 onwards)	**197**	197
€300m	Undated Subordinated Resettable Additional Tier 1 instrument 2018 (Callable March 2023 onwards)	**263**	—
At 31 Dec		**2,403**	3,781

The bank has issued capital instruments that are included in the group's capital base as fully CRD IV compliant additional tier 1 capital. During March 2018, the bank issued two new Undated Subordinated Additional Tier 1 Instruments.

With effect from 1 July 2018, under the ring-fencing transfer scheme, all rights and obligations in respect of the existing £1,096m Undated Subordinated Additional Tier 1 Instrument issued 2014 (Callable December 2019 onwards) and £1,100m Undated Subordinated Additional Tier 1 Instrument issued 2014 (Callable December 2024 onwards) issued by HSBC Bank plc were transferred to HSBC UK Bank plc.

Interest on these instruments will be due and payable only at the sole discretion of the bank, and the bank has sole and absolute discretion at all times and for any reason to cancel (in whole or in part) any interest payment that would otherwise be payable on any date. There are limitations on the payment of principal, interest or other amounts if such payments are prohibited under UK banking regulations, or other requirements, if the bank has insufficient distributable reserves or if the bank fails to satisfy the solvency condition as defined in the instruments terms.

The instruments are undated and are repayable, at the option of the bank, in whole at the initial call date, or on any Interest Payment Date after the initial call date. In addition, the instruments are repayable at the option of the bank in whole for certain regulatory or tax reasons. Any repayments require the prior consent of the Prudential Regulation Authority. These instruments rank pari passu with the bank's most senior class or classes of issued preference shares and therefore ahead of ordinary shares. These instruments will be written down in whole, together with any accrued but unpaid interest if either the group's solo or consolidated Common Equity Tier 1 Capital Ratio falls below 7.00%.

30 Contingent liabilities, contractual commitments and guarantees

	The group		The bank	
	2018	2017	**2018**	2017
	£m	£m	**£m**	£m
Guarantees and other contingent liabilities:				
– financial guarantees[1]	**6,054**	8,301	**5,578**	6,711
– performance and other guarantees[2]	**17,244**	16,591	**10,323**	11,657
– other contingent liabilities	**590**	353	**588**	351
At 31 Dec	**23,888**	25,245	**16,489**	18,719
Commitments:				
– documentary credits and short-term trade-related transactions	**2,186**	2,877	**963**	1,933
– forward asset purchases and forward deposits placed[2]	**50,116**	32,734	**1,526**	–
– standby facilities, credit lines and other commitments to lend	**96,593**	139,160	**63,449**	97,881
At 31 Dec	**148,895**	174,771	**65,938**	99,814

1 *'Financial guarantees' to which the impairment requirements in IFRS 9 are applied have been presented separately from other guarantees to align with credit risk disclosures. Comparatives have been re-presented accordingly.*
2 *For the group, 31 December 2017 balances have been restated to include £32.5bn of loan commitments (unsettled reverse repurchase agreements) and £2.3bn of performance and other guarantees not previously identified for disclosure.*

The above table discloses the nominal principal amounts, which represent the maximum amounts at risk should the contracts be fully drawn upon and clients default. As a significant portion of guarantees and commitments is expected to expire without being drawn upon, the total of the nominal principal amounts is not indicative of future liquidity requirements.

UK branches of HSBC overseas entities

In December 2017, HM Revenue & Customs ('HMRC') challenged the VAT status of certain UK branches of HSBC overseas entities. HMRC has also issued notices of assessment covering the period from 1 October 2013 to 31 December 2017 totalling £262m, with interest to be determined. No provision has been recognised in respect of these notices. Contingent liabilities arising from legal proceedings, regulatory and other matters against group companies are disclosed at Note 32.

In March 2018, HSBC requested that HMRC reconsider its assessment. In January 2019, HMRC reaffirmed its assessment that the UK branches are ineligible to be members of the UK VAT group. In February 2019, HSBC paid HMRC the sum of £262m and filed an appeal which remains pending. The payment of £262m will be recorded as an asset on HSBC's balance sheet in 2019.

Since January 2018, HSBC's returns have been prepared on the basis that the UK branches are not in the UK VAT group. In the event that HSBC's appeal is successful, HSBC will also be entitled to a refund of this VAT.

Financial Services Compensation Scheme

The Financial Services Compensation Scheme ('FSCS') has provided compensation to consumers following the collapse of a number of deposit takers. The compensation paid out to consumers was funded through loans from HM Treasury which has now been repaid (2017: £4.7bn). The bank could be liable to pay a proportion of any future amounts that the FSCS borrows from HM Treasury. The ultimate FSCS levy to the industry as a result of a collapse cannot currently be estimated reliably, as it is dependent on various uncertain factors, including the potential recoveries of assets by the FSCS and changes in the level of protected deposits and the population of FSCS members at the time.

Guarantees

	The group				The bank			
	2018		2017		**2018**		2017	
	In favour of third parties	**By the group in favour of other HSBC Group entities**	In favour of third parties	By the group in favour of other HSBC Group entities	**In favour of third parties**	**By the bank in favour of other HSBC Group entities**	In favour of third parties	By the bank in favour of other HSBC Group entities
	£m	**£m**	£m	£m	**£m**	**£m**	£m	£m
Financial guarantees[1,2]	**5,457**	**597**	7,659	642	**2,698**	**2,880**	4,666	2,045
Performance and other guarantees[3]	**16,243**	**1,001**	15,476	1,115	**9,238**	**1,085**	9,571	2,086
Total	**21,700**	**1,598**	23,135	1,757	**11,936**	**3,965**	14,237	4,131

1 *Financial guarantees contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss incurred because a specified debtor fails to make payment when due, in accordance with the original or modified terms of a debt instrument. The amounts in the above table are nominal principal amounts.*
2 *'Financial guarantees' to which the impairment requirements in IFRS 9 are applied have been presented separately from other guarantees to align with credit risk disclosures. Comparatives have been re-presented accordingly.*
3 *31 December 2017 balances have been restated to include £2.3bn of of performance and other guarantees not previously identified for disclosure.*

The group provides guarantees and similar undertakings on behalf of both third-party customers and other entities within HSBC Group. These guarantees are generally provided in the normal course of the group's banking businesses. Guarantees with terms of more than one year are subject to the group's annual credit review process.

31 Lease commitments

Operating lease commitments

At 31 December 2018, future minimum lease payments under non-cancellable operating leases for land, buildings and equipment were £608m (2017: £1,206m).

Finance lease receivables

The group leases a variety of assets to third parties under finance leases, including transport assets (such as aircraft), property and general plant and machinery. At the end of lease terms, assets may be sold to third parties or leased for further terms. Rentals are calculated to recover the cost of assets less their residual value, and earn finance income.

	2018			2017		
	Total future minimum payments	**Unearned finance income**	**Present value**	Total future minimum payments	Unearned finance income	Present Value
	£m	**£m**	**£m**	£m	£m	£m
Lease receivables[1]:						
No later than one year	**290**	**(23)**	**267**	1,891	(156)	1,735
Later than one year and no later than five years	**1,348**	**(82)**	**1,266**	3,634	(294)	3,340
Later than five years	**837**	**(45)**	**792**	1,283	(151)	1,132
At 31 Dec	**2,475**	**(150)**	**2,325**	6,808	(601)	6,207

1 *Impacted by the transfers to HSBC UK Bank plc under the ring-fence implementation. For further information see Note 35 Discontinued operations.*

32 Legal proceedings and regulatory matters

The group is party to legal proceedings and regulatory matters in a number of jurisdictions arising out of its normal business operations. Apart from the matters described below, the group considers that none of these matters are material. The recognition of provisions is determined in accordance with the accounting policies set out in Note 1 of the *Annual Report and Accounts 2018.* While the outcome of legal proceedings and regulatory matters is inherently uncertain, management believes that, based on the information available to it, appropriate provisions have been made in respect of these matters as at 31 December 2018 (see Note 25). Where an individual provision is material, the fact that a provision has been made is stated and quantified, except to the extent that doing so would be seriously prejudicial. Any provision recognised does not constitute an admission of wrongdoing or legal liability. It is not practicable to provide an aggregate estimate of potential liability for our legal proceedings and regulatory matters as a class of contingent liabilities.

Bernard L. Madoff Investment Securities LLC

Bernard L. Madoff ('Madoff') was arrested in December 2008 and later pleaded guilty to running a Ponzi scheme. His firm, Bernard L. Madoff Investment Securities LLC ('Madoff Securities'), is being liquidated in the US by a trustee (the 'Trustee').

Various non-US HSBC companies provided custodial, administration and similar services to a number of funds incorporated outside the US whose assets were invested with Madoff Securities. Based on information provided by Madoff Securities as at 30 November 2008, the purported aggregate value of these funds was $8.4bn, including fictitious profits reported by Madoff.

Based on information available to HSBC, the funds' actual transfers to Madoff Securities minus their actual withdrawals from Madoff Securities during the time HSBC serviced the funds are estimated to have totalled approximately $4bn. Various HSBC companies have been named as defendants in lawsuits arising out of Madoff Securities' fraud.

US litigation: The Trustee has brought lawsuits against various HSBC companies and others in the US Bankruptcy Court, seeking recovery of transfers from Madoff Securities to HSBC in an amount not yet pleaded or determined. HSBC and other parties to the actions have moved to dismiss the Trustee's claims. The US Bankruptcy Court granted HSBC's motion to dismiss with respect to certain of the Trustee's claims in November 2016. In September 2017, the Trustee appealed the US Bankruptcy Court's decision, and the case remains pending before the US Court of Appeals for the Second Circuit (the 'Second Circuit Court of Appeals').

Fairfield Sentry Limited, Fairfield Sigma Limited and Fairfield Lambda Limited (together, 'Fairfield') (in liquidation since July 2009) have brought a lawsuit in the US against fund shareholders, including HSBC companies that acted as nominees for clients, seeking restitution of redemption payments. In December 2018, the US Bankruptcy Court issued an opinion, which ruled in favour of the defendants' motion to dismiss in respect of certain claims by the liquidators for Fairfield and granted a motion by the liquidators for Fairfield to file amended complaints.

In December 2014, SPV Optimal SUS Ltd ('SPV OSUS'), the purported assignee of the Madoff-invested company, Optimal Strategic US Equity Ltd, filed a lawsuit in New York State Court against various HSBC companies and others, seeking damages on various alleged grounds, including breach of fiduciary duty and breach of trust. In April 2018, HSBC transferred the case to the US District Court for the Southern District of New York (the 'New York District Court'). In February 2019, SPV OSUS withdrew its action with prejudice against HSBC.

UK litigation: The Trustee has filed a claim against various HSBC companies in the High Court of England and Wales, seeking recovery of transfers from Madoff Securities to HSBC in an amount not yet pleaded or determined. The deadline for service of the claim has been extended to September 2019 for UK-based defendants and November 2019 for all other defendants.

Cayman Islands litigation: In February 2013, Primeo Fund Limited ('Primeo') (in liquidation since April 2009) brought an action against HSBC Securities Services Luxembourg ('HSSL') and Bank of Bermuda (Cayman) Limited, alleging breach of contract and breach of fiduciary duty and claiming damages and equitable compensation. The trial concluded in February 2017 and, in August 2017, the court dismissed all claims against the defendants. In September 2017, Primeo appealed to the Court of Appeal of the Cayman Islands, and the defendants cross-appealed in respect of certain of the trial court's findings. The appeals are pending before the court for a decision.

Luxembourg litigation: In April 2009, Herald Fund SPC ('Herald') (in liquidation since July 2013) brought an action against HSSL before the Luxembourg District Court, seeking restitution of cash and securities that Herald purportedly lost because of Madoff Securities' fraud,

or money damages. The Luxembourg District Court dismissed Herald's securities restitution claim, but reserved Herald's cash restitution claim and its claim for money damages. Herald has appealed this judgment to the Luxembourg Court of Appeal, where the matter is pending. In late 2018, Herald brought additional claims against HSSL and HSBC Bank plc before the Luxembourg District Court, seeking further restitution and damages.

In October 2009, Alpha Prime Fund Limited ('Alpha Prime') brought an action against HSSL before the Luxembourg District Court, seeking the restitution of securities, or the cash equivalent, or money damages. This action has been temporarily suspended at the plaintiffs' request. In December 2018, Alpha Prime brought additional claims before the Luxembourg District Court seeking damages against various HSBC companies.

In December 2014, Senator Fund SPC ('Senator') brought an action against HSSL before the Luxembourg District Court, seeking restitution of securities, or the cash equivalent, or money damages. In April 2015, Senator commenced a separate action against the Luxembourg branch of HSBC Bank plc asserting identical claims before the Luxembourg District Court. In December 2018, Senator brought additional claims against HSSL and HSBC Bank plc Luxembourg branch before the Luxembourg District Court, seeking restitution of Senator's securities or money damages.

HSSL has also been named as a defendant in various actions by shareholders in Primeo Select Fund, Herald, Herald (Lux) SICAV and Hermes International Fund Limited. Most of these actions have been dismissed, suspended or postponed.

Ireland litigation: In November 2013, Defender Limited brought an action against HSBC Institutional Trust Services (Ireland) Limited ('HTIE') and others, based on allegations of breach of contract and claiming damages and indemnification for fund losses. The trial commenced in October 2018. In December 2018, the Irish High Court issued a judgment in HTIE's favour on a preliminary issue, holding that Defender Limited had no effective claim against HTIE. This judgment concluded the trial without further issues in dispute being heard. In February 2019, Defender Limited appealed the judgment.

In December 2014, SPV OSUS filed an action against HTIE and HSBC Securities Services (Ireland) Limited alleging breach of contract and claiming damages and indemnification for fund losses, which was dismissed on the basis of a preliminary issue by the Irish High Court in October 2015. In July 2018, following further appeals by SPV OSUS, the Irish Supreme Court affirmed the dismissal on a final basis.

There are many factors that may affect the range of possible outcomes, and the resulting financial impact, of the various Madoff-related proceedings described above, including but not limited to the multiple jurisdictions in which the proceedings have been brought. Based upon the information currently available, management's estimate of the possible aggregate damages that might arise as a result of all claims in the various Madoff-related proceedings is up to or exceeding $500m, excluding costs and interest. Due to uncertainties and limitations of this estimate, the ultimate damages could differ significantly from this amount.

Anti-money laundering and sanctions-related matters

In 2010, HSBC Bank USA N.A. ('HSBC Bank USA') entered into a consent cease-and-desist order with the Office of the Comptroller of the Currency ('OCC'), and HSBC North America Holdings Inc. ('HNAH') entered into a consent cease-and-desist order with the Federal Reserve Board ('FRB'). In 2012, HSBC Bank USA further entered into an enterprise-wide compliance consent order with the OCC (each an 'Order' and together, the 'Orders'). These Orders required improvements to establish an effective compliance risk management programme across HSBC's US businesses, including risk management related to the Bank Secrecy Act ('BSA') and anti-money laundering ('AML') compliance. In 2012, an additional consent order was entered into with the OCC that required HSBC Bank USA to correct the circumstances noted in the OCC's report and imposed restrictions on HSBC Bank USA acquiring control of, or holding an interest in, any new financial subsidiary, or commencing a new activity in its existing financial subsidiary, without the OCC's approval. Between June and September 2018, following implementation of the required remediation actions by HNAH and HSBC Bank USA, the FRB and OCC terminated each of these orders.

In December 2012, among other agreements, HSBC Holdings plc ('HSBC Holdings') agreed to an undertaking with the UK Financial Conduct Authority ('FCA') and consented to a cease-and-desist order with the FRB, both of which contained certain forward-looking AML and sanctions-related obligations. HSBC also agreed to retain an independent compliance monitor (who is, for FCA purposes, a 'Skilled Person' under section 166 of the Financial Services and Markets Act and, for FRB purposes, an 'Independent Consultant') to produce periodic assessments of the HSBC Group's AML and sanctions compliance programme (the 'Skilled Person/Independent Consultant'). In December 2012, HSBC Holdings also entered into an agreement with the Office of Foreign Assets Control ('OFAC') regarding historical transactions involving parties subject to OFAC sanctions. The Skilled Person/Independent Consultant will continue to conduct country reviews and provide periodic reports for a period of time at the FCA's and FRB's discretion. The role of the Skilled Person/Independent Consultant is discussed on page 33.

Through the Skilled Person/Independent Consultant's country-level reviews, as well as internal reviews conducted by HSBC, certain potential AML and sanctions compliance issues have been identified that HSBC is reviewing further with the FRB, FCA and/or OFAC. The Financial Crimes Enforcement Network of the US Treasury Department, as well as the Civil Division of the US Attorney's Office for the Southern District of New York, are investigating the collection and transmittal of third-party originator information in certain payments instructed over HSBC's proprietary payment systems. The FCA is also conducting an investigation into HSBC Bank plc's compliance with UK money laundering regulations and financial crime systems and controls requirements. HSBC is cooperating with all of these investigations.

Since November 2014, a number of lawsuits have been filed in federal courts in the US against various HSBC companies and others on behalf of plaintiffs who are, or are related to, victims of terrorist attacks in Iraq. In each case, it is alleged that the defendants aided and abetted the unlawful conduct of various sanctioned parties in violation of the US Anti-Terrorism Act. Seven actions against HSBC Bank plc are currently pending in federal court in New York. In July 2018, in one case, the magistrate judge issued a recommendation that the New York District Court should deny the defendants' motion to dismiss. A motion to dismiss remains pending in one other case in the New York District Court. An action that was pending in federal court in Florida was dismissed by the court in October 2018 without prejudice. In December 2018, three new cases and two cases relating to existing actions were filed in the New York District Court. These new actions are at a very early stage.

Based on the facts currently known, it is not practicable at this time for HSBC to predict the resolution of these matters, including the timing or any possible impact on HSBC, which could be significant.

London interbank offered rates, European interbank offered rates and other benchmark interest rate investigations and litigation

In December 2016, the European Commission (the 'EC') issued a decision finding that HSBC, among other banks, engaged in anti-competitive practices in connection with the pricing of euro interest rate derivatives in early 2007. The EC imposed a fine on HSBC based on a one-month infringement. HSBC has appealed the decision.

US dollar Libor: Beginning in 2011, HSBC and other panel banks have been named as defendants in a number of private lawsuits filed in the US with respect to the setting of US dollar Libor. The complaints assert claims under various US laws, including US antitrust and racketeering laws, the US Commodity Exchange Act ('US CEA') and state law. The lawsuits include individual and putative class actions, most of which have been transferred and/or consolidated for pre-trial purposes before the New York District Court.

In 2017 and 2018, HSBC reached agreements with plaintiffs to resolve putative class actions brought on behalf of the following five groups of plaintiffs: persons who purchased US dollar Libor-indexed bonds; persons who purchased US Libor-indexed exchange-traded instruments; US-based lending institutions that made or purchased US dollar Libor-indexed loans (the 'Lender class'); persons who purchased US dollar Libor-indexed interest rate swaps and other instruments directly from the defendant banks and their affiliates (the 'OTC class'); and persons who purchased US dollar Libor-indexed interest rate swaps and other instruments from certain financial institutions that are not the defendant banks or their affiliates. During 2018, the New York District Court granted final approval of the settlements with the OTC and Lender classes. The remaining settlements are subject to final court approval. Additionally, a number of other US dollar Libor-related actions remain pending against HSBC in the New York District Court and the Second Circuit Court of Appeals.

Intercontinental Exchange ('ICE') Libor: In January 2019, HSBC and other panel banks were named as defendants in a putative class action filed in the New York District Court on behalf of persons who purchased over-the-counter instruments paying interest indexed to ICE Libor from a panel bank. The complaint alleges, among other things, misconduct related to the suppression of this benchmark rate in violation of US antitrust and state law. This matter is at a very early stage.

There are many factors that may affect the range of outcomes, and the resulting financial impact, of these matters, which could be significant.

Foreign exchange-related investigations and litigation

Various regulators and competition authorities around the world, including in the EU, Switzerland, Brazil and South Africa, are conducting investigations and reviews into trading by HSBC and others on the foreign exchange markets. HSBC is cooperating with these investigations and reviews.

In January 2018, HSBC Holdings entered into a three-year deferred prosecution agreement with the Criminal Division of the DoJ (the 'FX DPA'), regarding fraudulent conduct in connection with two particular transactions in 2010 and 2011. This concluded the DoJ's investigation into HSBC's historical foreign exchange activities. Under the terms of the FX DPA, HSBC has a number of ongoing obligations, including implementing enhancements to its internal controls and procedures in its Global Markets business, which will be the subject of annual reports to the DoJ. In addition, HSBC agreed to pay a financial penalty and restitution.

In December 2016, Brazil's Administrative Council of Economic Defense ('CADE') publicly announced that it is initiating an investigation into the onshore foreign exchange market and has identified a number of banks, including HSBC, as subjects of its investigation.

In February 2017, the Competition Commission of South Africa referred a complaint for proceedings before the South African Competition Tribunal against 18 financial institutions, including HSBC Bank plc, for alleged misconduct related to the foreign exchange market in violation of South African antitrust laws. In April 2017, HSBC Bank plc filed an exception to the complaint based on a lack of jurisdiction and statute of limitations. These proceedings are at an early stage.

In October 2018, HSBC Holdings and HSBC Bank plc received an information request from the EC concerning potential coordination in foreign exchange options trading. This matter is at an early stage.

In late 2013 and early 2014, various HSBC companies and other banks were named as defendants in various putative class actions consolidated in the New York District Court. The consolidated complaint alleged, among other things, that the defendants conspired to manipulate the WM/Reuters foreign exchange benchmark rates. In September 2015, HSBC reached an agreement with plaintiffs to resolve the consolidated action, and the court granted final approval of the settlement in August 2018.

A putative class action complaint making similar allegations on behalf of retail customers of foreign exchange products was filed in the US District Court for the Northern District of California in 2015, and was subsequently transferred to the New York District Court where it remains pending. In 2017, putative class action complaints making similar allegations on behalf of purported 'indirect' purchasers of foreign exchange products were filed in New York and were subsequently consolidated in the New York District Court, where they remain pending.

In September 2018, various HSBC companies and other banks were named as defendants in a class action complaint filed in Israel that alleges foreign exchange-related misconduct and, in November and December 2018, complaints alleging foreign exchange-related misconduct were filed in the New York District Court and the High Court of England and Wales against HSBC and other defendants, by certain plaintiffs that opted out of the US class action settlement. In February 2019, various HSBC companies were named as defendants in a claim issued in the High Court of England and Wales that alleges foreign exchange-related misconduct. These matters are at an early stage. It is possible that additional actions will be initiated against HSBC in relation to its historical foreign exchange activities.

As at 31 December 2018, the bank has recognised a provision for these and similar matters in the amount of £168m. There are many factors that may affect the range of outcomes, and the resulting financial impact, of these matters. Due to uncertainties and limitations of these estimates, the ultimate penalties could differ significantly from the amount provided.

Precious metals fix-related investigations and litigation

In November 2014, the Antitrust Division and Criminal Fraud Section of the DoJ issued a document request to HSBC Holdings, seeking the voluntary production of certain documents in connection with a criminal investigation that the DoJ is conducting of alleged anti-competitive and manipulative conduct in precious metals trading. In January 2019, the DoJ closed its investigation without taking any action against HSBC.

Gold: Beginning in March 2014, numerous putative class actions were filed in the New York District Court and the US District Courts for the District of New Jersey and the Northern District of California, naming HSBC and other members of The London Gold Market Fixing

Limited as defendants. The complaints allege that, from January 2004 to June 2013, the defendants conspired to manipulate the price of gold and gold derivatives for their collective benefit in violation of US antitrust laws, the US CEA and New York state law. The actions were consolidated in the New York District Court. The defendants' motion to dismiss the consolidated action was granted in part and denied in part in October 2016. In June 2017, the court granted the plaintiffs leave to file a third amended complaint, naming a new defendant. The court has denied the pre-existing defendants' request for leave to file a joint motion to dismiss, and discovery is proceeding.

Beginning in December 2015, numerous putative class actions under Canadian law were filed in the Ontario and Quebec Superior Courts of Justice against various HSBC companies and other financial institutions. The plaintiffs allege that, among other things, from January 2004 to March 2014, the defendants conspired to manipulate the price of gold and gold derivatives in violation of the Canadian Competition Act and common law. These actions are at an early stage.

Silver: Beginning in July 2014, numerous putative class actions were filed in the US District Courts for the Southern and Eastern Districts of New York, naming HSBC and other members of The London Silver Market Fixing Ltd as defendants. The complaints allege that, from January 2007 to December 2013, the defendants conspired to manipulate the price of silver and silver derivatives for their collective benefit in violation of US antitrust laws, the US CEA and New York state law. The actions were consolidated in the New York District Court. The defendants' motion to dismiss the consolidated action was granted in part and denied in part in October 2016. In June 2017, the court granted the plaintiffs leave to file a third amended complaint, which names several new defendants. The court has denied the pre-existing defendants' request for leave to file a joint motion to dismiss, and discovery is proceeding.

In April 2016, two putative class actions under Canadian law were filed in the Ontario and Quebec Superior Courts of Justice against various HSBC companies and other financial institutions. The plaintiffs in both actions allege that, from January 1999 to August 2014, the defendants conspired to manipulate the price of silver and silver derivatives in violation of the Canadian Competition Act and common law. The Ontario action is at an early stage. The Quebec action has been temporarily stayed.

Platinum and palladium: Between late 2014 and early 2015, numerous putative class actions were filed in the New York District Court, naming HSBC and other members of The London Platinum and Palladium Fixing Company Limited as defendants. The complaints allege that, from January 2008 to November 2014, the defendants conspired to manipulate the price of platinum group metals ('PGM') and PGM-based financial products for their collective benefit in violation of US antitrust laws and the US CEA. In March 2017, the defendants' motion to dismiss the second amended consolidated complaint was granted in part and denied in part. In June 2017, the plaintiffs filed a third amended complaint. The defendants filed a joint motion to dismiss, which remains pending.

Based on the facts currently known, it is not practicable at this time for HSBC to predict the resolution of these matters, including the timing or any possible impact on HSBC, which could be significant.

Other regulatory investigations, reviews and litigation

HSBC Bank plc and/or certain of its affiliates are subject to a number of other investigations and reviews by various regulators and competition and law enforcement authorities, as well as litigation, in connection with various matters relating to the firm's businesses and operations, including:

- an investigation by the Swiss Competition Commission in connection with the setting of Euribor and Japanese yen Libor;
- an information request from the UK Competition and Markets Authority concerning the financial services sector;
- putative individual and class actions brought in the New York District Court relating to the Canadian dealer offered rate, the credit default swap market and the Mexican government bond market, and putative class actions brought in the New York District Court and in the Superior and Federal Courts in Canada relating to the market for US dollar-denominated supranational sovereign and agency bonds; and
- putative class actions brought in the US District Court for the Northern District of Texas and a claim issued in the High Court of England and Wales in connection with HSBC Bank plc's role as a correspondent bank to Stanford International Bank Ltd from 2003 to 2009.

There are many factors that may affect the range of outcomes, and the resulting financial impact, of these matters, which could be significant.

33 Related party transactions

The immediate parent company of the group is HSBC UK Holdings Limited and the ultimate parent company is HSBC Holdings plc, both of which are incorporated in England.

Copies of the Group financial statements may be obtained from the following address:

HSBC Holdings plc

8 Canada Square

London E14 5HQ

IAS 24 'Related party disclosures' defines related parties as including the parent, fellow subsidiaries, associates, joint ventures, post-employment benefit plans for HSBC employees, Key Management Personnel ('KMP') of the group and its ultimate parent company, close family members of the KMP and entities which are controlled, jointly controlled or significantly influenced by the KMP or their close family members.

Particulars of transactions between the group and the related parties are tabulated below. The disclosure of the year-end balance and the highest amounts outstanding during the year are considered to be the most meaningful information to represent the amount of the transactions and outstanding balances during the year.

Key Management Personnel

The KMP of the bank are defined as those persons having authority and responsibility for planning, directing and controlling the activities of the bank. They include the Directors of HSBC Bank plc, and Directors and certain Group Managing Directors of HSBC Holdings plc, to the extent they have a role in directing the affairs of the bank.

A number of the bank's KMP are not Directors of the group, but are Directors or Group Managing Directors of HSBC Holdings plc. The emoluments of these KMP are paid by other members of the Group who make no recharge to the bank. It is not possible to make a reasonable apportionment of their emoluments in respect of the bank. Accordingly, no emoluments in respect of these KMP are included in the following disclosure.

The tables below represent the compensation for Directors of the bank in exchange for services rendered to the bank for the period they served during the year.

Compensation of Key Management Personnel

	2018	2017
	£000	£000
Short-term employee benefits	3,115	3,816
Post-employment benefits	4	10
Other long-term employee benefits	136	441
Share-based payments	801	1,359
Year ended 31 Dec	4,056	5,626

Transactions and balances during the year with Key Management Personnel of the bank

	2018 [4]		2017 [5]	
	Balance at 31 Dec[2]	Highest amounts outstanding during year[3]	Balance at 31 Dec	Highest amounts outstanding during year
	£m	£m	£m	£m
Key Management Personnel[1]				
Advances and credits[2]	2	4	19	24
Guarantees	—	—	—	—
Deposits	29	60	27	53

1 *Includes close family members and entities which are controlled or jointly controlled by KMP of the bank or their close family members.*
2 *Exchange rate applied for non-GBP amounts is at 31 December 2018.*
3 *Exchange rate applied for non-GBP amounts is the average for the year.*
4 *2018 excludes the qualifying components of the bank's RBWM UK, CMB UK and GPB UK businesses following ring-fencing in July 2018.*
5 *The 2017 amounts have been restated to just include transactions and balances between the KMP and the group.*

The above transactions were made in the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with persons of a similar standing or, where applicable, with other employees. The transactions did not involve more than the normal risk of repayment or present other unfavourable features.

In addition to the requirements of IAS 24, particulars of advances (loans and quasi-loans), credits and guarantees entered into by the group with Directors of HSBC Bank plc are required to be disclosed pursuant to section 413 of the Companies Act 2006. Under the Companies Act, there is no requirement to disclose transactions with KMP of the bank's ultimate parent company, HSBC Holdings plc.

Transactions with Directors: advances, credits and guarantees (Companies Act 2006)

	2018	2017
	Balance at 31 Dec	Balance at 31 Dec
	£000	£000
Directors		
Loans	265	1,564
Guarantees	—	—

Other related parties

Transactions and balances during the year with KMP of the bank's ultimate parent company

During the course of 2017 and 2018, there were no transactions and balances between KMP of the bank's ultimate parent company, who were not considered KMP of the bank, in respect of Advances and Credits, Guarantees and Deposits.

Transactions and balances during the year with associates and joint ventures

	2018		2017	
	Highest balance during the year	Balance at 31 Dec	Highest balance during the year	Balance at 31 Dec
	£m	£m	£m	£m
Unsubordinated amounts due from joint ventures[1]	102	—	102	88
Subordinated amounts due from associates	—	—	304	304
Guarantees and commitments[1]	610	—	480	480

1 *Impacted by the transfers to HSBC UK Bank plc under the ring-fence implementation. For further information see Note 35 Discontinued operations.*

The group provides certain banking and financial services to associates and joint ventures, including loans, overdrafts, interest and non-interest bearing deposits and current accounts. Details of the interests in associates and joint ventures are given in Notes 17 and 37.

The group's transactions and balances during the year with HSBC Holdings plc and subsidiaries of HSBC Holdings plc

	2018				2017			
	Due to/from HSBC Holdings plc		Due to/from subsidiaries of HSBC Holdings plc		Due to/from HSBC Holdings plc		Due to/from subsidiaries of HSBC Holdings plc	
	Highest balance during the year	31 Dec	Highest balance during the year	Balance at 31 Dec	Highest balance during the year	31 Dec	Highest balance during the year	Balance at 31 Dec
	£m	£m	£m	£m	£m	£m	£m	£m
Assets								
Trading assets	351	24	4,725	276	888	351	13,367	4,725
Derivatives	2,651	1,685	20,224	18,135	—	—	29,439	18,993
Financial assets designated at fair value	15	7	201	198	20	15	4	2
Loans and advances to banks	—	—	6,703	2,780	—	—	13,450	3,958
Loans and advances to customers	924	—	3,610	539	1,500	924	4,366	3,610
Financial investments	238	229	28	—	250	238	29	28
Total related party assets at 31 Dec	4,179	1,945	35,491	21,928	2,658	1,528	60,655	31,316
Liabilities								
Trading liabilities	968	303	18,634	1,114	2,650	968	28,316	18,634
Financial liabilities designated at fair value	2,167	1,183	68	66	2,161	2,161	—	—
Deposits by banks	—	—	8,647	2,859	1	—	5,460	4,901
Customer accounts	15,024	2,708	5,095	1,716	26,291	15,001	7,316	5,095
Derivatives	770	559	21,145	17,594	—	—	24,693	18,923
Subordinated liabilities	13,444	6,060	4,230	4,230	13,279	13,279	222	—
Total related party liabilities at 31 Dec	32,373	10,813	57,819	27,579	44,382	31,409	66,007	47,553
Guarantees and commitments	—	—	482	397	—	—	503	472

	Due to/from HSBC Holdings plc		Due to/from subsidiaries of HSBC Holdings plc	
	2018	2017	2018	2017
	£m	£m	£m	£m
Income statement				
Interest income	6	—	119	53
Interest expense	448	481	141	81
Fee income	13	17	95	98
Dividend income	—	—	—	—
Fee expense	—	—	387	377
Trading income	—	16	5	212
Trading expense	3	—	125	—
Other operating income	97	276	316	383
General and administrative expenses	67	45	2,719	3,997

The above outstanding balances arose in the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with third-party counterparties.

The bank's transactions and balances during the year with HSBC Bank plc subsidiaries, HSBC Holdings plc and subsidiaries of HSBC Holdings plc

	2018						2017					
	Due to/from subsidiaries of HSBC Bank plc subsidiaries		Due to/from HSBC Holdings plc		Due to/from subsidiaries of HSBC Holdings plc		Due to/from subsidiaries of HSBC Bank plc subsidiaries		Due to/from HSBC Holdings plc		Due to/from subsidiaries of HSBC Holdings plc	
	Highest balance during the year	Balance at 31 Dec	Highest balance during the year	Balance at 31 Dec	Highest balance during the year	Balance at 31 Dec	Highest balance during the year	Balance at 31 Dec	Highest balance during the year	Balance at 31 Dec	Highest balance during the year	Balance at 31 Dec
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Assets												
Trading assets	**3,547**	**1,051**	**351**	**24**	**4,403**	**276**	8,463	3,547	888	351	13,053	4,403
Derivatives	**11,668**	**11,557**	**2,651**	**1,685**	**29,257**	**17,329**	13,269	10,989	—	—	41,702	29,257
Loans and advances to banks	**7,491**	**4,142**	**—**	**—**	**6,570**	**2,650**	6,331	5,786	—	—	8,922	3,570
Loans and advances to customers	**15,422**	**7,444**	**911**	**—**	**3,594**	**539**	15,644	14,467	1,496	911	4,350	3,594
Financial investments	**820**	**185**	**—**	**—**	**—**	**—**	1,329	820	—	—	—	—
Total related party assets at 31 Dec	**38,948**	**24,379**	**3,913**	**1,709**	**43,824**	**20,794**	45,036	35,609	2,384	1,262	68,027	40,824
Liabilities												
Trading liabilities	**679**	**—**	**968**	**303**	**18,543**	**1,114**	8,246	679	2,650	968	27,925	18,543
Deposits by banks	**4,777**	**2,542**	**—**	**—**	**8,164**	**2,104**	14,162	4,777	—	—	5,061	4,666
Customer accounts	**1,410**	**922**	**15,024**	**2,708**	**4,997**	**1,705**	3,075	1,410	26,282	14,984	7,209	4,997
Derivatives	**12,444**	**12,309**	**770**	**559**	**34,043**	**16,709**	15,603	12,332	—	—	42,337	34,043
Subordinated liabilities	**700**	**700**	**13,137**	**5,827**	**4,230**	**4,230**	700	696	12,970	12,970	—	—
Total related party liabilities at 31 Dec	**20,010**	**16,473**	**29,899**	**9,397**	**69,977**	**25,862**	41,786	19,894	41,902	28,922	82,532	62,249
Guarantees and commitments	**1,502**	**1,475**	**—**	**—**	**361**	**273**	1,498	1,498	—	—	359	359

The above outstanding balances arose in the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with third-party counterparties.

Post-employment benefit plans

The HSBC Bank (UK) Pension Scheme (the 'Scheme') entered into swap transactions with the bank to manage the inflation and interest rate sensitivity of the liabilities. At 31 December 2018, the gross notional value of the swaps was £8,250m (2017: £8,345m), the swaps had a negative fair value of £810m to the bank (2017: negative fair value of £745m) and the bank had delivered collateral of £801m (2017: £745m) to the Scheme in respect of these swaps. All swaps were executed at prevailing market rates and within standard market bid/ offer spreads.

34 Effects of reclassifications upon adoption of IFRS 9

Reconciliation of consolidated balance sheet at 31 December 2017 and 1 January 2018

						IFRS 9 reclassification to					
	Footnotes	IAS 39 measurement category	IFRS 9 measurement category	IAS 39 carrying amount at 31 Dec 2017	Other changes in classification	Fair value through profit and loss	Fair value through other comprehensive income	Amortised cost	Carrying amount post reclassification	IFRS 9 remeasurement including expected credit losses	IFRS 9 carrying amount at 1 Jan 2018
				£m	£m	£m	£m	£m	£m	£m	£m
Assets											
Cash and balances at central banks		Amortised cost	Amortised cost	97,601	—	—	—	—	97,601	(1)	97,600
Items in the course of collection from other banks		Amortised cost	Amortised cost	2,023	—	—	—	—	2,023	—	2,023
Trading assets	1, 2	FVPL	FVPL	145,725	(156)	—	—	(26,447)	119,122	—	119,122
Financial assets designated and otherwise mandatorily measured at fair value through profit or loss	2,3	FVPL	FVPL	9,266	156	5,567	—	—	14,989	6	14,995
Derivatives		FVPL	FVPL	143,335	—	—	—	—	143,335	—	143,335
Loans and advances to banks	1, 3	Amortised cost	Amortised cost	14,149	(731)	(193)	—	—	13,225	(6)	13,219
Loans and advances to customers	1, 3, 4	Amortised cost	Amortised cost	280,402	(3,277)	(2,514)	—	—	274,611	(652)	273,959
Reverse repurchase agreements – non-trading		Amortised cost	Amortised cost	45,808	—	—	—	—	45,808	—	45,808
Financial investments	5	FVOCI (Available-for-sale – debt instruments)	FVOCI	57,338	—	(2,287)	—	(6)	55,045	—	55,045
	6	FVOCI (Available-for-sale – equity instruments)	FVOCI	662	—	(573)	—	—	89	—	89
	5	Amortised cost	Amortised cost	—	—	—	—	6	6	—	6
Prepayments, accrued income and other assets	1	Amortised cost	Amortised cost	16,026	4,008	—	—	26,447	46,481	(1)	46,480
Current tax assets		N/A	N/A	140	—	—	—	—	140	—	140
Interests in associates and joint ventures		N/A	N/A	327	—	—	—	—	327	—	327
Goodwill and intangible assets		N/A	N/A	5,936	—	—	—	—	5,936	—	5,936
Deferred tax assets		N/A	N/A	130	—	—	—	—	130	34	164
Total assets				818,868	—	—	—	—	818,868	(620)	818,248

For footnotes, see page 161.

Reconciliation of consolidated balance sheet at 31 December 2017 and 1 January 2018 (continued)

	Footnotes	IFRS 9 measurement category	IAS 39 carrying amount at 31 Dec 2017	Other changes in classification	IFRS 9 reclassification to: Fair value through profit and loss	Fair value through other comprehensive income	Amortised cost	Carrying amount post reclassification	IFRS 9 re-measurement including expected credit losses	IFRS 9 carrying amount at 1 Jan 2018
			£m	£m	£m	£m	£m	£m	£m	£m
Liabilities										
Deposits by banks	1	Amortised cost	29,349	(178)	–	–	–	29,171	–	29,171
Customer accounts	1	Amortised cost	381,546	(3,240)	–	–	–	378,306	–	378,306
Repurchase agreements – non-trading		Amortised cost	37,775	–	–	–	–	37,775	–	37,775
Items in the course of transmission to other banks		Amortised cost	1,089	–	–	–	–	1,089	–	1,089
Trading liabilities	1, 8	FVPL	106,496	(48,713)	–	–	–	57,783	–	57,783
Financial liabilities designated at fair value	7, 8	FVPL	18,249	17,958	–	–	(274)	35,933	–	35,933
Derivatives		FVPL	140,070	–	–	–	–	140,070	–	140,070
Debt securities in issue		Amortised cost	13,286	–	–	–	–	13,286	–	13,286
Accruals, deferred income and other liabilities	1	Amortised cost	6,615	34,173	–	–	–	40,788	–	40,788
Current tax liabilities		N/A	88	–	–	–	–	88	–	88
Liabilities under insurance contracts		N/A	21,033	–	–	–	–	21,033	–	21,033
Provisions	4	N/A	1,796	–	–	–	–	1,796	104	1,900
Deferred tax liabilities		N/A	933	–	–	–	–	933	(140)	793
Subordinated liabilities	7	Amortised cost	16,494	–	–	–	274	16,768	(52)	16,716
Total liabilities			774,819	–	–	–	–	774,819	(88)	774,731

For footnotes, see page 161.

Reconciliation of consolidated balance sheet at 31 December 2017 and 1 January 2018 (continued)

	Footnotes	IAS 39 carrying amount at 31 Dec 2017	IFRS 9 reclassification	Carrying amount post reclassification	IFRS 9 remeasurement including expected credit losses	Carrying amount at 1 January 2018
		£m	£m	£m	£m	£m
Equity						
Called up share capital		797	–	797	–	797
Other equity instruments		3,781	–	3,781	–	3,781
Other reserves	9	2,744	(192)	2,552	(57)	2,495
Retained earnings	9	36,140	192	36,332	(475)	35,857
Total Shareholders' equity		43,462	–	43,462	(532)	42,930
Non-controlling interests		587	–	587	–	587
Total equity		44,049	–	44,049	(532)	43,517

For footnotes, see page 161.

Reconciliation of impairment allowances under IAS 39 and provisions under IAS 37 to expected credit losses under IFRS 9

		Reclassification to			Remeasurement		
	IAS 39 measurement category	Fair value through profit or loss	Fair value through other comprehensive income	Amortised cost	Stage 3	Stage 1 & Stage 2	Total
		£m	£m	£m	£m	£m	£m
Financial assets at amortised cost							
IAS 39 impairment allowances at 31 Dec 2017							2,243
Cash and balances at central banks	Amortised cost (Loans and receivables)	–	–	–	–	1	1
Items in the course of collection from other banks	Amortised cost (Loans and receivables)	–	–	–	–	–	–
Loans and advances to banks	Amortised cost (Loans and receivables)	–	–	–	–	6	6
Loans and advances to customers	Amortised cost (Loans and receivables)	–	–	–	187	465	652
Reverse repurchase agreements – non-trading	Amortised cost (Loans and receivables)	–	–	–	–	–	–
Prepayments, accrued income and other assets	Amortised cost (Loans and receivables)	–	–	–	–	1	1
Expected credit loss allowances at 1 Jan 2018							**2,903**
Loan commitments and financial guarantee contracts							
IAS 37 provisions at 31 Dec 2017							55
Provisions (loan commitments and financial guarantees)	N/A	N/A	N/A	N/A	30	74	104
Expected credit loss provisions at 1 Jan 2018							**159**

The pre-tax net asset impact of additional impairment allowances on adoption of IFRS 9 is £764m; £660m in respect of financial assets at amortised cost and £104m related to loan commitments and financial guarantee contracts. The total expected credit loss allowance at 1 January 2018 is £2,903m in respect of financial assets at amortised cost and £159m related to loan commitments and financial guarantee contracts.

Effects of reclassification upon adoption of IFRS 9

				Assuming no reclassification		
	Footnotes	Carrying amount at 31 Dec 2018	Fair value at 31 Dec 2018	Fair value gains recognised in profit or loss	Fair value gains recognised in other comprehensive income	Interest revenue/ (expense) recognised
		£m	£m	£m	£m	£m
Reclassified from available-for-sale to amortised cost						
Other financial assets held at amortised cost		5	5	N/A	–	N/A
Reclassified from fair value through profit and loss to amortised cost or fair value though other comprehensive income						
Subordinated liabilities	10	235	279	27	5	(23)

For footnotes, see page 161.

Footnotes to Effects of reclassifications upon adoption of IFRS 9

1 *Cash collateral, margin and settlement accounts of £26,447m have been reclassified from 'Trading assets' to 'Prepayments, accrued income and other assets' as a result of the assessment of business models in accordance with IFRS 9. Cash collateral, margin and settlement accounts previously presented as 'Loans and advances to banks' of £573m and 'Loans and advances to customers' of £394m have been represented in 'Prepayments, accrued income and other assets' to ensure consistent presentation of all such balances. Cash collateral, margin and settlement accounts previously presented as 'Trading liabilities' of £30,755m, 'Deposits by banks' of £570m, and 'Customer accounts' of £548m have been represented in 'Accruals, deferred income and other liabilities'. This change in presentation for financial liabilities is considered to provide more relevant information, given the change in presentation for the financial assets. In addition, intragroup trade receivables have been reclassified from 'Loans and advances to banks' and 'Loans and advances to customers' to 'Prepayments, accrued income and other assets' and intragroup trade payables have been reclassified from 'Deposits from banks' and 'Customer accounts' to 'Accruals, deferred income and other liabilities'.*

2 *Default fund contributions of £156m have been reclassified from 'Trading assets' to 'Financial assets designated and otherwise mandatorily measured at fair value through profit or loss', as contrary to the assets mentioned in footnote 1 above, they did not meet the 'solely payments of principal and interest' ('SPPI') requirement for amortised cost classification under IFRS 9.*

3 *'Loans and advances to customers' of £2,514m and 'Loans and advances to banks' of £193m did not meet the SPPI requirement for amortised cost classification under IFRS 9. As a result, these financial assets were reclassified to 'Financial assets designated and otherwise mandatorily measured at fair value through profit or loss'. This resulted in a £6m upward remeasurement of the financial assets now measured at fair value.*

4 *IFRS 9 expected credit losses have decreased net assets by £764m, principally comprising of a £652m reduction in the carrying value of assets classified as 'Loans and advances to customers' and a £104m increase in 'Provisions' relating to expected credit losses on loan commitments and financial guarantee contracts.*

5 *Debt instruments of £2,287m, previously classified as available-for-sale under IAS 39, did not meet the SPPI requirement for FVOCI classification. As a result, these financial assets were classified as 'Financial assets designated and otherwise mandatorily measured at fair value through profit or loss' upon adoption of IFRS 9. Debt instruments of £6m, previously classified as available-for-sale under IAS 39, have been reclassified to amortised cost as a result of a 'hold to collect' business model classification under IFRS 9.*

6 *£573m of available-for-sale non-traded equity instruments have been reclassified as 'Financial assets designated and otherwise mandatorily measured at fair value through profit or loss' in accordance with IFRS 9. The group has elected to apply the FVOCI option under IFRS 9 for the remaining £89m.*

7 *As required by IFRS 9, the fair value designation of subordinated liabilities of £274m has been revoked since an accounting mismatch no longer exists. This resulted in these liabilities now being measured at amortised cost, decreasing 'Subordinated liabilities' by £52m.*

8 *We have considered market practices for the presentation of £17,958m of financial liabilities which contain both deposit and derivative components. We have concluded that a change in accounting policy and presentation from 'Trading liabilities' would be appropriate, since it would better align with the presentation of similar financial instruments by peers and therefore provide more relevant information about the effect of these financial liabilities on our financial position and performance. As a result, rather than being classified as held for trading, these liabilities are classified as 'Financial liabilities designated at fair value' from 1 January 2018.*

9 *While IFRS 9 expected credit losses have no effect on the carrying value of FVOCI debt instruments, which remain measured at fair value, the adoption of IFRS 9 resulted in a transfer of £57m between the FVOCI reserve (formerly AFS reserve) and 'Retained earnings' to reflect the difference between the cumulative impairment recognised in profit or loss in accordance with IFRS 9 and the cumulative impairment losses previously recognised in profit or loss under IAS 39. The resulting cumulative expected credit losses recognised in 'Retained earnings' on financial assets measured at FVOCI on adoption of IFRS 9 is £166m. In addition, the cumulative AFS reserve relating to financial investments reclassified to 'Financial assets designated and otherwise mandatorily measured at fair value through profit or loss' in accordance with IFRS 9 has been transferred to 'Retained earnings'.*

10 *The effective interest rate on subordinated liabilities reclassified at 1 January 2018 was 7.69%.*

35 Discontinued operations

To meet HSBC Holdings plc's UK ring-fencing obligations in accordance with the UK Banking Reform Act, on 1 July 2018, HSBC Bank plc's UK Retail Banking and Wealth Management (RBWM), Commercial Banking (CMB) and Global Private Banking (GPB), were legally separated into a ring-fenced bank, HSBC UK Bank plc. This legal separation resulted in the demerger of the ring-fenced businesses in accordance with the application made to the High Court. The transfer of the various assets and liabilities making up the ring-fenced bank followed a variety of legal mechanisms (the most significant mechanism being a transfer under Part VII of the Financial Services and Markets Act 2000).

The establishment of HSBC UK Bank plc was accounted for as a group restructuring. The series of transactions that comprised UK ring fencing were not designed to deliver economic benefits from changes in business activities, but represent a re-arrangement of the organisation of business activities across legal entities under the common control of HSBC Holdings plc in its capacity as the ultimate shareholder in order to be compliant with the relevant regulations.

HSBC's accounting policy required that assets and liabilities were recognised at their existing carrying amounts. The transfers to HSBC UK Bank plc were therefore at the 1 July 2018 carrying value of HSBC Bank plc. Equity reserves were not recycled through profit or loss, and were transferred to, and accounted for on the same basis by HSBC UK Bank plc. HSBC Bank plc reports the transferred business as discontinued operations. There was no gain or loss on disposal.

The 2018 results represent the six months to 30 June 2018, and the 2017 results are for the year ended 31 December 2017.

Discontinued operations income statement

	2018	2017
	£m	£m
Net operating income[1, 2]	**3,037**	5,767
Total operating expenses[2,3]	**(1,894)**	(4,635)
Operating profit	**1,143**	1,132
Profit before tax	**1,143**	1,132
Tax expense	**(323)**	(330)
Profit for the year	**820**	802
Profit from discontinued operations attributable to shareholders of the parent company	**820**	802
Profit/(loss) for the year attributable to non-controlling interests	**—**	—

1 *Includes operating income for RBWM, CMB and GPB, adjusted to exclude CMB operating income for customers not transferred to HSBC UK Bank plc.*
2 *Includes a portion of Global Foreign Exchange (GFX) and 50% of BSM operating income and operating expenses for 2017 and the first four months of 2018; until the establishment of separate BSM and GFX functions for HSBC UK Bank plc.*
3 *Includes 100% of costs to establish the UK ring-fenced bank of £251m in 2017 and an apportionment of the costs to achieve not assigned to a specific global business. Costs of establishment apportioned to HSBC UK Bank plc are on the basis that they were incurred to launch HSBC UK Bank plc retail and commercial business in the UK, in order to meet regulatory requirements on ring-fencing.*

Statement of other comprehensive income from discontinued operations

	2018	2017
	£m	£m
Available-for-sale investments[1]	N/A	—
Debt instruments at fair value through other comprehensive income	5	N/A
Foreign exchange reserve	(3)	—
Cash flow hedges[2]	(30)	(75)
Remeasurement of defined benefit asset/liability[3]	178	1,791
Other comprehensive loss, net of tax	**150**	1,716

1 Nil available-for-sale reserve was assigned to discontinued operations as no available-for-sale reserve was transferred to HSBC UK Bank plc on 1 July 2018.
2 The 2017 portion of cash flow hedging reserve was assigned based on currency and maturity because the separate BSM functions were not established until the second quarter of 2018.
3 The remeasurement of defined benefit asset/liability was recognised entirely in discontinued operations.

Cash flows from discontinued operations

	2018	2017
Cash flows from discontinued operations[1]	£m	£m
Net cash from operating activities	7,258	6,770
Net cash from investing activities	(1,296)	(624)
Net cash from financing activities	(946)	(2,809)
Net cash flows for the year	**5,016**	3,337

1 Net cash flows were approximated by summarising the movements from the ring-fenced bank balance sheets for December 2016 and December 2017 and the opening balance sheet at 1 July 2018. The 2016 and 2017 balance sheets were compiled by separating the qualifying components of HSBC Bank plc from the consolidated balance sheet including;
i) HSBC Bank plc's UK RBWM, CMB and GPB businesses;
ii) the qualifying subsidiaries most notably Marks and Spencer Financial Services plc, HSBC Private Bank (UK) Limited and a number of asset finance entities; and
iii) the transfer of HSBC Bank plc's excess reserves to HSBC UK Bank plc via a capital contribution.
The assumptions applied in preparing these balance sheets include:
a) other third party assets and liabilities and provisions were apportioned to the ring-fenced bank based on the underlying businesses to which the balances related;
b) derivative assets and liabilities included in the balance sheets related solely to hedging instruments used to hedge the ring-fenced bank's own risk;
c) no current tax was included in the balance sheets;
d) deferred tax was apportioned according to the related assets being transferred;
e) the surplus on the UK principal defined benefit plan has been recognised entirely within the ring-fenced bank balance sheet;
f) the balance sheets were prepared as though the capital injection and transfer of reserves had occurred as at the respective reporting dates;
g) intergroup payables and receivables created on separation were not included in the balance sheets at which time these were eliminated on consolidation; and
h) the approximated split of cash and financial investments were apportioned based on the actual split at 1 July 2018.

36 Events after the balance sheet date

A second interim dividend for 2018 of £406m to the shareholder of the parent company was declared on 12 February 2019 by the Directors and will be payable on 26 February 2019. A special dividend of £674m was declared after 31 December 2018 on the ordinary share capital of HSBC Bank plc in respect of 2018 and will be payable on 26 February 2019.

On 1 February 2019, the activities of HSBC Bank plc's branches in Belgium, the Netherlands, Spain, Italy, Ireland and Czech Republic were transferred to new branches of HSBC France in those countries.

In its assessment of events after the balance sheet date, HSBC considered, among others, the events related to the process of the UK's withdrawal from the European Union that occurred between 31 December 2018 and the date when the financial statements were authorised for issue, and concluded that no adjustments to the financial statements were required.

37 HSBC Bank plc's subsidiaries, joint ventures and associates

In accordance with section 409 of the Companies Act 2006 a list of HSBC Bank plc subsidiaries, joint ventures and associates, the registered office address and the effective percentage of equity owned at 31 December 2018 is disclosed below.

Unless otherwise stated, the share capital comprises ordinary or common shares which are held by HSBC Bank plc subsidiaries. The ownership percentage is provided for each undertaking. The undertakings below are consolidated by HSBC Bank plc unless otherwise indicated.

Subsidiaries

The undertakings below are consolidated by the group.

Subsidiaries	% of share class held by immediate parent company (or by HSBC Bank plc where this varies)		Footnotes
Assetfinance December (H) Limited	100.00		15
Assetfinance December (M) Limited	100.00		15
Assetfinance December (P) Limited	100.00		2, 15
Assetfinance December (R) Limited	100.00		15
Assetfinance June (A) Limited	100.00		15
Assetfinance Limited	100.00		15
Assetfinance March (B) Limited	100.00		16
Assetfinance March (F) Limited	100.00		15
Assetfinance September (F) Limited	100.00		15
Banco Nominees (Guernsey) Limited	100.00		17
Banco Nominees 2 (Guernsey) Limited	100.00		17
Beau Soleil Limited Partnership	n/a		7, 18
Billingsgate Nominees Limited	100.00		2, 15
Canada Crescent Nominees (UK) Limited	100.00		2, 15
Canada Water Nominees (UK) Limited (in liquidation)	100.00		2, 15
CCF & Partners Asset Management Limited	99.99		15
CCF Charterhouse GmbH & Co Asset Leasing KG (in liquidation)	n/a		7, 19
CCF Charterhouse GmbH (in liquidation)	100.00	(99.99)	4, 19
CCF Holding (LIBAN) S.A.L. (in liquidation)	74.99		1, 20
Charterhouse Administrators (D.T.) Limited	100.00	(99.99)	15
Charterhouse Development Limited (in liquidation)	100.00		21
Charterhouse Management Services Limited	100.00	(99.99)	15
Charterhouse Pensions Limited	100.00		2, 15
CL Residential Limited (in liquidation)	100.00		21
COIF Nominees Limited	n/a		2, 7, 15
Corsair IV Financial Services Capital Partners	n/a		7, 73
Dem 5	100.00	(99.99)	4, 22
Dem 9	100.00	(99.99)	4, 22
Dempar 1	100.00	(99.99)	4, 23
Dempar 4	100.00	(99.99)	4, 23
Elysees GmbH (in liquidation)	100.00	(99.99)	11, 19
Elysées Immo Invest	100.00	(99.99)	4, 24
Equator Holdings Limited (in liquidation)	100.00		2, 15
Eton Corporate Services Limited	100.00		17
Fdm 5 SAS	100.00	(99.99)	4, 22
Finanpar 2	100.00	(99.99)	4, 24
Finanpar 7	100.00	(99.99)	4, 24
Flandres Contentieux S.A.	100.00	(99.99)	1, 4, 25
Foncière Elysées	100.00	(99.99)	4, 23
Forward Trust Rail Services Limited (in liquidation)	100.00		15
Griffin International Limited	100.00		15
Grundstuecksgesellschaft Trinkausstrasse Kommanditgesellschaft	n/a		7, 26
Hg Janus A Co-Invest L.P.	n/a		7, 74
HITG Administration GmbH	100.00		2, 27
Hongkong International Trade Finance (Holdings) Limited (in liquidation)	100.00		2, 15
HSBC (BGF) Investments Limited	100.00		2, 15
HSBC Alpha Funding (UK) Holdings LP (in liquidation)	n/a		2, 7, 28
HSBC Asset Finance (UK) Limited	100.00		2, 15
HSBC Asset Finance Holdings Limited (in liquidation)	100.00		2, 15
HSBC Asset Finance M.O.G. Holdings (UK) Limited	100.00		2, 15
HSBC Assurances Vie (France)	100.00	(99.99)	4, 25
HSBC Bank (General Partner) Limited	100.00		2, 29
HSBC Bank (RR) (Limited Liability Company)	100.00		13, 30
HSBC Bank Armenia cjsc	70.00		31
HSBC Bank Capital Funding (Sterling 1) LP	n/a		7, 29
HSBC Bank Capital Funding (Sterling 2) LP	n/a		7, 29
HSBC Bank Malta p.l.c.	70.03		32
HSBC Bank Nominee (Jersey) Limited	100.00		2, 33
HSBC Bank Pension Trust (UK) Limited	100.00		2, 15

Subsidiaries	% of share class held by immediate parent company (or by HSBC Bank plc where this varies)		Footnotes
HSBC Bank Polska S.A.	100.00		3, 34
HSBC City Funding Holdings	100.00		15
HSBC Client Holdings Nominee (UK) Limited	100.00		2, 15
HSBC Corporate Trustee Company (UK) Limited	100.00		2, 15
HSBC Custody Services (Guernsey) Limited	100.00		17
HSBC Enterprise Investment Company (UK) Limited	100.00		2, 15
HSBC Epargne Entreprise (France)	100.00	(99.99)	4, 25
HSBC Equator (UK) Limited (in liquidation)	100.00		15
HSBC Equity (UK) Limited	100.00		2, 15
HSBC Europe B.V.	100.00		15
HSBC Factoring (France)	100.00	(99.99)	4, 23
HSBC France	99.99		2, 4, 23
HSBC Funding (UK) Holdings (active proposal to strike off)	100.00		15
HSBC Germany Holdings GmbH	100.00		2, 26
HSBC Global Asset Management (Deutschland) GmbH	100.00	(80.67)	26
HSBC Global Asset Management (France)	100.00	(99.99)	4, 35
HSBC Global Asset Management (International) Limited (in liquidation)	100.00		2, 36
HSBC Global Asset Management (Malta) Limited	100.00	(70.03)	37
HSBC Global Asset Management (Oesterreich) GmbH	100.00	(80.67)	6, 38
HSBC Global Asset Management (Switzerland) AG	100.00	(90.33)	4, 39
HSBC Global Custody Nominee (UK) Limited	100.00		2, 15
HSBC Global Custody Proprietary Nominee (UK) Limited	100.00		2, 15
HSBC Global Shared Services (India) Private Limited (in liquidation)	100.00	(99.99)	40
HSBC Infrastructure Limited	100.00		15
HSBC INKA Investment-AG TGV	100.00	(80.67)	9, 41
HSBC Institutional Trust Services (Ireland) DAC	100.00	(99.99)	42
HSBC Insurance Management Services Limited (in liquidation)	100.00		43
HSBC Insurance Services Holdings Limited	100.00		2, 15
HSBC International Holdings (Jersey) Limited (in liquidation)	100.00		33
HSBC International Limited (in liquidation)	100.00		33
HSBC International Trade Finance Limited (in liquidation)	100.00		15
HSBC Investment Bank Holdings Limited	100.00		2, 15
HSBC Issuer Services Common Depositary Nominee (UK) Limited	100.00		2, 15
HSBC Issuer Services Depositary Nominee (UK) Limited	100.00		2, 15
HSBC Leasing (France)	100.00	(99.99)	4, 22
HSBC Life (UK) Limited	100.00		2, 15
HSBC Life Assurance (Malta) Limited	100.00	(70.03)	37
HSBC Lodge Funding (UK) Holdings (active proposal to strike off)	100.00		15
HSBC LU Nominees Limited	100.00		2, 15
HSBC Marking Name Nominee (UK) Limited	100.00		2, 15
HSBC Middle East Leasing Partnership	n/a		7, 44
HSBC Operational Services GmbH	n/a		7, 45
HSBC Overseas Nominee (UK) Limited	100.00		2, 15
HSBC PB Corporate Services 1 Limited	100.00		46
HSBC Pension Trust (Ireland) DAC	100.00		2, 42
HSBC PI Holdings (Mauritius) Limited	100.00		47
HSBC Preferential LP (UK)	100.00		2, 15
HSBC Private Bank (C.I.) Limited	100.00		2, 17
HSBC Private Banking Nominee 3 (Jersey) Limited	100.00		46
HSBC Private Equity Investments (UK) Limited	100.00		15
HSBC Property Funds (Holding) Limited	100.00		15
HSBC Rail (UK) Limited (in liquidation)	100.00		15

Subsidiaries	% of share class held by immediate parent company (or by HSBC Bank plc where this varies)		Footnotes
HSBC Real Estate Leasing (France)	99.99		4, 25
HSBC REIM (France)	100.00	(99.99)	4, 25
HSBC Representative Office (Nigeria) Limited	100.00		2, 48
HSBC Securities (South Africa) (Pty) Limited	100.00		2, 50
HSBC Securities Services (Guernsey) Limited	100.00		17
HSBC Securities Services (Ireland) DAC	100.00		42
HSBC Securities Services (Luxembourg) S.A.	100.00		2, 51
HSBC Securities Services Holdings (Ireland) DAC	100.00		42
HSBC Services (France)	99.99		4, 23
HSBC SFH (France)	99.99		4, 25
HSBC Specialist Investments Limited	100.00		5, 15
HSBC Transaction Services GmbH	100.00	(80.67)	6, 52
HSBC Trinkaus & Burkhardt (International) S.A.	100.00	(80.67)	51
HSBC Trinkaus & Burkhardt AG	80.67		9, 26
HSBC Trinkaus & Burkhardt Gesellschaft fur Bankbeteiligungen mbH	100.00	(80.67)	26
HSBC Trinkaus Europa Immobilien-Fonds Nr. 5 GmbH	100.00	(80.67)	26
HSBC Trinkaus Family Office GmbH	100.00	(80.67)	6, 26
HSBC Trinkaus Immobilien Beteiligungs KG	100.00	(80.67)	26
HSBC Trinkaus Real Estate GmbH	100.00	(80.67)	6, 26
HSBC Trustee (C.I.) Limited	100.00		2, 46
HSBC Trustee (Guernsey) Limited	100.00		2, 17
HSIL Investments Limited	100.00		15
InfraRed NF China Real Estate Investments LP	n/a		7, 75
INKA Internationale Kapitalanlagegesellschaft mbH	100.00	(80.67)	52
IRERE Property Investments (French Offices) Sarl (in liquidation)	100.00		53
James Capel & Co. Limited	100.00		2, 15
James Capel (Channel Islands) Nominees Limited (in liquidation)	100.00		36
James Capel (Nominees) Limited	100.00		2, 15
James Capel (Second Nominees) Limited (in liquidation)	100.00		2, 21
James Capel (Taiwan) Nominees Limited	100.00		2, 15
Keyser Ullmann Limited	100.00	(99.99)	15
Legend Estates Limited (in liquidation)	100.00		15
Marks and Spencer Retail Financial Services Holdings Limited (in liquidation)	100.00		2, 54
Midcorp Limited	100.00		2, 15
MIL (Jersey) Limited	100.00		46
Prudential Client HSBC GIS Nominee (UK) Limited	100.00		2, 15
Republic Nominees Limited	100.00		2, 17
RLUKREF Nominees (UK) One Limited	100.00		2, 15
RLUKREF Nominees (UK) Two Limited	100.00		2, 15
S.A.P.C. - Ufipro Recouvrement	99.97		11, 22
Saf Baiyun	100.00	(99.99)	4, 24
Saf Chang Jiang	100.00	(99.99)	4, 24
Saf Guangzhou	100.00	(99.99)	4, 24
Saf Zhu Jiang	100.00	(99.99)	4, 24
Saf Zhu Jiang Jiu	100.00	(99.99)	4, 24
Saf Zhu Jiang Shi Ba	100.00	(99.99)	4, 24
Saf Zhu Jiang Shi Er	100.00	(99.99)	4, 24
Saf Zhu Jiang Shi Jiu	100.00	(99.99)	4, 24
Saf Zhu Jiang Shi Liu	100.00	(99.99)	4, 24
Saf Zhu Jiang Shi Qi	100.00	(99.99)	4, 24
Saf Zhu Jiang Shi Wu	100.00	(99.99)	4, 24
SAS Bosquet -Audrain	100.00	(94.90)	4, 55
SAS Cyatheas Pasteur	100.00	(94.93)	4, 22
SAS Orona	100.00	(94.92)	1, 4, 56
SCI HSBC Assurances Immo	100.00	(99.99)	11, 25
SFM	99.99		4, 23
SFSS Nominees (Pty) Limited	100.00		50
SNC Dorique	100.00	(99.99)	1, 11, 57
SNC Kerouan	100.00	(99.99)	11, 24

Subsidiaries	% of share class held by immediate parent company (or by HSBC Bank plc where this varies)		Footnotes
SNC Les Mercuriales	100.00	(99.99)	1, 11, 24
SNC Les Oliviers D'Antibes	60.00		11, 25
SNC Makala	100.00	(99.99)	1, 11, 24
SNC Nuku-Hiva Bail	100.00	(99.99)	1, 11, 24
SNCB/M6 - 2008 A	100.00	(99.99)	1, 4, 24
SNCB/M6-2007 A	100.00	(99.99)	1, 4, 24
SNCB/M6-2007 B	100.00	(99.99)	1, 4, 24
Societe CCF Finance Moyen-Orient S.A.L. (in liquidation)	99.64	(99.08)	1, 20
Société Française et Suisse	100.00	(99.99)	4, 24
Somers Dublin DAC	100.00	(99.99)	42
Sopingest	100.00	(99.99)	4, 24
South Yorkshire Light Rail Limited	100.00		15
Swan National Leasing (Commercials) Limited	100.00		15
Swan National Limited	100.00		15
Thasosfin	100.00	(99.99)	4, 25
The Venture Catalysts Limited	100.00		2, 15
Trinkaus Australien Immobilien Fonds Nr. 1 Brisbane GmbH & Co. KG	100.00	(80.67)	26
Trinkaus Australien Immobilien-Fonds Nr. 1 Treuhand-GmbH	100.00	(80.67)	6, 26
Trinkaus Europa Immobilien-Fonds Nr.3 Objekt Utrecht Verwaltungs-GmbH	100.00	(80.67)	26
Trinkaus Immobilien-Fonds Geschaeftsfuehrungs-GmbH	100.00	(80.67)	6, 26
Trinkaus Immobilien-Fonds Verwaltungs-GmbH	100.00	(80.67)	6, 26
Trinkaus Private Equity Management GmbH	100.00	(80.67)	26
Trinkaus Private Equity Verwaltungs GmbH	100.00	(80.67)	6, 26
Valeurs Mobilières Elysées	100.00	(99.99)	4, 58

Joint ventures

The undertakings below are joint ventures and equity accounted.

Joint Ventures	% of share class held by immediate parent company or by HSBC Bank plc where this varies)		Footnotes
HCM Holdings Limited	50.99		21
Sino AG	24.94	(20.11)	71
The London Silver Market Fixing Limited	n/a		1, 2, 7, 72

Associates

The undertakings below are associates and equity accounted.

Associates	% of share class held by immediate parent company (or by HSBC Bank plc where this varies)		Footnotes
BGF Group PLC	24.48		59
Bud Financial Limited	8.02		3, 14, 60
CFAC Payment Scheme Limited	33.33		1, 2, 3, 61
Chemi & Cotex (Rwanda) Limited	99.98	(33.99)	1, 62
Chemi & Cotex Kenya Limited	99.99	(33.99)	1, 63
Chemi and Cotex Industries Limited	100.00	(33.99)	1, 64
HSBC Mortgage Limited Liability Partnership (in liquidation)	n/a		2, 7, 66
Jeppe Star Limited	100.00	(33.99)	67
Novo Star Limited	33.99		68
Quantexa Limited	10.51		14, 69
Services Epargne Entreprise	14.35		4, 14, 49
Vizolution Limited	17.95		14, 65
We Trade Innovation Designated Activity Company	8.52		14, 70

Footnotes

1	Management has determined that these undertakings are excluded from consolidation in the group accounts as these entities do not meet the definition of subsidiaries in accordance with IFRS. HSBC's consolidation policy is described in Note 1.2(a).
2	Directly held by HSBC Bank plc

Description of shares

3	Preference Shares
4	Actions
5	Redeemable Preference Shares
6	GmbH Anteil
7	This undertaking is a partnership and does not have share capital
8	Liquidating Share Class
9	Stückaktien
10	Non-Participating Voting Shares
11	Parts
12	Registered Capital Shares
13	Russian Limited Liability Company Shares
14	HSBC Bank plc exercises control or significant influence over this undertakings notwithstanding its equity interest

Registered offices

15	8 Canada Square, London, United Kingdom, E14 5HQ
16	5 Donegal Square South, Belfast, Northern Ireland, BT1 5JP
17	Arnold House, St Julians Avenue, St Peter Port, Guernsey, GY1 3NF
18	HSBC Main Building, 1 Queen's Road Central, Hong Kong
19	Unsoeldstrasse 2, Munich, Germany, 80538
20	Solidere - Rue Saad Zaghloul Immeuble - 170 Marfaa, PO Box 17 5476 Mar Michael 11042040, Beyrouth, Lebanon
21	Hill House, 1 Little New Street, London, United Kingdom, EC4A 3TR
22	39, rue de Bassano, Paris, France, 75008
23	103, avenue des Champs-Elysées, Paris, France, 75008
24	64, rue Galilée, Paris, France, 75008
25	15, rue Vernet, Paris, France, 75008
26	Königsallee 21/23, Düsseldorf, Germany, 40212
27	11-17 Ludwig-Erhard-Str., Hamburg, Germany, 20459
28	PO Box 513, HSBC House, 68 West Bay Road, George Town, Grand Cayman, Cayman Islands, KY1-1102
29	HSBC House Esplanade, St. Helier, Jersey, JE4 8UB
30	2 Paveletskaya Square, Building 2, Moscow, Russian Federation, 115054
31	66 Teryan Street, Yerevan, Armenia, 0009
32	116 Archbishop Street, Valletta, Malta
33	HSBC House Esplanade, St. Helier, Jersey, JE1 1HS
34	Rondo ONZ 1, Warsaw, Poland, 00-124
35	Immeuble Coeur Défense 110, Esplanade du Général de Gaulle- La défense 4, Courbevoie, France, 92400
36	HSBC House Esplanade, St. Helier, Jersey, JE4 8WP
37	80 Mill Street, Qormi, Malta, QRM 3101
38	Herrengasse 1-3, Wien, Austria, 1010
39	Gartenstrasse 26, Zurich, Switzerland
40	52/60 M G Road, Fort, Mumbai, India, 400 001
41	Breite Str. 29/31, Düsseldorf, Germany, 40213
42	1 Grand Canal Square, Grand Canal Harbour, Dublin 2, D02 P820, Ireland
43	1 More London Place, London, United Kingdom, SE1 2AF
44	Precinct Building 4, Level 3 Dubai International Financial Centre, Dubai, United Arab Emirates, PO BOX 506553
45	21-23 Yorckstraße, Düsseldorf, Nordrhein-Westfalen, Germany, 40476
46	HSBC House Esplanade, St. Helier, Jersey, JE1 1GT
47	HSBC Centre Eighteen, Cybercity, Ebene, Mauritius
48	St Nicholas House, 10th Floor Catholic Mission St Lagos, Nigeria
49	32 Rue du Champ de Tir, 44300 Nantes
50	2 Exchange Square, 85 Maude Street, Sandown, Sandton, South Africa, 2196
51	16 Boulevard d'Avranches, Luxembourg, L-1160
52	Yorckstraße 21 - 23 40476, Duesseldorf, Germany
53	6, rue Adolphe, Luxembourg, L-1116
54	Kings Meadow Chester Business Park, Chester, United Kingdom, CH99 9FB
55	15 rue Guynemer BP 412, Noumea, 98845
56	10, rue Jean Jaurès BP Q5, Noumea, New Caledonia, 98845
57	43 rue de Paris, Saint Denis, 97400
58	109 avenue des Champs-Elysees, Paris, France, 75008
59	13 - 15 York Buildings, London, United Kingdom, WC2N 6JU
60	207 First Floor The Bower, 207 Old Street, England, United Kingdom, EC1V 9NR
61	6th Floor, 65 Gresham Street, London, United Kingdom, EC2V 7NQ
62	Kacyiru BP 3094, Kigali, Rwanda
63	LR No. 1758/13 Grevella Grove Road, Kalamu House PO Box 47323-00100, Nairobi, Kenya
64	Plot No. 89-90 Mbezi Industrial Area, Box 347, Dar es Salaam City
65	Office Block A, Bay Studios Business Park, Fabian Way, Swansea, SA1 8QB, Wales, United Kingdom
66	40a Station Road, Upminster, United Kingdom, RM14 2TR
67	c/o Trident Trust Company, Trident Chambers, PO Box 146, Tortola, British Virgin Islands
68	Jayla Place Wickhams Cay I, PO Box 3190, Road Town, British Virgin Islands
69	75 Park Lane, Croydon, Surrey, United Kingdom, CR9 1XS
70	10 Earlsfort Terrace, Dublin, Ireland, D02 T380
71	Ernst-Schneider-Platz 1, Duesseldorf, Germany, 40212
72	C/O Hackwood Secretaries Limited, One Silk Street, London, EC2Y 8HQ
73	c/o Maples Corporate Services Limited, Ugland House, PO Box 309, Grand Cayman, KY1-1104, Cayman Islands
74	1 Royal Plaza, Royal Avenue, St Peter Port, Guernsey, Channel Islands, GY1 2HL
75	Regency Court, Glategny Esplanade, St. Peter Port, Guernsey GY1 1WW

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