

HSBC Bank Middle East Limited

Annual Report and Accounts 2017



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Presentation of Information

This document comprises the *Annual Report and Accounts 2017* for HSBC Bank Middle East Limited ('the bank') and its subsidiary undertakings (together 'the group'). It contains the Directors' Report and Accounts, together with the Auditor's report. References to 'HSBC' or 'the HSBC Group' within this document mean HSBC Holdings plc together with its subsidiaries.

Board of Directors

D G Eldon, Chairman	Sir W C Patey
G Elhedery, Chief Executive Officer and Deputy Chairman	A M Sharaf
R E Al Gurg	J Bartlett
A M Keir	C D Spooner
A H M H B Mostafawi	D Dew

Change in Directors

- D Dew was appointed as a Director on 17 May 2017.
- J Bartlett was appointed as a Director on 13 September 2017.
- T L Slattery resigned as a Director on 31 December 2017.
- K A A Almolhem resigned as a Director on 14 February 2018.

The Directors who held office during the year and up to the date the *Annual Report and Accounts* were approved are listed above.

Principal activities

The group through its branch network and subsidiary undertakings provides a range of banking and related financial services in the Middle East and North Africa. Changes in the group during the year are outlined below.

On 16 November 2016, the bank entered into an agreement with BLOM BANK S.A.L. to sell the banking operations in Lebanon and on 16 June 2017 completed the disposal.

On 29 June 2017, the bank acquired 10.01% stake in HSBC Bank A.S. in Turkey from HSBC Bank plc.

Attributable profit and dividends

The profit attributable to the shareholders of the parent company amounted to US\$545 million (2016: US\$536 million) as set out in the consolidated income statement on page 8.

During the year, a fourth interim dividend for 2016 and first, second and third interim dividends for 2017 of US\$25 million, US\$138 million, US\$161 million, and US\$106 million (2016: US\$1,095 million) were declared on 15 February 2017, 11 May 2017, 13 September 2017 and 6 December 2017 and were paid on 1 March 2017, 25 May 2017, 20 September 2017 and 11 December 2017, respectively.

A fourth interim dividend for 2017 of US\$140 million was declared by the Directors on 13 February 2018.

Registered office

The bank is incorporated in Dubai International Financial Centre, Dubai with number 2199. Its head office and registered office is Level 1, Gate Village Building 8, Dubai International Financial Centre, Dubai, United Arab Emirates.

Auditors

PricewaterhouseCoopers Limited has expressed its willingness to continue in office and the Board recommends that it be reappointed. A resolution proposing the reappointment of PricewaterhouseCoopers Limited as auditor of the bank and giving authority to the Directors to determine its remuneration will be submitted to the forthcoming Annual General Meeting.

On behalf of the Board

J A Tothill

Secretary

18 February 2018

Report on the audit of the consolidated financial statements

Our opinion

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of HSBC Bank Middle East Limited ('the bank') and its subsidiaries (together 'the group') as at 31 December 2017, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as endorsed by the European Union.

What we have audited

The group's consolidated financial statements comprise:

- the consolidated statement of financial position as at 31 December 2017;
- the consolidated income statement for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing ('ISAs'). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated 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 are independent of the group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants ('IESBA Code') and the requirements of the Dubai Financial Services Authority (the 'DFSA'). We have fulfilled our other ethical responsibilities in accordance with these requirements and with the IESBA Code.

Our audit approach

Overview

Materiality	Overall group materiality: US\$31 million, which represents 5% of profit before tax.
Group scoping	The scope of our audit and the nature, timing and extent of audit procedures performed were determined by our risk assessment, the financial significance of the components and other qualitative factors. Full scope audits were carried out at two of the five locations.
Key audit matters	The Key Audit Matters identified during the year are: <ul style="list-style-type: none">• Impairment of loans and advances• Valuation of unlisted equity investments• IT access management• Disclosure of the likely impact of IFRS 9

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the consolidated financial statements. In particular, we considered where management made subjective judgements; for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

How we tailored our group audit scope

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the consolidated financial statements as a whole, taking into account the structure of the group, the accounting processes and controls, and the industry in which the group operates.

Given the geographically dispersed nature of the group's operations in the Middle East and North Africa and the diversity of its banking activities, our approach was designed to cover each of the significant locations, being the United Arab Emirates ('UAE') and Qatar. We audited the operations of the group in the UAE and instructed a PwC member firm to perform work and issue an audit opinion to us in respect of the group's operations in Qatar. Each location that was not individually significant was assessed for any significant risks or material balances and, where appropriate, we instructed PwC member firms in those locations to perform and report on specific procedures relating to matters which were judgemental in nature and/or material to the overall group. The work in these locations was carried out by applying standard benchmarks on materiality and reflected the size and complexity of the operations.

Independent Auditor's Report to the Shareholder of HSBC Bank Middle East Limited

A significant amount of the group's operational processes which are critical to financial reporting are undertaken in global shared service centres that are operated by related entities of the group. The service centres that undertake operational and finance processes for the group are based across eight individual sites in four countries. The audit work over the shared service centre processes and controls was performed by PwC member firms in each of the global shared service centre locations and coordinated by the PwC member firm in the UK, with oversight from us. This work enabled us to evaluate the effectiveness of the controls over key processes that supported material balances, classes of transactions and disclosures within the group consolidated financial statements, and to consider the implications on our audit work.

In aggregate, the audit work performed across the locations above provided us with the audit evidence required to form an opinion on the group consolidated financial statements.

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the consolidated financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall group materiality for the consolidated financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the consolidated financial statements as a whole.

Overall group materiality	US\$31 million
How we determined it	5% of profit before tax
Rationale for the materiality benchmark applied	We chose profit before tax as the benchmark because, in our view, it is the benchmark against which the performance of the group is most commonly measured by users, and is a generally accepted benchmark. We chose 5% which is within the range of acceptable quantitative materiality thresholds in auditing standards.

We agreed with those charged with governance that we would report to them misstatements identified during our audit above US\$1.5 million as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter	How our audit addressed the key audit matter
<p>Impairment of loans and advances</p> <p>Our audit was focused on impairment due to the materiality of the loan balances and associated impairment allowances and the subjective nature of the impairment calculation.</p> <p>As disclosed in note 30, as at 31 December 2017, the group has recognised a provision for impairment of loans and advances of US\$1.071 billion.</p> <p>Impairment allowances represent management's best estimate of the losses incurred within the loan portfolios at the balance sheet date. They are calculated on a collective basis for portfolios of loans of a similar nature and on an individual basis for non-performing or impaired wholesale business loans. The calculation of both collective and individual impairment allowances is inherently judgemental for most banks.</p> <p>Collectively assessed impairment allowances are calculated using models which approximate the impact of current economic and credit conditions on large portfolios of loans.</p> <p>There is judgement applied to determine inputs into these models (such as the economic sector risk, loss given default and loss emergence periods) which are used to calculate impairment.</p> <p>For individually assessed impairments, judgement is required to determine when an impairment event has occurred and then to estimate the expected future cash flows related to that loan.</p> <p>The largest loan portfolios and significant impairment allowances are in the UAE, Qatar and Bahrain.</p>	<p>We assessed and tested the design and operating effectiveness of the key controls that management has established to support their collectively assessed and individually assessed impairment calculations.</p> <p>For collectively assessed impairment, these controls included testing over the appropriateness of methodology used to calculate the impairment, the process of determining key assumptions.</p> <p>For individually assessed impairment, our work included testing of controls over the monitoring of the credit watch list, the determination of internal credit risk ratings, credit file review processes, approval of external vendors providing collateral valuations and the approval of significant individual impairments.</p> <p>In addition, we evaluated the appropriateness of key management judgements in respect of calculation methodologies, economic factors, loss emergence periods and loss given defaults.</p> <p>For individually assessed allowances we also tested the application of the group's provisioning methodologies and policies for a sample of loans across the portfolios. Where an impairment had been identified, for a sample of loans, we examined the forecasts of future cash flows prepared by management to support the calculation of impairment, including those related to collateral values, and we challenged the assumptions used.</p> <p>We examined a sample of loans and advances, which had not been identified by management as potentially impaired and formed our judgement as to whether that was appropriate.</p>
<p>Valuation of unlisted equity investments</p> <p>We focused on the valuation of unlisted investments due to the materiality of the investments and the subjective nature of the valuations which involve the use of judgemental assumptions.</p> <p>As disclosed in note 14, as at 31 December 2017 the group has investments in unlisted equity securities of US\$118 million. These investments are classified as available-for-sale securities and are measured at fair value through other comprehensive income.</p>	<p>We assessed and tested the design and operating effectiveness of the key controls that management has established to support the review and approval of the model design, key model inputs and valuation.</p> <p>We assessed the appropriateness of the valuation method used by management with the assistance of our valuation experts. The key inputs used in the determination of assumptions within the model were challenged by our experts and corroborating information was obtained. The mathematical accuracy of the model was also tested.</p>

IT access management

Our audit focused in this area as all banks are highly dependent on technology due to the significant number of transactions that are processed daily. 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 improvement. Access management controls are critical to ensure that charges to applications and underlying data are appropriate.

Appropriate access controls contribute to mitigating the risk of potential fraud or errors as a result of changes to applications and data.

Management implemented several remediation activities that contributed to reducing the risk over access management in the financial reporting process. These included the implementation of HSBC Group-wide preventative and detective controls across critical applications and infrastructure.

Due to the pervasive nature of access management issues, we continued to assess the risk of a material misstatement arising from inappropriate or unauthorised access to technology as significant for our audit.

We received regular briefings from management on the progress made in remediating weaknesses in HSBC Group-wide systems and we communicated with other PwC member firms in respect of their validation of remediated controls.

We reviewed formal reporting on the results of work performed in relation to the HSBC Group systems used by the group.

Access rights were tested over applications, operating systems and databases relied upon for financial reporting.

Specially 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 changed role;
- access rights to applications, operating systems and databases were periodically monitored for appropriateness; and
- highly privileged access is restricted to appropriate personnel.

Other areas that we independently tested 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 business performance reviews;
- testing was performed over toxic combination controls; and
- the risk of inadequate segregation of duties was assessed, taking into account mitigating controls, and additional work was performed where segregation of duties was deemed to be of higher risk.

Disclosure of the likely impact of IFRS 9

Our audit was focused on the disclosure of the impact of the implementation of IFRS 9 – Financial Instruments (IFRS 9), as this is a new and complex accounting standard, which will have a material impact on the group's financial statements for the year ended 31 December 2018, and has required considerable judgement and interpretation in its implementation.

As disclosed in note 2.1(b), management has estimated that the first time adoption of IFRS 9 on 1 January 2018 will not result in any change to net assets as a result of the classification and measurement requirements, and will result in a decrease in retained earnings of US\$106 million due to the impairment requirements.

IFRS 9 introduces a new classification and measurement approach for financial assets that reflects the business model in which financial assets are managed and the underlying cash flow characteristics. IFRS 9 contains three principal classification categories for financial assets:

- measured at amortised cost ('AC');
- fair value through other comprehensive income ('FVOCI'); and
- fair value through profit or loss ('FVPL').

IFRS 9 introduces new impairment rules which prescribe a new, forward looking, expected credit loss ('ECL') impairment model which takes into account reasonable and supportable forward-looking information which will generally result in the earlier recognition of impairment provisions.

There are a number of significant judgements which are required in measuring ECL under IFRS 9 including:

- determining the criteria for a significant increase in credit risk ('SICR');
- factoring in future economic guidance; and
- techniques used to determine the Probability of Default ('PD') and Loss Given Default ('LGD').

These judgements have required new models to be built and implemented to measure the expected credit losses on loans measured at amortised cost.

There is a large increase in the data inputs required by these models which increases the risk of completeness and accuracy of the data that has been used to develop assumptions and operate the model.

We assessed and tested the design and effectiveness of the key controls that management has established in relation to meeting the classification and measurement requirements under IFRS 9. In addition, we have independently assessed the business model documentation and tested a sample of contracts to assess if those contracts pass solely through payment of principal and interest criteria.

For expected credit loss calculations, we also assessed and tested the design and operating effectiveness of the key controls that management has established. This includes testing the key controls over governance and model development.

We have used our experts to test the modelling methodology and assumptions for material portfolios. In addition, our experts performed substantive procedures over material models which included assessing the reasonableness of key assumptions.

We also tested the design and operating effectiveness of key reconciliations over the completeness and accuracy of data, including testing material exceptions noted in reconciliations. Our testing also includes substantiation of material adjustments recorded by management.

Further, we tested the controls performed by management to assess the reasonableness of the disclosed impact of adopting IFRS 9 and independently validated the disclosures against the requirements of IFRS.

Independent Auditor's Report to the Shareholder of HSBC Bank Middle East Limited

Other information

The Board of Directors is responsible for the other information. The other information, which we obtained prior to the date of the auditor's report, comprises the Report of the Directors (but does not include the consolidated financial statements and our auditor's report thereon).

Our opinion on the consolidated financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the consolidated financial statements

The Board of Directors is responsible for the preparation and fair presentation of the consolidated financial statements that give a true and fair view in accordance with International Financial Reporting Standards as endorsed by the European Union and in accordance with the applicable regulatory requirements of the DFSA and for such internal control as they determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the Board of Directors are responsible for assessing the group'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 management either intends to liquidate the group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's 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 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 consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of the Board of Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other legal and regulatory requirements

As required by the applicable provisions of the DFSA Rulebook, we report that the consolidated financial statements have been properly prepared in accordance with the applicable requirements of the DFSA.

PricewaterhouseCoopers

Dubai, United Arab Emirates

18 February 2018

Audit Principal: David R Cox

Consolidated income statement for the year ended 31 December

	<i>Notes</i>	2017 US\$000	2016 US\$000
Net interest income		906,492	916,834
– interest income		1,062,823	1,068,578
– interest expense		(156,331)	(151,744)
Net fee income		435,045	473,877
– fee income		530,756	537,412
– fee expense		(95,711)	(63,535)
Net trading income		216,248	251,836
– trading income excluding net interest income		235,736	267,860
– net interest expense on trading activities		(19,488)	(16,024)
Net income/(expense) from financial instruments designated at fair value	3	4,988	(209)
Net (losses)/gains from financial investments		(5,015)	4,023
Dividend income		3,872	2,609
Other operating income, net		126,320	29,079
Net operating income before loan impairment charges and other credit risk provisions		1,687,950	1,678,049
Loan impairment charges and other credit risk provisions	4	(149,912)	(150,355)
Net operating income		1,538,038	1,527,694
Employee compensation and benefits	5	(522,261)	(511,562)
General and administrative expenses		(359,683)	(349,161)
Depreciation and impairment of property, plant and equipment		(13,364)	(13,144)
Amortisation and impairment of intangible assets		(5,663)	(5,911)
Total operating expenses		(900,971)	(879,778)
Operating profit	4	637,067	647,916
Share of profit in associates	16	290	1,879
Profit before tax		637,357	649,795
Tax expense	7	(92,004)	(112,694)
Profit for the year		545,353	537,101
Attributable to:			
– shareholders of the parent company		545,212	536,239
– non-controlling interests		141	862
Profit for the year		545,353	537,101

The accompanying notes on pages 13 to 63 form an integral part of these financial statements.

Consolidated statement of comprehensive income
for the year ended 31 December

	2017	2016
	US\$000	US\$000
Profit for the year	545,353	537,101
Other comprehensive income/(expense)		
Items that will be reclassified subsequently to profit or loss when specific conditions are met:		
Available-for-sale investments	(5,324)	(16,735)
– fair value losses	(7,225)	(14,482)
– fair value gains reclassified to the income statement	(801)	(12,180)
– amounts reclassified to the income statement in respect of impairment losses	2,652	9,782
– income taxes	50	145
Cash flow hedges	(3,997)	5,026
– fair value (losses)/gains	(4,441)	5,585
– income taxes	444	(559)
Exchange differences	(10,662)	(6,293)
Items that will not be reclassified subsequently to profit or loss:		
Remeasurement of defined benefit asset/liability	(15,162)	2,309
– before income taxes	(16,553)	2,432
– income taxes	1,391	(123)
Changes in fair value of financial liabilities designated at fair value due to movement in own credit risk	(3,577)	–
– before income taxes	(3,577)	–
– income taxes	–	–
Other comprehensive expense for the year, net of tax	(38,722)	(15,693)
Total comprehensive income for the year	506,631	521,408
Attributable to:		
– shareholders of the parent company	506,490	520,546
– non-controlling interests	141	862
Total comprehensive income for the year	506,631	521,408

The accompanying notes on pages 13 to 63 form an integral part of these financial statements.

Financial Statements

Consolidated statement of financial position at 31 December

	<i>Notes</i>	2017 US\$000	2016 US\$000
Assets			
Cash and balances at central banks		671,440	462,057
Items in the course of collection from other banks		64,419	47,053
Trading assets	10	440,624	182,406
Derivatives	13	963,102	1,319,251
Loans and advances to banks	25	6,203,202	6,249,298
Loans and advances to customers	25	18,316,780	21,010,573
Reverse repurchase agreements – non-trading		1,387,254	1,050,843
Financial investments	14	6,746,504	6,582,181
Assets held for sale	19	–	851,691
Prepayments, accrued income and other assets	18	657,894	684,891
Current tax assets		1,383	3,881
Interests in associates	16	1,948	1,658
Intangible assets		10,502	13,458
Deferred tax assets	7	205,857	209,111
Total assets at 31 Dec		35,670,909	38,668,352
Liabilities and equity			
Liabilities			
Deposits by banks	25	1,798,474	3,246,654
Customer accounts	25	22,583,649	22,588,927
Items in the course of transmission to other banks		87,502	90,415
Trading liabilities	20	1,309,860	1,496,561
Financial liabilities designated at fair value	21	739,425	401,592
Derivatives	13	952,332	1,409,040
Debt securities in issue	22	2,092,390	2,645,483
Liabilities of disposal groups held for sale	19	–	804,272
Accruals, deferred income and other liabilities	23	1,619,693	1,617,334
Current tax liabilities		110,141	149,666
Provisions	24	71,608	43,789
Deferred tax liabilities	7	–	523
Total liabilities at 31 Dec		31,365,074	34,494,256
Equity			
Called up share capital	28	931,055	931,055
Share premium account	28	61,346	–
Other reserves		(132,153)	(106,760)
Retained earnings		3,441,349	3,345,703
Total shareholders' equity		4,301,597	4,169,998
Non-controlling interests		4,238	4,098
Total equity at 31 Dec		4,305,835	4,174,096
Total liabilities and equity at 31 Dec		35,670,909	38,668,352

The accompanying notes on pages 13 to 63 form an integral part of these financial statements.

G Elhedery

Chief Executive Officer and Deputy Chairman

Consolidated statement of cash flows
for the year ended 31 December

	Notes	2017 US\$000	2016 US\$000
Cash flows from operating activities			
Profit before tax		637,357	649,795
Adjustments for:			
Net gain from investing activities		(14,450)	(13,107)
Share of profits in associates		(290)	(1,879)
Gain on disposal of branches and associates		(55,438)	(13,052)
Other non-cash items included in profit before tax	29	250,656	255,042
Change in operating assets	29	1,160,275	1,654,886
Change in operating liabilities	29	(2,514,965)	(2,324,413)
Elimination of exchange differences ¹		(80,498)	177,749
Dividends received from associates		–	1,312
Contribution paid for defined benefit plans		–	(536)
Tax paid		(121,794)	(108,735)
Net cash (used in)/generated from operating activities		(739,147)	277,062
Cash flows from investing activities			
Purchase of financial investments		(2,918,692)	(4,192,070)
Proceeds from the sale and maturity of financial investments		2,494,611	3,311,065
Purchase of property, plant and equipment		(9,456)	(18,025)
Proceeds from sale of property, plant and equipment		27,815	1,625
Purchase of intangible assets		(7,070)	(3,303)
Proceeds from sale of intangible assets		3,009	262
Net cash flow on disposal of businesses and associates		123,347	16,900
Net cash used in investing activities		(286,436)	(883,546)
Cash flows from financing activities			
Dividends paid to shareholders of the parent company		(430,000)	(1,095,000)
Net cash used in financing activities		(430,000)	(1,095,000)
Net decrease in cash and cash equivalents		(1,455,583)	(1,701,484)
Cash and cash equivalents at 1 Jan		7,208,806	8,996,879
Exchange differences in respect of cash and cash equivalents		46,863	(86,589)
Cash and cash equivalents at 31 Dec	29	5,800,086	7,208,806

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.

The accompanying notes on pages 13 to 63 form an integral part of these financial statements.

Consolidated statement of changes in equity
for the year ended 31 December

	Other reserves								
	Called up share capital and share premium	Retained earnings	Available-for-sale fair value reserve	Cash flow hedging reserve	Foreign exchange reserve	Merger and other reserves	Total shareholders' equity	Non-controlling interests	Total equity
	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000
At 1 Jan 2017	931,055	3,345,703	17,139	(3,358)	(105,220)	(15,321)	4,169,998	4,098	4,174,096
Profit for the year	–	545,212	–	–	–	–	545,212	141	545,353
Other comprehensive income (net of tax)	–	(18,804)	(5,231)	(3,996)	(10,691)	–	(38,722)	–	(38,722)
– available-for-sale investments	–	–	(5,324)	–	–	–	(5,324)	–	(5,324)
– cash flow hedges	–	–	–	(3,997)	–	–	(3,997)	–	(3,997)
– changes in fair value of financial liabilities designated at fair value arising from changes in own credit risk	–	(3,577)	–	–	–	–	(3,577)	–	(3,577)
– remeasurement of defined benefit asset/liability	–	(15,162)	–	–	–	–	(15,162)	–	(15,162)
– exchange differences	–	(65)	93	1	(10,691)	–	(10,662)	–	(10,662)
Total comprehensive income for the year	–	526,408	(5,231)	(3,996)	(10,691)	–	506,490	141	506,631
Ordinary share issued (Note 28)	61,346	–	–	–	–	–	61,346	–	61,346
Dividends to shareholders	–	(430,000)	–	–	–	–	(430,000)	–	(430,000)
Exercise and lapse of share options and vesting of share awards	–	(9,377)	–	–	–	–	(9,377)	–	(9,377)
Cost of share-based payment arrangements	–	9,627	–	–	–	–	9,627	–	9,627
Other movements	–	(1,012)	(5,475)	–	–	–	(6,487)	(1)	(6,488)
At 31 Dec 2017	992,401	3,441,349	6,433	(7,354)	(115,911)	(15,321)	4,301,597	4,238	4,305,835
At 1 Jan 2016	931,055	3,899,654	35,019	(8,384)	(98,964)	(15,321)	4,743,059	3,236	4,746,295
Profit for the year	–	536,239	–	–	–	–	536,239	862	537,101
Other comprehensive income (net of tax)	–	2,281	(16,744)	5,026	(6,256)	–	(15,693)	–	(15,693)
– available-for-sale investments	–	–	(16,735)	–	–	–	(16,735)	–	(16,735)
– cash flow hedges	–	–	–	5,026	–	–	5,026	–	5,026
– changes in fair value of financial liabilities designated at fair value arising from changes in own credit risk	–	–	–	–	–	–	–	–	–
– remeasurement of defined benefit asset/liability	–	2,309	–	–	–	–	2,309	–	2,309
– exchange differences	–	(28)	(9)	–	(6,256)	–	(6,293)	–	(6,293)
Total comprehensive income for the year	–	538,520	(16,744)	5,026	(6,256)	–	520,546	862	521,408
Ordinary share issued (Note 28)	–	–	–	–	–	–	–	–	–
Dividends to shareholders	–	(1,095,000)	–	–	–	–	(1,095,000)	–	(1,095,000)
Exercise and lapse of share options and vesting of share awards	–	(6,140)	–	–	–	–	(6,140)	–	(6,140)
Cost of share-based payment arrangements	–	10,056	–	–	–	–	10,056	–	10,056
Other movements	–	(1,387)	(1,136)	–	–	–	(2,523)	–	(2,523)
At 31 Dec 2016	931,055	3,345,703	17,139	(3,358)	(105,220)	(15,321)	4,169,998	4,098	4,174,096

The accompanying notes on pages 13 to 63 form an integral part of these financial statements.

1 Legal status and principal activities

The group has its place of incorporation and head office in Dubai International Financial Centre ('DIFC'), in the United Arab Emirates, under a category 1 licence issued by the Dubai Financial Services Authority ('DFSA').

The group's registered office is Level 1, Gate Village Building 8, Dubai International Financial Centre, Dubai, United Arab Emirates.

The group through its branch network and subsidiary undertakings provides a range of banking and related financial services in the Middle East and North Africa.

The immediate parent company of the group is HSBC Middle East Holdings BV and the ultimate parent company of the group is HSBC Holdings plc, which is incorporated in England.

2 Basis of preparation and significant accounting policies

2.1 Basis of preparation

(a) Compliance with International Financial Reporting Standards

The consolidated financial statements of the group have been prepared in accordance with the International Financial Reporting Standards ('IFRS') 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 2017, there were no unendorsed standards effective for the year ended 31 December 2017 affecting these consolidated 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 2017

The group has adopted the requirements of IFRS 9 'Financial Instruments' relating to the presentation of gains and losses on financial liabilities designated at fair value from 1 January 2017 in the consolidated financial statements. As a result, the effects of changes in those liabilities' credit risk is presented in other comprehensive income with the remaining effect presented in profit or loss. As permitted by the transitional requirements of IFRS 9, comparatives have not been restated. Adoption increased profit after tax by US\$3.6 million with the opposite effect on other comprehensive income and no effect on net assets.

There were no other new standards applied in 2017. However, during 2017, the group adopted a number of interpretations and amendments to standards which had an insignificant effect on the consolidated financial statements of the group.

(b) Future accounting developments

Minor amendments to IFRSs

The IASB has published a number of minor amendments to IFRSs in its 'Annual Improvements to IFRSs 2014-2016' and in a series of stand-alone amendments which are effective from 1 January 2018, but which have not yet 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. The group has not early adopted any of the amendments effective after 31 December 2017, except the requirements of IFRS 9 'Financial Instruments' relating to the presentation of gains and losses on financial liabilities designated at fair value which was adopted from 1 January 2017.

Major new IFRSs

The IASB has published IFRS 9 'Financial Instruments', IFRS 15 'Revenue from Contracts with Customers', IFRS 16 'Leases' and IFRS 17 'Insurance contracts'. IFRS 9, IFRS 15 and IFRS 16 have been endorsed for use in the EU and IFRS 17 has not yet been endorsed.

IFRS 9 'Financial Instruments'

In July 2014, the IASB issued IFRS 9 'Financial Instruments', which is the comprehensive standard to replace IAS 39 'Financial Instruments: Recognition and Measurement', and includes requirements for classification and measurement of financial assets and liabilities, impairment of financial assets and hedge accounting.

Classification and measurement

The classification and measurement of financial assets will depend on how these are managed (the entity's business model) and their contractual cash flow characteristics. These factors determine whether the financial assets are measured at amortised cost, fair value through other comprehensive income ('FVOCI') or fair value through profit or loss ('FVPL'). The combined effect of the application of the business model and the contractual cash flow characteristics tests may result in some differences in the population of financial assets measured at amortised cost or fair value compared with IAS 39. In addition, on transition to IFRS 9 entities are required to revoke previous designations of financial assets and financial liabilities measured at fair value through profit or loss where the accounting mismatch no longer exists and are permitted to revoke such designations where accounting mismatches continue to exist.

Impairment

The impairment requirements apply to financial assets measured at amortised cost and FVOCI, lease receivables and certain loan commitments and financial guarantee contracts. At initial recognition, an impairment allowance (or provision in the case of commitments and guarantees) is required for expected credit losses ('ECL') resulting from default events that are possible within the next 12 months ('12-month ECL'). In the event of a significant increase in credit risk, an 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'.

The assessment of credit risk and the estimation of ECL are required to be unbiased and probability-weighted, and should incorporate all available information which is relevant to the assessment including information about past events, current conditions and reasonable and supportable forecasts of economic conditions at the reporting date. In addition, the estimation of ECL should take into account the time value of money. As a result, the recognition and measurement of impairment is intended to be more forward-looking than under IAS 39 and the resulting impairment charge will tend to be more volatile. It will also tend to result in an increase in the total level of impairment allowances, since all financial assets will be assessed for at least 12-month ECL and the population of financial assets to which lifetime ECL applies is likely to be larger than the population for which there is objective evidence of impairment in accordance with IAS 39.

Notes on the Financial Statements

Hedge accounting

The general hedge accounting requirements aim to simplify hedge accounting, creating a stronger link with risk management strategy and permitting hedge accounting to be applied to a greater variety of hedging instruments and risks, but do not explicitly address macro-hedge accounting strategies, which are particularly important for banks. As a result, IFRS 9 includes an accounting policy choice to remain with IAS 39 hedge accounting.

Transition

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, the requirements of IFRS 9 'Financial Instruments' will be adopted from 1 January 2018. IFRS 9 includes an accounting policy choice to continue IAS 39 hedge accounting, which the group has exercised, although it will implement the revised hedge accounting disclosures required by the related amendments to IFRS 7 'Financial Instruments: Disclosures'. The classification and measurement and impairment requirements are applied retrospectively by adjusting the opening balance sheet at the date of initial application, with no requirement to restate comparative periods. The group does not intend to restate comparatives. For the consolidated financial statements of the group, adoption is expected to reduce net assets at 1 January 2018 by US\$106 million due to impairment reducing net assets by US\$117 million, net of deferred tax of US\$11 million.

IFRS 15 'Revenue from Contracts with Customers'

In May 2014, the IASB issued IFRS 15 'Revenue from Contracts with Customers' and it is effective for annual periods beginning on or after 1 January 2018. IFRS 15 provides a principles-based approach for revenue recognition, and introduces the concept of recognising revenue for performance obligations as they are satisfied. The group will adopt the standard on its mandatory effective date, and the standard will be applied on a modified retrospective basis, recognising the cumulative effect, if any, of initially applying the standard as an adjustment to the opening balance of retained earnings. The group has assessed the impact of IFRS 15 and expects that the standard will have no significant effect, when applied, on the consolidated financial statements of the group.

IFRS 16 'Leases'

In January 2016, the IASB issued IFRS 16 'Leases' with 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' 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. The group is currently assessing the impact of IFRS 16, and it is not practicable to quantify the effect at the date of the publication of these financial statements. Existing operating lease commitments are set out in Note 32.

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. IFRS 17 is effective from 1 January 2021. The group has assessed the impact of IFRS 17 and expects that the standard will have no significant effect, when applied, on the consolidated financial statements of the group.

(c) Foreign currencies

The group's consolidated financial statements are presented in US dollars because the US dollar and currencies linked to it form the major currency bloc in which the group transacts and funds its business. The US dollar is also the bank's functional currency because the US dollar and currencies linked to it are the most significant currencies relevant to the underlying transactions, events and conditions of its subsidiaries, as well as representing a significant proportion of its funds generated from financing activities.

Transactions in foreign currencies are recorded in the functional currency at the rate of exchange prevailing on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rate of exchange at the balance sheet date. Any resulting exchange differences are included in the income statement. Non-monetary assets and liabilities that are measured at historical cost in a foreign currency are translated into the functional currency using the rate of exchange at the date of the initial transaction. Non-monetary assets and liabilities measured at fair value in a foreign currency are translated into the functional currency using the rate of exchange at the date the fair value was determined. Any exchange component of a gain or loss on a non-monetary item is recognised either in other comprehensive income or in the income statement depending where the gain or loss on the underlying non-monetary item is recognised.

In the consolidated financial statements, the assets and liabilities of branches, subsidiaries, joint ventures and associates whose functional currency is not US dollars, are translated into the group's presentation currency at the rate of exchange at the balance sheet date, while their results are translated into US dollars at the average rates of exchange for the reporting period. Exchange differences arising from the retranslation of opening foreign currency net assets, and exchange differences arising from retranslation of the result for the reporting period from the average rate to the exchange rate at the period end, are recognised in other comprehensive income. Exchange differences on a monetary item that is part of a net investment in a foreign operation are recognised in the income statement of the separate financial statements and in other comprehensive income in consolidated accounts. On disposal of a foreign operation, exchange differences previously recognised in other comprehensive income are reclassified to the income statement as a reclassification adjustment.

(d) 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 2.2 below, it is possible that the outcomes in the next financial year could differ from those on which management's estimates are based, resulting in materially different conclusions from those reached by management for the purposes of these Financial Statements. Management's selection of the group's accounting policies which 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.

(e) Segmental analysis

The group's chief operating decision-maker is the Board. Operating segments are reported in a manner consistent with the internal reporting provided to the Board.

Measurement of segmental assets, liabilities, income and expenses is in accordance with the group'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.

Products and services

The group manages products and services to its customers in the geographical regions through global businesses.

- Retail Banking and Wealth Management ('RBWM') serves its customers through four main businesses: Retail Banking, Wealth Management, Asset Management and Insurance. The HSBC Premier and Advance propositions are aimed at mass affluent and emerging affluent customers who value international connectivity and benefit from the global reach and scale. For customers with simpler banking needs, RBWM offers a full range of products and services reflecting local requirements.
- Commercial Banking ('CMB') customers range from small enterprises focused primarily on their domestic markets through to corporates operating globally. CMB support customers with tailored financial products and services to allow them to operate efficiently and grow. Services provided include working capital, term loans, payment services and international trade facilitation, as well as expertise in mergers and acquisitions, and access to financial markets.
- Global Banking and Markets ('GB&M') supports major government, corporate and institutional clients. GB&M product specialists continue to deliver a comprehensive range of transaction banking, financing, advisory, capital markets and risk management services.
- Global Private Banking ('GPB') serves high net worth individuals and families, including those with international banking needs. GPB provides a full range of private banking services, including Investment Management, which includes advisory and brokerage services, and Private Wealth Solutions, which comprises trusts and estate planning, to protect and preserve wealth for future generations.
- Corporate Centre comprises Central Treasury, including Balance Sheet Management ('BSM'), interests in associates and central stewardship costs that support our businesses.

(f) Composition of the group

Lebanon

On 16 November 2016, the bank entered into an agreement with BLOM BANK S.A.L. to sell the banking operations in Lebanon. On 16 June 2017 bank completed the disposal at a sale consideration of US\$123 million which resulted in a net gain on disposal of US\$55 million included in 'Other operating income, net'.

2.2 Summary of significant accounting policies

(a) Consolidation and related policies

Investments in subsidiaries

The group controls and consequently consolidates an entity when it is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Control is initially assessed based on consideration of all facts and circumstances, and is subsequently reassessed when there are significant changes to the initial setup.

Where an entity is governed by voting rights, the group would consolidate 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 over the relevant activities or holding the power as agent or principal.

Business combinations are accounted for using the acquisition method. The amount of non-controlling interest is measured at the non-controlling interest's proportionate share of the acquiree's identifiable net assets.

The group has adopted the policy of 'predecessor accounting' for the transfer of business combinations under common control within the HSBC Group. Under IFRS where both HSBC Group entities adopt the same method for accounting for common control transactions the excess of the cost of the purchased group entity over the carrying value is recorded as a merger reserve on consolidation.

Changes in a parent's ownership interest in a subsidiary that do not result in a loss of control are treated as transactions between equity holders and are reported in equity.

Entities that are controlled by the group are consolidated from the date the group gains control and cease to be consolidated on the date the group loses control of the entities.

The group performs a re-assessment of consolidation whenever there is a change in the facts and circumstances of determining the control of all entities.

All intra-group transactions are eliminated on consolidation.

The 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 the relevant counterparties to a structured transaction. The group is not considered a sponsor if the only involvement with the entity is to provide services at arms' length and it ceases to be a sponsor once it has no ongoing involvement with that structured.

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 are recognised using the equity method. The attributable share of the results and reserves of associates are included in the consolidated financial statements of 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 of financial statements available and 31 December.

Notes on the Financial Statements

Investments in associates are assessed at each reporting date and tested for impairment when there is an indication that the investment may be impaired.

(b) Income and expenses

Operating income

Interest income and expense

Interest income and expense for all financial instruments except for those classified as held for trading or designated at fair value (except for debt securities issued by the group and derivatives managed in conjunction with those debt securities) are recognised in 'Interest income' and 'Interest expense' in the income statement using the effective interest method. The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument or, where appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability.

Non-interest income and expense

Fee income is earned from a diverse range of services provided by the group to its customers. Fee income is accounted for as follows:

- income earned on the execution of a significant act is recognised as revenue when the act is completed (for example, fees arising from negotiating, or participating in the negotiation of, a transaction for a third party, such as an arrangement for the acquisition of shares or other securities);
- income earned from the provision of services is recognised as revenue as the services are provided (for example, asset management, portfolio and other management advisory and service fees); and
- income which forms an integral part of the effective interest rate of a financial instrument is recognised as an adjustment to the effective interest rate (for example, certain loan commitment fees) and recorded in 'Interest income'.

Net trading income comprises 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.

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 designated at fair value' includes all gains and losses from changes in the fair value of financial assets and liabilities designated at fair value through profit or loss, including derivatives that are managed in conjunction with those financial assets and liabilities, and liabilities under investment contracts. Interest income, interest expense and dividend income in respect of those financial instruments are also included, except for interest arising from debt securities issued by the group and derivatives managed in conjunction with those debt securities, which is recognised in 'Interest expense'.

(c) Valuation of financial instruments

All financial instruments are recognised initially 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 the transaction price (that is, the fair value of the consideration given or received). In certain circumstances, however, the fair value will be based on other observable current market transactions in the same instrument, without modification or repackaging, or on a valuation technique whose variables include only data from observable markets, such as interest rate yield curves, option volatilities and currency rates. When such evidence exists, the group recognises a trading gain or loss on inception of the financial instrument, being the difference between the transaction price and the fair value. When unobservable market data have a significant impact on the valuation of financial instruments, the entire initial difference in fair value from the transaction price as indicated by the valuation model from the transaction price is not recognised immediately in the income statement. Instead, it is recognised over the life of the transaction on an appropriate basis, or when the inputs become observable, or the transaction matures or is closed out, or when the group enters into an offsetting transaction.

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 group measures the fair value of the group of financial instruments on a net basis but presents the underlying financial assets and liabilities separately in the financial statements, unless they satisfy the IFRS offsetting criteria.

Critical accounting estimates and judgements

The majority of valuation techniques employ only observable market data. However, certain financial instruments are valued 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, a significant proportion of the instrument's inception profit or 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

These include loans and advances originated by the group, not classified as held for trading or designated at fair value. They are recognised when cash is advanced to a borrower and are derecognised when either the borrower repays its obligations, or the loans are sold or written off, or substantially all the risks and rewards of ownership are transferred. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method, less impairment allowance.

The group may commit to underwrite 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, a provision on the loan commitment is only recorded where it is probable that the group 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, the group 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, 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 the group has incurred as a result of events occurring before the balance sheet date which the group is not able to identify on an individual loan basis, and that can be reliably estimated. When information becomes available which 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 that are used to calculate collective allowances are:

- When appropriate empirical information is available, the group utilises roll-rate methodology, which employs statistical analyses of historical data and experience of delinquency and default to reliably estimate the amount of loans that will eventually be written off as a result of the events occurring before the balance sheet date and which the group is not able to identify individually. Individual loans are grouped using ranges of past due days; statistical analysis is then used to estimate 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 as described above. In applying this methodology, adjustments are made to estimate the periods of time between a loss event occurring and its discovery, for example through a missed payment (known as the emergence period) and the period of time between discovery and write-off (known as the outcome period). Current economic conditions are also evaluated when calculating the appropriate level of allowance required to cover inherent loss.
- When the portfolio size is small or when information is insufficient or not reliable enough to adopt a roll-rate methodology, the group 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 explicitly 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.

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 payments required have 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.

Notes on the Financial Statements

Critical accounting estimates and judgements

Loan impairment allowances represent management's best estimate of losses incurred in the loan portfolios at the balance sheet date. Management is required to exercise judgement in making assumptions and estimates when calculating loan impairment allowances on both individually and collectively assessed loans and advances.

Collective impairment allowances are subject to estimation uncertainty, in part because it is not practicable to identify losses on an individual loan basis due to the large number of individually insignificant loans in the portfolio. The estimation methods include the use of statistical analyses of historical information, supplemented with significant management judgement, to assess whether current economic and credit conditions are such that the actual level of incurred losses is likely to be greater or less than historical experience. Where changes in economic, regulatory or behavioural conditions result in the most recent trends in portfolio risk factors being not fully reflected in the statistical models, risk factors are taken into account by adjusting the impairment allowances derived solely from historical loss experience.

For individually assessed loans, judgement is required in determining whether there is objective evidence that a loss event has occurred and, if so, the measurement of the impairment allowance. In determining whether there is objective evidence that a loss event has occurred, judgement is exercised in evaluating all relevant information on indicators of impairment, including the consideration of whether payments are contractually past-due and the consideration of other factors indicating deterioration in the financial condition and outlook of borrowers affecting their ability to pay.

Non-trading reverse repurchase and repurchase agreements

When 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.

(e) Financial instruments measured at fair value

Available-for-sale financial assets

Available-for-sale financial assets are recognised on the trade date when the group enters into contractual arrangements to purchase those instruments, and are normally derecognised when either the securities are 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, the group 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 also 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.

Under this criterion, the main classes of financial instruments designated by the group 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 the group does not accept significant insurance risk from another party is not classified as an insurance contract, but is accounted for as a financial liability. 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.

Designated financial assets are recognised when the group 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 the group 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 designated at fair value'.

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. Derivatives are classified as assets when their fair value is positive or as liabilities when their fair value is negative, this includes embedded derivatives which are bifurcated from the host contract when they meet the definition of a derivative on a stand-alone basis.

Gains and losses from changes in the fair value of derivatives that do not qualify for hedge accounting are reported in 'Net trading income'. Gains and losses on derivatives managed in conjunction with financial instruments designated at fair value are reported in 'Net income from financial instruments designated at fair value' together with the gains and losses on the economically hedged items. Where the derivatives are managed with debt securities issued by the group 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 held for risk management purposes they are designated in hedge relationships where the required criteria for documentation and hedge effectiveness are met. The group enters into fair value hedges, cash flow hedges or hedges of net investments in foreign operations as appropriate to the risk being hedged.

Fair value hedge

Changes in the fair value of derivatives are recorded in the income statement, along with changes in the fair value of the hedged assets or liabilities attributable to the hedged risk. 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 over the residual period to maturity, 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 changes in the fair value of derivatives is recognised in other comprehensive income; the ineffective portion of the change in fair value 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. In hedges of forecast transactions that result in recognition of a non-financial asset or liability, previous gains and losses recognised in other comprehensive income are included in the initial measurement of the asset or liability. When a hedge relationship is 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.

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.

(f) Employee compensation and benefits

Share-based payments

Shares in HSBC Holdings plc are awarded to employees in certain cases. Equity-settled share-based payment arrangements entitle employees to receive equity instruments of HSBC.

The vesting period for these schemes may commence before the grant date if the employees have started to render services in respect of the award before the grant date. 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 contributes to the Government pension and social security schemes in the countries in which it operates, as per local regulations. Where the group's obligations under the plans are equivalent to a defined contribution plan the payments made are charged as an expense as they fall due. End of service benefits are calculated and paid in accordance with local law. The group's net obligation in respect of such end of service benefits is the amount of future benefits that employees have earned in return for their service in current and prior periods.

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.

Re-measurements 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.

The group also makes contributions to the HSBC International Staff Retirement Benefit Scheme in respect of a small number of International Managers being seconded to the group by the HSBC Group. The group accounts for contributions to this scheme as if it is a defined contribution scheme on the basis that any actuarial gains and losses would not be material.

Notes on the Financial Statements

(g) 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 it 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 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.

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 in which the assets will be realised or the liabilities settled.

Current and deferred tax is calculated based on tax rates and laws enacted, or substantively enacted, by the balance sheet date.

Critical accounting estimates and judgements

The recognition of a deferred tax asset relies on an assessment of the probability and sufficiency of future taxable profits, future reversals of existing taxable temporary differences and ongoing tax planning strategies. In the absence of a history of taxable profits, the most significant judgements relate to expected future profitability and to the applicability of tax planning strategies.

(h) Debt securities in issue

Financial liabilities for debt securities issued are recognised when the group enters into contractual arrangements with counterparties and are initially measured at fair value, which is normally the consideration received, net of directly attributable transaction costs incurred. Subsequent measurement of financial liabilities, other than those measured at fair value through profit or loss and financial guarantees, is at amortised cost, using the effective interest method to amortise the difference between proceeds received, net of directly attributable transaction costs incurred, and the redemption amount over the expected life.

(i) 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 which 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 which 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.

(j) Acceptances and endorsements

Acceptances arise when the group is under an obligation to make payments against documents drawn under letters of credit. Acceptances specify the amount of money, the date, and the person to which the payment is due. After acceptance, the instrument becomes an unconditional liability (time draft) of the group and is therefore recognised as a financial liability with a corresponding contractual right of reimbursement from the customer recognised as a financial asset.

3 Net income/(expense) from financial instruments designated at fair value

	Footnote	2017 US\$000	2016 US\$000
Net income/(expense) arising on:			
– changes in own credit spread on long-term debt	1	–	(50)
– other changes in fair value		4,988	(159)
Year ended 31 Dec		4,988	(209)

1 From 1 January 2017, the group adopted, in its consolidated financial statements, the requirements of IFRS 9 'Financial Instruments' relating to the presentation of gains and losses on financial liabilities designated at fair value. As a result, changes in fair value attributable to changes in own credit risk are presented in other comprehensive income with the remaining effect presented in profit or loss.

4 Operating profit

Operating profit is stated after the following items:

	2017 US\$000	2016 US\$000
Income		
Interest recognised on impaired financial assets	11,353	18,154
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)	426,002	432,968
Fees earned on trust and other fiduciary activities	21,355	20,538
Expense		
Interest on financial instruments, excluding interest on financial liabilities held for trading or designated at fair value	(144,471)	(133,980)
Fees payable on financial liabilities that are not at fair value through profit or loss (other than amounts included in determining the effective interest rate)	(67,633)	(42,038)
Fees payable relating to trust and other fiduciary activities	–	–
Payments under lease agreements	(24,955)	(31,246)
Gains/(losses)		
Impairment of available-for-sale equity securities	(2,660)	(9,782)
Gains/(losses) recognised on assets held for sale	55,438	(26,900)
Losses on disposal or settlement of loans and advances	(145)	(5,260)
Gains on disposal of property, plant and equipment, intangible assets and non-financial investments	16,805	12,354
Loan impairment charges and other credit risk provisions	(149,912)	(150,355)
– net impairment charge on loans and advances	(141,228)	(124,630)
– other credit risk provisions	(8,684)	(25,725)

5 Employee compensation and benefits

	2017 US\$000	2016 US\$000
Wages and salaries	490,572	478,485
Social security costs	5,059	5,379
Post-employment benefits	26,630	27,698
Year ended 31 Dec	522,261	511,562

Average number of persons employed by the group during the year

	2017	2016
Retail Banking and Wealth Management	1,266	1,274
Commercial Banking	672	685
Global Banking and Markets	427	457
Global Private Banking	9	9
Corporate Centre	1,432	1,545
Total	3,806	3,970

Year in which income statement is expected to reflect deferred bonuses

	Current year bonus pool ¹ US\$000	Prior year bonus pools US\$000	Total US\$000
2017			
Charge recognised in 2017	4,767	5,687	10,454
– deferred share awards	2,268	4,330	6,598
– deferred cash awards	2,499	1,357	3,856
Charge expected to be recognised in 2018 or later	6,657	4,921	11,578
– deferred share awards	4,204	3,481	7,685
– deferred cash awards	2,453	1,440	3,893
2016			
Charge recognised in 2016	4,713	7,100	11,813
– deferred share awards	2,466	5,908	8,374
– deferred cash awards	2,247	1,192	3,439
Charge expected to be recognised in 2017 or later	5,694	5,626	11,320
– deferred share awards	3,908	4,028	7,936
– deferred cash awards	1,786	1,598	3,384

¹ Current year bonus pool relates to the bonus pool declared for the reporting period (2017 for the current year, 2016 for the 2016 comparatives).

Deferred cash awards are recognised where there is a service period over which conditions are required to be satisfied in order for an employee to become unconditionally entitled to the cash.

Notes on the Financial Statements

Share-based payments

'Wages and salaries' include the effect of share-based payments arrangements, all equity settled, as follows:

	2017 US\$000	2016 US\$000
Restricted share awards	9,818	11,962
Savings-related and other share award option plans	18	12
Year ended 31 Dec	9,836	11,974

HSBC share awards

Award	Policy
Restricted share awards (including annual incentive awards delivered in shares) and GPSP	<ul style="list-style-type: none"> 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.

Movement on HSBC share awards

	2017 Number (000s)	2016 Number (000s)
Restricted share awards outstanding at 1 Jan	4,041	2,497
Additions during the year	1,915	4,102
Released and forfeited in the year	(2,368)	(2,558)
Restricted share awards outstanding at 31 Dec	3,588	4,041
Weighted average fair value of awards granted (£)	7.26	6.10

HSBC share option plans

Main plans	Policy
Savings-related share option plans ('Sharesave')	<ul style="list-style-type: none"> Exercisable within six months following either the third or fifth anniversaries of the commencement of a three-year or five-year contract, respectively. The exercise price is set at a 20% (2016: 20%) discount to the market value immediately preceding the date of invitation.

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 (000s)	WAEP ¹ £
Outstanding at 1 Jan 2017	131	7.21
Granted during the year	11	7.91
Exercised during the year	(57)	7.52
Transferred during the year	1	4.79
Forfeited, expired and cancelled during the year	(12)	7.46
Outstanding at 31 Dec 2017	74	7.03
Weighted average remaining contractual life (years)	1.83	
Outstanding at 1 Jan 2016	214	4.59
Granted during the year	6	5.38
Exercised during the year	(51)	7.39
Transferred during the year	78	5.47
Forfeited, expired and cancelled during the year	(116)	7.52
Outstanding at 31 Dec 2016	131	7.21
Weighted average remaining contractual life (years)	1.72	

¹ Weighted average exercise price.

Post-employment benefit plans

Income statement charge

	2017 US\$000	2016 US\$000
Defined benefit pension plans	24,049	25,669
Defined contribution pension plans	2,512	1,930
Defined benefit and contribution healthcare plans	69	99
Year ended 31 Dec	26,630	27,698

Net liabilities recognised on the balance sheet in respect of defined benefit plans

	2017 US\$000	2016 US\$000
Net employee benefit liabilities (Note 23)	(175,445)	(144,520)

Defined benefit pension plans

Net asset/(liability) under defined benefit pension plans

	Fair value of plan assets US\$000	Present value of defined benefit obligations US\$000	Net defined benefit liability US\$000
At 1 Jan 2017	–	(144,520)	(144,520)
Service cost	–	(21,574)	(21,574)
– Current service cost	–	(21,574)	(21,574)
– Past service cost and gains from settlements	–	–	–
Net interest cost on the net defined benefit liability	–	(2,475)	(2,475)
Re-measurement effects recognised in other comprehensive income	–	(16,553)	(16,553)
– actuarial losses	–	(16,553)	(16,553)
Exchange differences and other movements	–	(1,145)	(1,145)
Contributions by the group	–	–	–
– normal	–	–	–
Benefits paid	–	10,822	10,822
At 31 Dec 2017	–	(175,445)	(175,445)
Present value of defined benefit obligation relating to:		(175,445)	
– actives	–	(163,134)	–
– deferreds	–	(12,311)	–
At 1 Jan 2016	4,864	(144,713)	(139,849)
Service cost	–	(22,965)	(22,965)
– Current service cost	–	(23,027)	(23,027)
– Past service cost and gains from settlements	–	62	62
Net interest cost on the net defined benefit liability	–	(2,548)	(2,548)
Re-measurement effects recognised in other comprehensive income	–	2,432	2,432
– actuarial gains	–	2,432	2,432
Exchange differences and other movements	(4,227)	7,313	3,086
Contributions by the group	536	–	536
– normal	536	–	536
Benefits paid	(1,173)	15,961	14,788
At 31 Dec 2016	–	(144,520)	(144,520)
Present value of defined benefit obligation relating to:		(144,520)	
– actives	–	(134,540)	–
– deferreds	–	(9,980)	–

Post-employment defined benefit plans' principal actuarial financial assumptions

The principal actuarial financial assumptions used to calculate the group's obligations under its defined benefit pension plans at 31 December for each year, and used as the basis for measuring periodic costs under the plans in the following years, were as follows:

Key actuarial assumptions for the principal plan

	Discount rate %	Rate of pay increase %	Combined rate of resignation and employment termination %
United Arab Emirates			
At 31 Dec 2017	2.20	6.40	9.30
At 31 Dec 2016	1.80	5.00	12.30

The group determines discount rates to be applied to its obligations in consultation with the plans' local actuaries, on the basis of current average yields of long term, high quality corporate bonds.

Notes on the Financial Statements

The effect of changes in key assumptions on the principal plan

	United Arab Emirates	
	2017 US\$000	2016 US\$000
Discount rate		
Change in scheme obligation at year end from a 25bps increase	(3,250)	(2,267)
Change in scheme obligation at year end from a 25bps decrease	3,367	2,350
Change in following year scheme cost from a 25bps increase	(170)	(73)
Change in following year scheme cost from a 25bps decrease	176	73
Rate of pay increase		
Change in scheme obligation at year end from a 25bps increase	3,393	2,414
Change in scheme obligation at year end from a 25bps decrease	(3,293)	(2,341)
Change in following year scheme cost from a 25bps increase	645	445
Change in following year scheme cost from a 25bps decrease	(626)	(434)

6 Auditors' remuneration

	2017 US\$000	2016 US\$000
Audit fees payable to PwC	1,384	826
Other audit fees payable	34	52
Year ended 31 Dec	1,418	878

Fees payable by the group to PwC

	Footnotes	2017 US\$000	2016 US\$000
Fees for HSBC Bank Middle East Limited statutory audit	1	1,384	826
– relating to current year		1,329	834
– relating to prior year		55	(8)
Fees for other services provided to the group		1,416	1,238
– audit-related assurance services	2	705	802
– taxation-related services		323	214
– other non-audit services		388	222
Year ended 31 Dec		2,800	2,064

1 Fees payable to PwC for the statutory audit of the consolidated financial statements of the group.

2 Including services for assurance and other services that relate to statutory and regulatory filings, including comfort letters and interim reviews.

No fees were payable by the group to PwC as principal auditor for the following types of services: internal audit services and services related to litigation, recruitment and remuneration.

7 Tax

Tax expense

	2017 US\$000	2016 US\$000
Current tax	87,864	94,399
– for this year	94,798	89,430
– adjustments in respect of prior years	(6,934)	4,969
Deferred tax	4,140	18,295
– origination and reversal of temporary differences	4,140	25,295
– adjustments in respect of prior years	–	(7,000)
Year ended 31 Dec	92,004	112,694

The group provides for taxation at the appropriate rates in the countries in which it operates.

Tax reconciliation

The tax charged to the income statement differs from the tax charge that would apply if all profits had been taxed at the UAE corporation tax rate as follows:

	2017		2016	
	US\$000	%	US\$000	%
Profit before tax	637,357		649,795	
Tax expense				
Taxation at UAE corporate tax rate of 20% (2016: 20%)	127,471	20.0	129,959	20.0
Effect of differently taxed overseas profits	(17,368)	(2.7)	(5,051)	(0.8)
Adjustments in respect of prior period liabilities	(7,200)	(1.1)	(2,032)	(0.3)
Non-taxable income and gains	(22,379)	(3.5)	(17,951)	(2.8)
Permanent disallowables	188	—	5,517	0.8
Local taxes and overseas withholding taxes	11,797	1.9	2,260	0.3
Other items	(505)	(0.1)	(8)	—
Overall tax expense	92,004	14.4	112,694	17.3

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 group only recognises current and deferred tax assets where recovery is probable.

Movement of deferred tax assets and liabilities

	Retirement benefits	Loan impairment allowances	Revaluation of property	Other	Total
	US\$000	US\$000	US\$000	US\$000	US\$000
Assets	11,194	190,058	—	7,859	209,111
Liabilities	—	—	(523)	—	(523)
At 1 Jan 2017	11,194	190,058	(523)	7,859	208,588
Income statement	—	(4,165)	523	(498)	(4,140)
Other comprehensive income	1,391	—	—	—	1,391
Foreign exchange and other adjustments	—	(22)	—	40	18
At 31 Dec 2017	12,585	185,871	—	7,401	205,857
Assets	12,585	185,871	—	7,401	205,857
Liabilities	—	—	—	—	—
Assets	11,318	205,887	—	10,715	227,920
Liabilities	—	—	(523)	—	(523)
At 1 Jan 2016	11,318	205,887	(523)	10,715	227,397
Income statement	—	(15,827)	—	(2,468)	(18,295)
Other comprehensive income	(123)	—	—	—	(123)
Foreign exchange and other adjustments	(1)	(2)	—	(388)	(391)
At 31 Dec 2016	11,194	190,058	(523)	7,859	208,588
Assets	11,194	190,058	—	7,859	209,111
Liabilities	—	—	(523)	—	(523)

Unrecognised deferred tax

The amount of temporary differences, unused tax losses and tax credits for which no deferred tax asset is recognised in the balance sheet was nil (2016: nil).

8 Dividends

Dividends to shareholders of the parent company

	2017		2016	
	Per share	Total	Per share	Total
	US\$	US\$000	US\$	US\$000
Dividends paid on ordinary shares				
In respect of previous year:				
– fourth interim dividend	0.0269	25,000	0.2256	210,000
In respect of current year:				
– first interim dividend	0.1482	138,000	0.2256	210,000
– second interim dividend	0.1729	161,000	0.0806	75,000
– special dividend	—	—	0.5370	500,000
– third interim dividend	0.1138	106,000	0.1074	100,000
Total	0.4618	430,000	1.1762	1,095,000

On 13 February 2018, the Directors declared a fourth interim dividend in respect of the financial year ended 31 December 2017 of US\$0.1504 per ordinary share, a distribution of US\$140 million.

9 Segment analysis

Profit/(loss) for the year

	2017					
	Retail Banking and Wealth Management	Commercial Banking	Global Banking and Markets	Global Private Banking	Corporate Centre	Total
	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000
Net interest income	382,556	213,829	220,537	—	89,570	906,492
Net fee income/(expense)	105,936	132,551	203,472	—	(6,914)	435,045
Net trading income/(expense)	38,026	29,275	159,673	—	(10,726)	216,248
Other income	16,811	15,391	16,552	163	81,248	130,165
Net operating income before loan impairment charges and other credit risk	543,329	391,046	600,234	163	153,178	1,687,950
Loan impairment charges and other credit risk provisions	(74,539)	(57,708)	(17,665)	—	—	(149,912)
Net operating income	468,790	333,338	582,569	163	153,178	1,538,038
Total operating expenses	(334,980)	(232,023)	(246,973)	(163)	(86,832)	(900,971)
Operating profit	133,810	101,315	335,596	—	66,346	637,067
Share of profit in associates	—	—	—	—	290	290
Profit before tax	133,810	101,315	335,596	—	66,636	637,357
By geographical region						
U.A.E.	110,156	52,702	256,909	—	45,468	465,235
Qatar	12,743	24,178	68,020	—	3,380	108,321
Rest of Middle East	10,911	24,435	10,667	—	17,788	63,801
Profit before tax	133,810	101,315	335,596	—	66,636	637,357

	2016					
Net interest income	395,605	228,038	197,336	—	95,855	916,834
Net fee income/(expense)	119,186	155,121	203,427	—	(3,857)	473,877
Net trading income/(expense)	43,347	43,306	182,704	—	(17,521)	251,836
Other income/(expenses)	(4,600)	3,459	11,897	116	24,630	35,502
Net operating income before loan impairment charges and other credit risk	553,538	429,924	595,364	116	99,107	1,678,049
Loan impairment charges and other credit risk provisions	(106,854)	(28,556)	(14,445)	—	(500)	(150,355)
Net operating income	446,684	401,368	580,919	116	98,607	1,527,694
Total operating expenses	(345,290)	(218,229)	(232,752)	(116)	(83,391)	(879,778)
Operating profit	101,394	183,139	348,167	—	15,216	647,916
Share of profit in associates	—	—	—	—	1,879	1,879
Profit before tax	101,394	183,139	348,167	—	17,095	649,795

By geographical region

U.A.E.	83,349	93,608	284,554	—	7,242	468,753
Qatar	9,888	41,823	56,820	—	(4,705)	103,826
Rest of Middle East	8,157	47,708	6,793	—	14,558	77,216
Profit before tax	101,394	183,139	348,167	—	17,095	649,795

Balance sheet information

	2017					
	Retail Banking and Wealth Management	Commercial Banking	Global Banking and Markets	Global Private Banking	Corporate Centre	Total
	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000
Loans and advances to customers (net)	3,788,578	6,033,990	8,492,130	—	2,082	18,316,780
Interest in associates	—	—	—	—	1,948	1,948
Total assets	3,800,405	6,369,620	12,801,850	—	12,699,034	35,670,909
Customer accounts	10,647,785	4,562,150	6,846,188	—	527,526	22,583,649
Total liabilities	10,838,029	5,736,970	10,744,100	—	4,045,975	31,365,074
2016						
Loans and advances to customers (net)	4,045,873	6,333,490	10,618,598	—	12,612	21,010,573
Interest in associates	—	—	—	—	1,658	1,658
Total assets	4,308,355	6,963,158	14,308,069	—	13,088,770	38,668,352
Customer accounts	10,617,868	5,325,799	6,066,278	—	578,982	22,588,927
Total liabilities	11,356,923	6,615,091	10,191,701	—	6,330,541	34,494,256

Other financial information

Net operating income by global business

	Footnote	2017					Total US\$000
		Retail Banking and Wealth Management US\$000	Commercial Banking US\$000	Global Banking and Markets US\$000	Global Private Banking US\$000	Corporate Centre US\$000	
Net operating income	1	543,329	391,046	600,234	163	153,178	1,687,950
– external		439,999	434,724	650,102	–	163,125	1,687,950
– internal		103,330	(43,678)	(49,868)	163	(9,947)	–
2016							
Net operating income	1	553,538	429,924	595,364	116	99,107	1,678,049
– external		488,835	502,375	658,205	–	28,634	1,678,049
– internal		64,703	(72,451)	(62,841)	116	70,473	–

1 Net operating income before loan impairment charges and other credit risk provisions, also referred to as revenue.

Information by country

	2017		2016	
	External net operating income ¹ US\$000	Non-current assets ² US\$000	External net operating income ¹ US\$000	Non-current assets ² US\$000
	U.A.E.	1,303,304	44,405	1,265,825
Qatar	197,261	4,435	199,395	5,347
Rest of Middle East	187,385	11,850	212,829	13,081
Total	1,687,950	60,690	1,678,049	77,769

1 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.

2 Non current assets consist of property, plant and equipment, other intangible assets and certain other assets expected to be recovered more than 12 months after the reporting period.

Performance ratios

	2017					
	Retail Banking and Wealth Management %	Commercial Banking %	Global Banking and Markets %	Global Private Banking %	Corporate Centre %	Total %
Year ended 31 December 2017						
Share of the group's profit before tax	21.0	15.9	52.6	–	10.5	100.0
Cost efficiency ratio	61.7	59.3	41.1	100.0	56.7	53.4
2016						
Year ended 31 December 2016						
Share of the group's profit before tax	15.6	28.2	53.6	–	2.6	100.0
Cost efficiency ratio	62.4	50.8	39.1	100.0	84.1	52.4

10 Trading assets

	2017 US\$000	2016 US\$000
Trading assets:		
– not subject to repledge or resale by counterparties	440,624	182,406
At 31 Dec	440,624	182,406
Debt securities	280,747	103,787
Treasury and other eligible bills	46,294	–
Trading securities	327,041	103,787
Loans and advances to banks	53,231	44,828
Loans and advances to customers	60,352	33,791
At 31 Dec	440,624	182,406

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.

Where fair values are determined by reference to externally quoted prices or observable pricing inputs to models, independent price determination or validation is used. For inactive markets, the group sources alternative market information, with greater weight given to information that is considered to be more relevant and reliable. Examples of the factors considered are price observability, instrument comparability, consistency of data sources, underlying data accuracy and timing of prices.

For fair values determined using valuation models, the control framework includes development or validation by independent support functions of the model logic, inputs, model outputs and adjustments. Valuation models are subject to a process of due diligence 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 concerned, where available. An example of this is where own debt in issue is hedged with interest rate derivatives. When quoted market prices are unavailable, the own debt in issue is valued using valuation techniques, the inputs for which are either based upon 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 which is appropriate to the group's liabilities. The change in fair value of issued debt securities attributable to the group's own credit spread is computed as follows: for each security at each reporting date, an externally verifiable price is obtained or a price is derived using credit spreads for similar securities for the same issuer. Then, using discounted cash flow, each security is valued using a Libor-based discount curve. The difference in the valuations is attributable to the group's own credit spread. This methodology is applied consistently across all securities.

Structured notes issued and certain other hybrid instrument liabilities are included within trading liabilities and are measured at fair value. The credit spread applied to these instruments is derived from the spreads at which the group issues structured notes.

Gains and losses arising from changes in the credit spread of liabilities issued by the group reverse over the contractual life of the debt, provided that the debt is not repaid at a premium or a discount.

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 the group 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

	2017				2016			
	Level 1 US\$000	Level 2 US\$000	Level 3 US\$000	Total US\$000	Level 1 US\$000	Level 2 US\$000	Level 3 US\$000	Total US\$000
Recurring fair value measurements at 31 Dec								
Assets								
Trading assets	–	440,624	–	440,624	–	182,406	–	182,406
Derivatives	–	960,097	3,005	963,102	–	1,312,021	7,230	1,319,251
Financial investments: available for sale	–	6,628,271	118,233	6,746,504	–	6,511,701	70,480	6,582,181
Liabilities								
Trading liabilities	–	1,309,860	–	1,309,860	–	1,496,561	–	1,496,561
Financial liabilities designated at fair value	–	739,425	–	739,425	–	401,592	–	401,592
Derivatives	–	949,327	3,005	952,332	–	1,401,810	7,230	1,409,040

Transfers between levels of the fair value hierarchy are deemed to occur at the end of each semi-annual reporting period. The transfers between levels during the year are updated in 'Movement in Level 3 financial instruments'.

Fair value adjustments

Fair value adjustments are adopted when the group considers that there are additional factors that would be considered by a market participant which are not incorporated within the valuation model. The group classifies fair value adjustments as either 'risk-related' or 'model-related'. The majority of these adjustments relate to Global Banking and Markets.

Movements in the level of fair value adjustments do not necessarily result in the recognition of profits or losses within the income statement. For example, as models are enhanced, fair value adjustments may no longer be required. Similarly, fair value adjustments will decrease when the related positions are unwound, but this may not result in profit or loss.

Risk-related adjustments

Bid-offer

IFRS 13 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 cost 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, there exists a range of possible values that the financial instrument or market parameter may assume and an adjustment may be necessary to reflect the likelihood that in estimating the fair value of the financial instrument, 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 adjustment

The credit valuation adjustment is an adjustment to the valuation of OTC derivative contracts to reflect within fair value the possibility that the counterparty may default and that the group may not receive the full market value of the transactions.

The debit valuation adjustment is an adjustment to the valuation of OTC derivative contracts to reflect within fair value the possibility that the group may default, and that the group may not pay full market value of the transactions.

The group calculates a separate credit valuation adjustment ('CVA') and debit valuation adjustment ('DVA') for each group legal entity, and within each entity for each counterparty to which the entity has exposure.

The group calculates the CVA by applying the probability of default ('PD') of the counterparty conditional on the non-default of the group to the expected positive exposure to the counterparty and multiplying the result by the loss expected in the event of default. Conversely, the group calculates the DVA by applying the PD of the group, conditional on the non-default of the counterparty, to the expected positive exposure of the counterparty to the group and multiplying by the loss expected in the event of default. Both calculations are performed over the life of the potential exposure.

Funding fair value adjustment

The funding fair value adjustment is calculated by applying future market funding spreads to the expected future funding exposure of any uncollateralised component of the OTC derivative portfolio. This includes the uncollateralised component of collateralised derivatives in addition to derivatives that are fully uncollateralised. The expected future funding exposure is calculated by a simulation methodology, where available. The expected future funding exposure is adjusted for events that may terminate the exposure such as the default of the group or the counterparty.

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.

Fair value valuation bases

Financial instruments measured at fair value using a valuation technique with significant unobservable inputs – Level 3

	Assets			Liabilities	
	Available for sale	Derivatives	Total	Derivatives	Total
	US\$000	US\$000	US\$000	US\$000	US\$000
Private equity including strategic investments	118,233	–	118,233	–	–
Other derivatives	–	3,005	3,005	3,005	3,005
At 31 Dec 2017	118,233	3,005	121,238	3,005	3,005
Private equity including strategic investments	70,480	–	70,480	–	–
Other derivatives	–	7,230	7,230	7,230	7,230
At 31 Dec 2016	70,480	7,230	77,710	7,230	7,230

Private equity including strategic investments

The group's private equity positions are generally classified as available-for-sale and are not traded in active markets. In the absence of an active market, an 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, as well as by reference to market valuations for similar entities quoted in an active market, or the price at which similar companies have changed ownership.

Derivatives

OTC (i.e. non-exchange traded) derivatives are valued using valuation models. Valuation models calculate the present value of expected future cash flows, based upon 'no-arbitrage' principles. For many vanilla derivative products, such as interest rate swaps and European options, 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 via model calibration procedures or estimated from historical data or other sources.

Notes on the Financial Statements

Reconciliation of fair value measurements in Level 3 of the fair value hierarchy

Movement in Level 3 financial instruments

	Assets		Liabilities
	Available for sale US\$000	Derivatives US\$000	Derivatives US\$000
At 1 Jan 2017	70,480	7,230	7,230
Total gains/(losses) recognised in profit or loss	(2,870)	59,577	59,577
– trading income excluding net interest income	–	59,577	59,577
– gains less losses from financial investments	(2,870)	–	–
Total losses recognised in other comprehensive income ('OCI')	(2,119)	–	–
– available-for-sale investments: fair value losses	(2,160)	–	–
– exchange differences	41	–	–
Purchases	61,346	–	–
Sales	(8,604)	–	–
Transfers out	–	(63,802)	(63,802)
Transfers in	–	–	–
At 31 Dec 2017	118,233	3,005	3,005
Unrealised gains/(losses) recognised in profit or loss relating to assets and liabilities held at 31 Dec 2017	(2,652)	3,005	(3,005)
– trading income/(expense) excluding net interest income	–	3,005	(3,005)
– gains less losses from financial investments	(2,652)	–	–
At 1 Jan 2016	102,624	2,222	20,999
Total gains/(losses) recognised in profit or loss	2,527	1,610	(17,601)
– trading income/(expense) excluding net interest income	–	1,610	(17,601)
– gains less losses from financial investments	2,527	–	–
Total losses recognised in other comprehensive income ('OCI')	(12,808)	–	–
– available-for-sale investments: fair value losses	(12,793)	–	–
– exchange differences	(15)	–	–
Purchases	–	–	–
Sales	(22,012)	–	–
Transfers out	–	–	–
Transfers in	149	3,398	3,832
At 31 Dec 2016	70,480	7,230	7,230
Unrealised gains/(losses) recognised in profit or loss relating to assets and liabilities held at 31 Dec 2016	(9,782)	7,230	(7,230)
– trading income/(expense) excluding net interest income	–	7,230	(7,230)
– gains less losses from financial investments	(9,782)	–	–

Effect of changes in significant unobservable assumptions to reasonably possible alternatives

Sensitivity of Level 3 fair values to reasonably possible alternative assumptions

	Footnote	2017				2016			
		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
		US\$000	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000
Derivatives, trading assets and trading liabilities	1	301	(301)	–	–	723	(723)	–	–
Financial investments: available for sale		2,443	(1,222)	9,380	(4,690)	2,566	(1,283)	3,106	(2,241)
At 31 Dec		2,744	(1,523)	9,380	(4,690)	3,289	(2,006)	3,106	(2,241)

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

	2017				2016			
	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
	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000
Private equity including strategic investments	2,443	(1,222)	9,380	(4,690)	2,566	(1,283)	3,106	(2,241)
Other derivatives	301	(301)	–	–	723	(723)	–	–
At 31 Dec	2,744	(1,523)	9,380	(4,690)	3,289	(2,006)	3,106	(2,241)

Favourable and unfavourable changes are determined on the basis of changes in the value of the instrument as a result of varying the levels of the unobservable parameters using statistical techniques. The statistical techniques aim to apply a 95% confidence interval. When parameters are not amenable to statistical analysis, the quantification of uncertainty is judgemental, but is also guided by the 95% confidence interval.

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		2017				2016			
	Assets	Liabilities	Full range of inputs		Core range of inputs ¹		Full range of inputs		Core range of inputs ¹	
	US\$000	US\$000	Lower	Higher	Lower	Higher	Lower	Higher	Lower	Higher
Private equity including strategic investments	118,233	—	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Interest rate derivatives	—	—	—	—	—	—	45.3%	98.5%	57.1%	98.0%
FX derivatives	3,005	3,005	0.4%	5.0%	0.4%	5.0%	0.6%	3.6%	0.6%	3.6%
At 31 Dec 2017	121,238	3,005								

¹ The core range of inputs is the estimated range within which 90% of the inputs fall.

A description of the categories of key unobservable inputs is given below.

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 for which specific market pricing is not available, but evidence is available in respect of instruments that have 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 are 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 group 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, group 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 a 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. Credit spreads 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 impact of changing market variables upon the group portfolio will depend upon the group'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				Total US\$000
	Carrying amount US\$000	Quoted market price Level 1 US\$000	Observable inputs Level 2 US\$000	Significant unobservable inputs Level 3 US\$000	
	At 31 Dec 2017				
Assets					
Loans and advances to banks	6,203,202	–	6,194,592	–	6,194,592
Loans and advances to customers	18,316,780	–	–	18,155,119	18,155,119
Reverse repurchase agreements – non-trading	1,387,254	–	1,387,254	–	1,387,254
Liabilities					
Deposits by banks	1,798,474	–	1,797,266	–	1,797,266
Customer accounts	22,583,649	–	22,793,255	–	22,793,255
Debt securities in issue	2,092,390	–	2,028,795	–	2,028,795
At 31 Dec 2016					
Assets					
Loans and advances to banks	6,249,298	–	6,271,084	–	6,271,084
Loans and advances to customers	21,010,573	–	–	20,914,443	20,914,443
Reverse repurchase agreements – non-trading	1,050,843	–	1,050,843	–	1,050,843
Liabilities					
Deposits by banks	3,246,654	–	3,246,307	–	3,246,307
Customer accounts	22,588,927	–	22,778,320	–	22,778,320
Debt securities in issue	2,645,483	–	2,554,319	–	2,554,319

Other financial instruments not carried at fair value are typically short-term in nature and re-priced to current market rates frequently. Accordingly, their carrying amount is a reasonable approximation of fair value.

Valuation

The fair value measurement is the group's 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 the group expects to flow from the instruments' cash flows over their expected future lives. Other reporting entities may use different valuation methodologies and assumptions in determining fair values for which no observable market prices are available.

Loans and advances to banks and customers

The fair value of loans and advances is based on observable market transactions, where available. In the absence of observable market transactions, fair value is estimated using valuation models that incorporate a range of input assumptions. These assumptions may include forward looking discounted cash flow models using assumptions which the group believes are consistent with those which would be used by market participants in valuing such loans; and trading inputs from other market participants which includes observed primary and secondary trades.

Loans are grouped, as far as possible, into homogeneous groups and stratified by loans with similar characteristics to improve the accuracy of estimated valuation outputs. The stratification of a loan book considers all material factors, including vintage, origination period, estimates of future interest rates, prepayment speeds, delinquency rates, loan-to-value ratios, the quality of collateral, default probability, and internal credit risk ratings.

The fair value of a loan reflects both loan impairments 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.

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 take into consideration the prices and future earnings streams of equivalent quoted securities.

Deposits by banks and customer accounts

Fair values are estimated using discounted cash flows, applying current rates offered for deposits of similar remaining maturities. The fair value of a deposit repayable on demand is approximated by its carrying value.

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 their balances are generally short dated.

13 Derivatives

Notional contract amounts and fair values of derivatives by product contract type held by the group

	Notional contract amount		Fair value – Assets			Fair value – Liabilities		
	Trading US\$000	Hedging US\$000	Trading US\$000	Hedging US\$000	Total US\$000	Trading US\$000	Hedging US\$000	Total US\$000
Foreign exchange	66,715,598	1,346,629	484,842	4,424	489,266	498,264	24	498,288
Interest rate	46,525,580	4,354,726	415,242	22,697	437,939	410,801	7,555	418,356
Equities	52,036	–	685	–	685	685	–	685
Credit	217,634	–	857	–	857	234	–	234
Commodity and other	1,168,608	–	34,355	–	34,355	34,769	–	34,769
At 31 Dec 2017	114,679,456	5,701,355	935,981	27,121	963,102	944,753	7,579	952,332
Foreign exchange	65,216,460	1,779,973	797,074	12,426	809,500	796,468	149,481	945,949
Interest rate	49,548,301	4,006,087	429,980	26,440	456,420	402,521	5,899	408,420
Equities	74,204	–	1,375	–	1,375	1,375	–	1,375
Credit	235,723	–	871	–	871	2,210	–	2,210
Commodity and other	64,807	–	51,085	–	51,085	51,086	–	51,086
At 31 Dec 2016	115,139,495	5,786,060	1,280,385	38,866	1,319,251	1,253,660	155,380	1,409,040

The notional contract amounts of derivatives held for trading purposes and derivatives designated in qualifying hedge accounting indicate the nominal value of transactions outstanding at the balance sheet date; they do not represent amounts at risk.

Use of derivatives

The group transacts derivatives 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 the group's own risks.

The group's derivative activities give rise to significant open positions in portfolios of derivatives. These positions are managed constantly to ensure that they remain within acceptable risk levels. When entering into derivative transactions, the group employs the same credit risk management framework to assess and approve potential credit exposures that it uses for traditional lending.

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.

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 valuation techniques used for subsequent measurement been applied at initial recognition, less subsequent releases, is nil (2016: nil).

Hedge accounting derivatives

Fair value hedges

The group's fair value hedges principally consist of interest rate swaps that are used to protect against changes in the fair value of fixed-rate long-term financial instruments due to movements in market interest rates.

Notional contract amounts and fair values of derivatives designated as fair value hedges by product type

	2017			2016		
	Notional US\$000	Assets US\$000	Liabilities US\$000	Notional US\$000	Assets US\$000	Liabilities US\$000
Interest rate	1,243,682	15,140	2,862	1,081,697	13,420	3,592
At 31 Dec	1,243,682	15,140	2,862	1,081,697	13,420	3,592

Gains or losses arising from fair value hedges

	2017 US\$000	2016 US\$000
Gains/(losses):		
– on hedging instruments	3,923	9,615
– on the hedged items attributable to the hedged risk	(4,334)	(9,506)
Year ended 31 Dec	(411)	109

Notes on the Financial Statements

Cash flow hedges

The group's cash flow hedges consist principally of interest rate swaps, futures and cross-currency swaps that are used to protect against exposures to variability in future interest cash flows on non-trading assets and liabilities which bear interest at variable rates or which are expected to be re-funded or reinvested in the future. 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 principal balances and interest cash flows across all portfolios over time form the basis for identifying gains and losses on the effective portions of derivatives designated as cash flow hedges of forecast transactions.

Notional contract amounts and fair values of derivatives designated as cash flow hedges by product type

	2017			2016		
	Notional US\$000	Assets US\$000	Liabilities US\$000	Notional US\$000	Assets US\$000	Liabilities US\$000
Foreign exchange	1,346,629	4,424	24	1,779,973	12,426	149,481
Interest rate	3,111,044	7,557	4,693	2,924,390	13,020	2,307
At 31 Dec	4,457,673	11,981	4,717	4,704,363	25,446	151,788

Forecast principal balances on which interest cash flows are expected to arise

	3 months or less US\$000	More than 3 months but less than 1 year US\$000	5 years or less but more than 1 year US\$000	More than 5 years US\$000
Net cash inflows exposure				
Assets		3,507,289	3,960,191	1,928,606
Liabilities		–	–	–
At 31 Dec 2017		3,507,289	3,960,191	1,928,606
Net cash inflows/(outflows) exposure				
Assets		4,454,018	2,373,932	912,128
Liabilities		(250,494)	(250,484)	–
At 31 Dec 2016		4,203,524	2,123,448	912,128

This table reflects the interest rate repricing profile of the underlying hedged items. During the year to 31 December 2017 the losses of US\$0.2 million (31 December 2016: nil) were recognised due to hedge ineffectiveness.

14 Financial investments

Carrying amount of financial investments

	2017 US\$000	2016 US\$000
Available for sale securities at fair value		
Treasury and other eligible bills	1,326,312	1,274,331
Debt securities	5,301,959	5,237,370
Equity securities	118,233	70,480
At 31 Dec	6,746,504	6,582,181

15 Assets charged as security for liabilities, and collateral accepted as security for assets

Collateral accepted as security for assets

The fair value of financial assets accepted as collateral that the group is permitted to sell or repledge in the absence of default is US\$1,410 million (2016: US\$1,051 million). The fair value of any such collateral sold or repledged is nil (2016: nil). The group is obliged to return these assets. These transactions are conducted under terms that are usual and customary to standard securities borrowing and reverse repurchase agreements.

16 Interests in associates and joint arrangement

Associates of the group

	At 31 Dec 2017			
	Country of incorporation	Principal activity	The group's interest in equity capital	Issued equity capital
MENA Infrastructure Fund (GP) Limited	Dubai, UAE	Private Equity fund management	33.33%	US\$0.99 million fully paid

The above associate is not considered significant to the group and is unlisted.

Summarised financial information in respect of associates not individually significant

	2017 US\$000	2016 US\$000
Carrying value	1,948	1,658
The group's share of		
– assets	2,180	1,827
– liabilities	232	169
– profit or loss from continuing operations	290	1,879
– total comprehensive income	290	1,879

Movements in interests in associates

	2017 US\$000	2016 US\$000
At 1 Jan	1,658	82,173
Disposals	–	(5,646)
Share of results	290	1,879
Dividends	–	(1,312)
Other movements and foreign exchange	–	9
Reclassification from associate to joint operation	–	(75,445)
At 31 Dec	1,948	1,658

Joint arrangement of the group

	At 31 Dec 2017			
	Country of incorporation	Principal activity	The group's interest in equity capital	Issued equity capital
HSBC Middle East Leasing Partnership - (Joint operation)	Dubai, UAE	Leasing	15.00%	US\$621 million fully paid

17 Investments in subsidiaries

Subsidiary undertakings of the bank

	At 31 Dec 2017	
	Country of incorporation or registration	Bank's interest in equity capital
HSBC Financial Services (Middle East) Limited (in liquidation)	Dubai, UAE	100%
HSBC Middle East Finance Company Limited	Dubai, UAE	80%
HSBC Middle East Securities LLC	Dubai, UAE	100%
HSBC Insurance Services (Lebanon) S.A.L. (in liquidation)	Lebanon	100%
HSBC Bank Middle East Representative Office Morocco S.A.R.L.	Morocco	100%

All the above prepare their financial statements up to 31 December and the countries of operation are the same as the countries of incorporation.

The subsidiary undertakings are unlisted, directly owned and are included in the consolidated financial statements of the group.

In order to comply with local legal requirements, the ownership of the investment in HSBC Middle East Securities LLC is held 49.00% in the name of the bank and 51.00% in the personal name of Mr. Abdul Wahid Al Ulama, as nominee. Under a Memorandum of Understanding, the nominee has transferred his legal and/or beneficial interest in HSBC Middle East Securities LLC to the bank. The total book value of the assets of HSBC Middle East Securities LLC amount to US\$3.2 million (2016: US\$3.5 million).

18 Prepayments, accrued income and other assets

	2017 US\$000	2016 US\$000
Prepayments and accrued income	82,271	75,857
Endorsements and acceptances	461,318	491,427
Other accounts	66,065	54,954
Property, plant and equipment	48,240	62,653
At 31 Dec	657,894	684,891

19 Assets held for sale and liabilities of disposal groups held for sale

	2017 US\$000	2016 US\$000
Held for sale at 31 Dec		
Disposal groups	–	851,691
Liabilities of disposal groups	–	804,272

Notes on the Financial Statements

Disposal groups

Lebanon

On 16 November 2016, the bank entered into an agreement with BLOM BANK S.A.L. to sell the banking operations in Lebanon and on 16 June 2017 completed the disposal.

20 Trading liabilities

The sale of borrowed securities is classified as trading liabilities.

	2017	2016
	US\$000	US\$000
Deposits by banks	6,457	4,963
Customer accounts	1,743	–
Other debt securities in issue (Note 22)	1,267,800	1,459,505
Other liabilities – net short positions in securities	33,860	32,093
At 31 Dec	1,309,860	1,496,561

21 Financial liabilities designated at fair value

	2017	2016
	US\$000	US\$000
Debt securities in issue (Note 22)	739,425	401,592

At 31 December 2017, the accumulated amount of change in fair value attributable to changes in credit risk was a loss of US\$2.8 million (2016: US\$0.8 million gain).

22 Debt securities in issue

	2017		2016	
	Carrying amount US\$000	Fair value US\$000	Carrying amount US\$000	Fair value US\$000
Medium-term notes	3,149,615	3,150,286	3,556,580	3,556,181
Non-equity preference shares	950,000	885,734	950,000	859,235
Total debt securities in issue	4,099,615	4,036,020	4,506,580	4,415,416
Included within:				
– trading liabilities (Note 20)	(1,267,800)	(1,267,800)	(1,459,505)	(1,459,505)
– financial liabilities designated at fair value (Note 21)	(739,425)	(739,425)	(401,592)	(401,592)
At 31 Dec	2,092,390	2,028,795	2,645,483	2,554,319

Certain debt securities in issue are managed on a fair value basis as part of the group's interest rate risk management policies. The hedged portion of these debt securities is presented within the balance sheet caption 'Financial liabilities designated at fair value', with the remaining portion included within 'Trading liabilities'.

Non-equity preference share capital

Authorised

The authorised non-equity preference share capital of the bank at 31 December 2017 and 31 December 2016 was 1,125,000 dated preference shares of US\$1.00 each and 225,000 undated preference shares of US\$1.00 each.

Issued

Undated preference shares

Issue number	Issue date	Undated preference shares		Preference dividends	Redeemable at the option of the bank on any date after
		Number	%		
1	29 October 1997	50,000	12 month US dollar LIBOR + 0.35	30 October 2002	
2	1 April 1998	25,000	12 month US dollar LIBOR + 0.70	2 April 2003	
6	14 March 2006	150,000	12 month US dollar LIBOR + 0.65	15 March 2011	

1 The undated preference shares have been issued at a nominal value of US\$1 each with a premium of US\$999 per share.

2 Preference dividends are payable annually on the issue price of each undated share.

3 The undated preference shares bear no mandatory redemption date. On redemption, the holders of the shares shall be entitled to receive an amount equal to any accrued but unpaid dividends plus the issue price of each share.

4 Each share carries one vote at meetings of the shareholders of the bank.

5 In the event of a winding up, the preference shareholders would receive, in priority to the ordinary shareholders of the bank, repayment of US\$1,000 per share, plus an amount equal to any accrued but unpaid dividends. With the exception of the above, the preference shares do not carry any right to participate in the surplus of assets on a winding up.

Dated preference shares

Issue number	Issue date	Dated preference shares		Preference dividends	Redeemable at the option of the bank on any date after	
		Number			%	Date
11	16 December 2014	250,000		3 month US dollar LIBOR + 2.40		16 December 2019
11	16 December 2014	250,000		3 month US dollar LIBOR + 2.70		16 December 2024
12	30 December 2014	225,000		3 month US dollar LIBOR + 2.70		30 December 2024

1 The dated preference shares have been issued at a nominal value of US\$1 each with a premium of US\$999 per share.

2 Preference dividends are payable quarterly on the issue price of each dated share.

3 Redemption of the dated preference shares, other than at the option of the bank, will be subject to the approval of the ordinary shareholders of the bank. The earliest redemption date is as disclosed in the table above and if not approved by the shareholders will next fall for review at 10 yearly intervals thereafter. However, the shares may be redeemed at the option of the Bank without the approval of the ordinary shareholders of the bank. On redemption, the holders of the shares shall be entitled to receive an amount equal to any accrued but unpaid dividends plus the issue price of each share.

4 In the event of a winding up, the preference shareholders would receive, in priority to the ordinary shareholders of the bank, repayment of US\$1,000 per share, plus an amount equal to any accrued but unpaid dividends. With the exception of the above, the preference shares do not carry any right to participate in the surplus of assets on a winding up.

23 Accruals, deferred income and other liabilities

	2017	2016
	US\$000	US\$000
Accruals and deferred income	194,893	151,271
Share-based payments liability to HSBC Holdings plc	16,981	16,187
Endorsements and acceptances	461,318	491,427
Employee benefit liabilities (Note 5)	175,445	144,520
Other liabilities	771,056	813,929
At 31 Dec	1,619,693	1,617,334

24 Provisions

	Legal proceedings and regulatory matters					Total
	Restructuring costs	Contractual commitments	Legal proceedings and regulatory matters	Customer remediation	Other provisions	
	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000
At 1 Jan 2017	5,032	8,391	7,420	3,150	19,796	43,789
Additions	6,749	8,193	21,715	375	11,109	48,141
Amounts utilised	(3,623)	—	(849)	(690)	(8,888)	(14,050)
Unused amounts reversed	(1,398)	—	(1,580)	(2,597)	(89)	(5,664)
Exchange and other movements	2	(953)	646	—	(303)	(608)
At 31 Dec 2017	6,762	15,631	27,352	238	21,625	71,608
At 1 Jan 2016	10,008	—	2,508	2,019	9,161	23,696
Additions	5,649	2,674	5,700	2,992	13,034	30,049
Amounts utilised	(6,575)	—	(987)	(6)	(4,299)	(11,867)
Unused amounts reversed	(3,844)	—	(15)	(1,721)	—	(5,580)
Exchange and other movements	(206)	5,717	214	(134)	1,900	7,491
At 31 Dec 2016	5,032	8,391	7,420	3,150	19,796	43,789

25 Maturity analysis of assets, liabilities and off-balance sheet commitments

The following is an analysis by remaining contractual maturities at the balance sheet date, of assets and liability line items that combine amounts expected to be recovered or settled within one year and after more than one year.

Trading assets and liabilities are excluded because they are not held for collection or settlement over the period of contractual maturity.

Maturity analysis of assets and liabilities

	At 31 Dec 2017			At 31 Dec 2016		
	Due within 1 year US\$000	Due after 1 year US\$000	Total US\$000	Due within 1 year US\$000	Due after 1 year US\$000	Total US\$000
Financial assets						
Loans and advances to banks	6,047,593	155,609	6,203,202	5,927,118	322,180	6,249,298
Loans and advances to customers	9,956,254	8,360,526	18,316,780	13,008,027	8,002,546	21,010,573
Reverse repurchase agreements – non-trading	1,387,254	–	1,387,254	1,050,843	–	1,050,843
Financial investments	4,444,066	2,302,438	6,746,504	4,732,047	1,850,134	6,582,181
Other financial assets	525,120	2,227	527,347	545,248	465	545,713
	22,360,287	10,820,800	33,181,087	25,263,283	10,175,325	35,438,608
Financial liabilities						
Deposits by banks	1,638,836	159,638	1,798,474	3,020,092	226,562	3,246,654
Customer accounts	22,561,753	21,896	22,583,649	22,577,850	11,077	22,588,927
Financial liabilities designated at fair value	–	739,425	739,425	–	401,592	401,592
Debt securities in issue	594,783	1,497,607	2,092,390	1,253,772	1,391,711	2,645,483
Other financial liabilities	1,205,108	27,153	1,232,261	1,264,775	39,863	1,304,638
	26,000,480	2,445,719	28,446,199	28,116,489	2,070,805	30,187,294

Cash flows payable by the group under financial liabilities by remaining contractual maturities

	On demand	Due within 3 months	Due between 3 and 12 months	Due between 1 and 5 years	Due after 5 years
	US\$000	US\$000	US\$000	US\$000	US\$000
Deposits by banks	1,365,333	128,275	148,739	166,599	–
Customer accounts	19,600,841	1,717,815	1,247,771	22,252	–
Trading liabilities	1,309,860	–	–	–	–
Financial liabilities designated at fair value	–	6,298	30,447	764,184	–
Derivatives	944,753	236	845	6,498	–
Debt securities in issue	225,000	349,935	20,365	774,672	725,000
Other financial liabilities	902,077	406,058	128,081	27,148	–
	24,347,864	2,608,617	1,576,248	1,761,353	725,000
Loan and other credit-related commitments	3,135,419	5,037,874	6,318,227	1,397,841	1,042,070
Financial guarantees and similar contracts	6,816,340	–	–	–	–
At 31 Dec 2017	34,299,623	7,646,491	7,894,475	3,159,194	1,767,070
Deposits by banks	2,684,966	184,632	153,132	232,146	–
Customer accounts	19,934,797	1,788,216	856,833	11,153	–
Trading liabilities	1,496,561	–	–	–	–
Financial liabilities designated at fair value	–	–	10,986	421,973	–
Derivatives	1,253,660	151	149,890	5,339	–
Debt securities in issue	225,000	274,629	781,890	602,785	765,921
Other financial liabilities	896,175	454,268	98,263	39,863	–
	26,491,159	2,701,896	2,050,994	1,313,259	765,921
Loan and other credit-related commitments	2,871,563	6,724,877	5,864,865	1,223,170	341,934
Financial guarantees and similar contracts	7,075,357	–	–	–	–
At 31 Dec 2016	36,438,079	9,426,773	7,915,859	2,536,429	1,107,855

Trading liabilities and trading derivatives have been included in the ‘On demand’ time bucket, and not by contractual maturity, because trading liabilities are typically held for short periods of time. The undiscounted cash flows on hedging derivative liabilities are classified according to their contractual maturity. The undiscounted cash flows potentially payable under financial guarantee contracts are classified on the basis of the earliest date they can be drawn down.

Further discussion of the group’s liquidity and funding management can be found in Note 30 ‘Risk management’.

26 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 to set off only in the event of default, insolvency or bankruptcy, or the offset criteria are otherwise not satisfied; and
- 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 to set off remains appropriate.

	Amounts subject to enforceable netting arrangements				
	Gross amounts US\$000	Amounts offset US\$000	Net amounts in the balance sheet US\$000	Amounts not set off in the balance sheet	
				Cash collateral US\$000	Net amount US\$000
Financial assets					
Derivatives (Note 13)	963,102	–	963,102	–	963,102
Reverse repos, securities borrowing and similar agreements classified as:					
– loans and advances to banks and customers at amortised cost	1,387,254	–	1,387,254	–	1,387,254
Loans and advances to customers excluding reverse repos at amortised cost	581,219	–	581,219	(103,251)	477,968
At 31 Dec 2017	2,931,575	–	2,931,575	(103,251)	2,828,324
Derivatives (Note 13)	1,319,251	–	1,319,251	–	1,319,251
Reverse repos, securities borrowing and similar agreements classified as:					
– loans and advances to banks and customers at amortised cost	1,050,843	–	1,050,843	–	1,050,843
Loans and advances to customers excluding reverse repos at amortised cost	712,130	–	712,130	(156,296)	555,834
At 31 Dec 2016	3,082,224	–	3,082,224	(156,296)	2,925,928
Financial liabilities					
Derivatives (Note 13)	952,332	–	952,332	–	952,332
At 31 Dec 2017	952,332	–	952,332	–	952,332
Derivatives (Note 13)	1,409,040	–	1,409,040	–	1,409,040
At 31 Dec 2016	1,409,040	–	1,409,040	–	1,409,040

27 Foreign exchange exposure

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 subsidiaries, branches and associates with non-US dollar functional currencies. Gains or losses on structural foreign exchange exposures are recognised in other comprehensive income.

The main operating currencies of the group are UAE dirham and other Gulf currencies that are linked to the US dollar.

The group's management of structural foreign currency exposures is discussed in Note 30 'Risk management'.

Net structural foreign currency exposures

Currency of structural exposure

	2017 US\$000	2016 US\$000
Algerian dinar	151,586	171,635
Bahraini dinar	79,160	179,039
Kuwaiti dinar	198,260	182,527
Lebanese pound	345	71,853
Moroccan dirham	117	52
Qatari riyal	374,482	491,046
UAE dirham	2,054,022	2,072,539
Total	2,857,972	3,168,691

Notes on the Financial Statements

28 Called up share capital and share premium

Authorised

The authorised ordinary share capital of the Bank at 31 December 2017 was 1,500,000,000 (2016: 1,500,000,000) ordinary shares¹ of US\$1.00 each.

Called up share capital and share premium

Issued and fully paid

	Footnotes	2017		2016	
		Number	US\$000	Number	US\$000
At 1 Jan		931,055,000	931,055	931,055,000	931,055
Shares issued	2	1	—	—	—
At 31 Dec	1	931,055,001	931,055	931,055,000	931,055

Share premium

	Footnote	2017	2016
		US\$000	US\$000
At 31 Dec	2	61,346	—

Total called up share capital and share premium

	Footnote	2017	2016
		US\$000	US\$000
At 31 Dec	2	992,401	931,055

¹ All ordinary shares in issue confer identical rights, including in respect of capital, dividends and voting.

² On 29 June 2017 (the 'transaction date'), the bank acquired 10.01% stake in HSBC Bank A.S. in Turkey from HSBC Bank plc. The acquisition was settled through the issuance of one ordinary share, which was allotted to its sole shareholder, HSBC Middle East Holdings BV, with a nominal value of US\$1.00, at a premium of US\$61.3 million recognised as share premium account as at the transaction date.

29 Notes on the statement of cash flows

Non-cash items included in profit before tax

	2017	2016
	US\$000	US\$000
Depreciation, amortisation and impairment	19,027	19,055
Share-based payment expense	9,836	11,974
Loan impairment losses gross of recoveries and other credit risk provisions	149,912	150,355
Provisions	42,477	24,469
Impairment of financial investments	2,660	9,782
Charge for defined benefit plans	24,049	25,669
Accretion of discounts and amortisation of premiums	2,695	13,738
	250,656	255,042

Change in operating assets

	2017	2016
	US\$000	US\$000
Change in prepayments, accrued income and other assets	863,639	(532,437)
Change in net trading securities and net derivatives	(545,480)	(31,573)
Change in loans and advances to banks	(1,347,949)	(85,024)
Change in loans and advances to customers	2,526,476	2,547,835
Change in reverse repurchase agreements – non-trading	(336,411)	(243,915)
	1,160,275	1,654,886

Change in operating liabilities

	2017	2016
	US\$000	US\$000
Change in accruals, deferred income and other liabilities	(832,197)	602,730
Change in deposits by banks	(1,448,180)	357,016
Change in customer accounts	(5,278)	(2,663,152)
Change in debt securities in issue	(553,093)	(162,494)
Change in financial liabilities designated at fair value	337,833	(446,645)
Change in provisions	(14,050)	(11,868)
	(2,514,965)	(2,324,413)

Cash and cash equivalents

	2017	2016
	US\$000	US\$000
Cash and balances at central banks	671,440	462,057
Items in the course of collection from other banks	64,419	47,053
Loans and advances to banks of one month or less	3,389,318	4,783,360
Treasury bills, other bills and certificates of deposit less than three months	1,762,411	2,006,751
Less: items in the course of transmission to other banks	(87,502)	(90,415)
Total cash and cash equivalents	5,800,086	7,208,806

Total interest paid by the group during the year was US\$129 million (2016: US\$122 million). Total interest received by the group during the year was US\$1,067 million (2016: US\$1,059 million). Total dividends received by the group during the year were US\$4 million (2016: US\$3 million).

30 Risk management

All the group's activities involve, to varying degrees, the analysis, evaluation, acceptance and active management of risks or combinations of risks. The key financial risks that the group is exposed to are credit risk (including cross-border country risk), market risk (predominantly foreign exchange and interest rate risks) and liquidity risk. The group is also exposed to operational risk in various forms (including technology, projects, process, people, security and fraud risks). The group continues to enhance its capabilities and coverage of financial crime control. Other risks that the group is actively managing include legal risk, reputational risk, pensions risk, strategic risk (direction and execution) and ensuring the group complies with various regulatory requirements or takes necessary actions where it is not yet doing so.

Risk governance and ownership

An established risk governance and ownership structure ensures oversight of, and accountability for, the effective management of risk at the group and global business level. The 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 the enterprise tools of Risk Appetite, Top and Emerging ('T&E') Risks, Risk Map and Stress Testing.

The Board approves the group's risk appetite framework, plans and performance targets for the group and its principal operating subsidiaries, the appointment of senior officers, the delegation of authorities for credit and other risks and the establishment of effective control procedures. The Audit and Risk Committees are responsible for advising the Board on material risk matters and providing non-executive oversight of risks. Under authority delegated by the Board, the separately convened Risk Management Meeting ('RMM') formulates high-level group risk management policy and oversees the implementation of risk appetite and controls. The RMM together with the Asset and Liability Committee ('ALCO') monitors all categories of risk, receives reports on actual performance and emerging issues, determines action to be taken and reviews the efficacy of the group's risk management framework.

In their oversight and stewardship of risk management at group level, RMM are supported by a dedicated Risk function headed by the Chief Risk Officer ('CRO'), who is a Chair of the RMM and reports to the Chief Executive Officer ('CEO') and functionally to the Europe CRO in the HSBC Group.

Risk management tools

The group uses a range of tools to identify, monitor and manage risk. The key tools are summarised below.

Risk appetite

Risk appetite, a key component of the group's risk management framework, is approved by the Board and describes the types and levels of risk that the group is prepared to accept in executing the group's strategy. The group's risk appetite is set out in the group's Risk Appetite Statement and is central to the annual planning process. Global businesses as well as countries are required to articulate their Risk Appetite Statements which are aligned with the group strategy.

Quantitative and qualitative metrics are organised under 15 categories, namely; returns, costs, capital, risk-weighted assets, liquidity and funding, loan impairments, exposure to the HSBC Group, credit and portfolio concentrations, market risk, operational risk, internal audit, financial crime compliance, reputational risk, sustainability risk and technology infrastructure. Measurements against the metrics serve to:

- guide underlying business activity, ensuring it is aligned to risk appetite statements;
- determine risk-adjusted remuneration;
- enable the key underlying assumptions to be monitored and, where necessary, adjusted through subsequent business planning cycles; and
- promptly identify business decisions needed to mitigate risk.

Risk map

The group uses a risk map to provide a point-in-time view of its risk profile across a suite of risk categories. This highlights the potential for these risks to materially affect our financial results, reputation or business sustainability on current and projected bases.

The risks presented on the risk map are regularly assessed against risk appetite, are stress tested and, where longer-term thematic issues arise, are considered for inclusion as top or emerging risks.

Top and emerging risks

The group uses a top and emerging risks process to provide a forward-looking view of issues that have the potential to threaten the execution of the group's strategy or operations over the medium to long term.

The group defines a 'top risk' as a thematic issue that may form and crystallise in between six months and one year, and that has the potential to materially affect the group's financial results, reputation or business model. It may arise across any combination of risk types,

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regions or global businesses. The impact may be well understood by senior management and some mitigating actions may already be in place. Stress tests of varying granularity may also have been carried out to assess the impact.

An 'emerging risk' is a thematic issue with large unknown components that may form and crystallise beyond a one-year time horizon. If it were to materialise, it could have a material effect on the group's long-term strategy, profitability and reputation. Existing mitigation plans are likely to be minimal, reflecting the uncertain nature of these risks at this stage. Some high-level analysis and/or stress testing may have been carried out to assess the potential impact.

Stress testing

Stress testing is a critical component of the HSBC Group's strategic, risk and capital management governance as the regulatory expectations and demands in this area continue to expand significantly. It is an important tool used to evaluate the potential financial impact of plausible scenarios in the event of an economic downturn or a geopolitical duress. The stress testing and scenario analysis programme examines the sensitivities of our capital plans and unplanned demand for regulatory capital under a number of scenarios and ensures that top and emerging risks are appropriately considered. These scenarios include, but are not limited to, adverse macroeconomic events, failures at country, sector and counterparty levels, geopolitical occurrences and a variety of projected major operational risk events. The group entities are included in the annual Group stress test submitted to the Bank of England.

In addition to the HSBC Group-wide risk scenarios, the group conducts regular macroeconomic and event-driven scenario analyses specific to the region. The bank is subject to regulatory stress testing in many jurisdictions within the region. These have increased both in frequency and in the granularity of information required by supervisors. Assessment by regulators is on both quantitative and qualitative bases, the latter focusing on portfolio quality, data provision, stress testing capability, forward-looking capital management processes and internal management processes.

Apart from the aforementioned Enterprise Wide Stress Tests the group also undertakes Reverse Stress Testing, which is conducted to examine a set of potential scenarios that may render the bank's business model non-viable. Non-viability might occur before the bank's capital is depleted, and could result from a variety of events, including idiosyncratic or systemic events or combinations thereof. Reverse stress testing is used to strengthen our resilience by helping to inform early-warning triggers, management actions and contingency plans designed to mitigate the potential stresses and vulnerabilities which we might face.

The results of aforementioned stress tests feed into the regional recovery plan and forms a part of the group's Internal Capital Adequacy Assessment Process ('ICAAP') submission to the regulator.

Risk culture

The group's strong risk governance reflects the importance placed by the Board on managing risks effectively. It is supported by a clear policy framework of risk ownership and by the accountability of all staff for identifying, assessing and managing risks within the scope of their assigned responsibilities. This personal accountability, reinforced by the governance structure, experience and mandatory learning, helps to foster a disciplined and constructive culture of risk management and control throughout the group. Personal accountability is also reinforced by the group's values, with staff expected to be:

- dependable, doing the right thing;
- open to different ideas and culture; and
- connected to our customers, regulators and each other.

Credit risk

Credit risk management

Credit risk is the risk of financial loss if a customer or counterparty fails to meet an obligation under a contract. It arises principally from direct lending, trade finance and leasing business, but also from other products such as guarantees and credit derivatives, and from the group's holdings of debt and other securities. Credit risk generates the largest regulatory capital requirement of the risks the group incurs.

HSBC Holdings plc is responsible for the formulation of high-level credit risk policies and provides high-level centralised oversight and management of credit risk for the HSBC Group worldwide. In addition its responsibilities include:

- Controlling exposures to sovereign entities, banks and other financial institutions, as well as debt securities that are not held solely for the purpose of trading.
- Monitoring intra-HSBC Group exposures to ensure they are maintained within regulatory limits.
- Controlling cross-border exposures, through the imposition of country limits with sub-limits by maturity and type of business. Country limits are determined by taking into account economic and political factors, and applying local business knowledge. Transactions with countries deemed to be higher risk are considered case by case.

Within the group, the Credit Risk function is headed by the CRO who reports to the CEO, with a functional reporting line to the Europe CRO in the HSBC Group. Its responsibilities include:

- Formulating and recording detailed credit policies and procedures, consistent with HSBC Group policy.
- Issuing policy guidelines to subsidiaries and offices on appetite for credit risk exposure to specified market sectors, activities and banking products, and controlling exposures to certain high-risk sectors.
- Undertaking independent review and objective assessment of risk. Credit Risk assesses all commercial non-bank credit facilities and exposures over designated limits, prior to the facilities being committed to customers or transactions being undertaken.
- Monitoring the performance and management of portfolios.
- Maintaining 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.
- Maintaining and developing the governance and operation of HSBC Group's risk rating framework and systems, to classify exposures.
- Reporting on retail portfolio performance, high risk portfolios, risk concentrations, country limits and cross-border exposures, large impaired accounts, impairment allowances and stress testing results and recommendations to the RMM, the Audit and Risk Committee and the Board of Directors.

- Acting on behalf of the group as the primary interface, for credit-related issues, with external parties, including the rating agencies, corporate analysts, trade associations etc.

The group is required to implement credit policies, procedures and lending guidelines that meet local requirements while conforming to the HSBC Group standards.

Credit quality

The group's 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.

The group's risk rating system facilitates the Internal Ratings Based ('IRB') approach for portfolio management purposes. The system adopted by the HSBC Group to support calculation under Basel II of the minimum credit regulatory capital requirement for banks, sovereigns and certain larger corporates.

Special attention is paid to problem exposures in order to accelerate remedial action. Where appropriate, the group uses specialist units to provide customers with support in order to help them avoid default wherever possible.

Periodic risk-based audits of the group's credit processes and portfolios are also undertaken by an independent function.

Impairment Assessment

It is the group's policy that each operating company creates allowances for impaired loans promptly and consistently.

Impairment allowances may be assessed and created either for individually significant accounts or, on a collective basis, for groups of individually significant accounts for which no evidence of impairment has been individually identified or for high-volume groups of homogeneous loans that are not considered individually significant.

When impairment losses occur, the group reduces the carrying amount of loans and advances through the use of an allowance account. When impairment of available-for-sale financial assets and held-to-maturity financial investments occurs, the carrying amount of the asset is reduced directly.

Write-off of loans and advances

Loans are normally written off, either partially or in full, when there is no realistic prospect of further recovery. For secured loans, write-off generally occurs after receipt of any proceeds from the realisation of security.

Unsecured personal facilities, including credit cards, are generally written off at between 150 and 210 days past due, the standard period being the end of the month in which the account becomes 180 days contractually delinquent. Write-off periods may be extended, generally to no more than 360 days past due but in very exceptional circumstances exceeding that figure, in a few countries where local regulation or legislation constrain earlier write-off, or where the realisation of collateral for secured real estate lending extends to this time.

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

Refinance risk

Many types of lending require the repayment of a significant proportion of the principal at maturity. Typically, the mechanism of repayment for the customer is through the acquisition of a new loan to settle the existing debt. Refinance risk arises where a customer is unable to repay such term debt on maturity, or to refinance debt at commercial rates. When there is evidence that this risk may apply to a specific contract, the group may need to refinance the loan on concessionary terms that it would not otherwise have considered, in order to recoup the maximum possible cash flows from the contract and potentially avoid the customer defaulting on the repayment of principal. When there is sufficient evidence that borrowers, based on their current financial capabilities, may fail at maturity to repay or refinance their loans, these loans are disclosed as impaired with recognition of a corresponding impairment allowance where appropriate.

Credit exposure

Maximum exposure to credit risk

The group's exposure to credit risk is spread across a broad range of asset classes, including derivatives, trading assets, loans and advances to customers, loans and advances to banks, and financial investments.

The following table presents the group's maximum exposure to credit risk from balance sheet and off-balance sheet financial instruments before taking account of any collateral held or other credit enhancements (unless such enhancements meet accounting offsetting requirements). For financial assets recognised on the balance sheet, the maximum exposure to credit risk equals their carrying amount; for financial guarantees and similar contracts 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 relate 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.

In the case of derivatives and reverse repos the offset column also includes collateral received in cash and other financial assets.

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Maximum exposure to credit risk

	2017			2016		
	Maximum exposure US\$000	Offset US\$000	Net US\$000	Maximum exposure US\$000	Offset US\$000	Net US\$000
Derivatives	963,102	–	963,102	1,319,251	–	1,319,251
Loans and advances to customers held at amortised cost	18,316,780	(101,437)	18,215,343	21,010,573	(154,720)	20,855,853
– personal	3,874,807	(1,566)	3,873,241	4,105,881	(2,738)	4,103,143
– corporate and commercial	13,647,323	(99,871)	13,547,452	14,540,747	(151,982)	14,388,765
– non-bank financial institutions	794,650	–	794,650	2,363,945	–	2,363,945
Loans and advances to banks held at amortised cost	6,203,202	–	6,203,202	6,249,298	–	6,249,298
Reverse repurchase agreements – non-trading	1,387,254	–	1,387,254	1,050,843	–	1,050,843
Total off-balance sheet	23,747,771	–	23,747,771	24,101,766	–	24,101,766
– financial guarantees and similar contracts	6,816,340	–	6,816,340	7,075,357	–	7,075,357
– loan and other credit-related commitments	16,931,431	–	16,931,431	17,026,409	–	17,026,409

Collateral and other credit enhancements held

Loans and advances held at amortised cost

Although collateral can be an important mitigant of credit risk, it is the group's practice to lend on the basis of the customer's ability to meet their obligations out of 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 without security. However, for other lending a charge over collateral is obtained and considered in determining the credit decision and pricing. In the event of default, the bank may utilise the collateral as a source of repayment. Depending on its form, collateral can have a significant financial effect in mitigating the group's exposure to credit risk.

The tables below provide a quantification of the value of fixed charges the group holds over specific asset (or assets) where the group has a history of enforcing, and are able to enforce, the 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 in the tables below excludes any adjustments for obtaining and selling the collateral.

The group may also manage its risk by employing other types of collateral and credit risk enhancements, such as second charges, other liens and unsupported guarantees, but the valuation of such mitigants is less certain and their financial effect has not been quantified. In particular, loans shown in the tables below as not collateralised or partially collateralised may benefit from such credit mitigants.

Residential mortgage loans including loan commitments by level of collateral

	2017 US\$000	2016 US\$000
Non-impaired loans and advances		
Uncollateralised	–	–
Fully collateralised	1,760,787	1,841,548
LTV ratio:		
– Less than 50%	426,910	480,499
– 51% to 60% LTV	240,589	281,134
– 61% to 70% LTV	369,245	403,208
– 71% to 80% LTV	561,762	514,325
– 81% to 90% LTV	126,154	131,254
– 91% to 100% LTV	36,127	31,128
Partially collateralised		
Greater than 100% LTV (A)	69,796	66,008
– 101% to 110% LTV	14,532	14,826
– 111% to 120% LTV	7,070	10,860
– greater than 120% LTV	48,194	40,322
Collateral value on A	47,134	38,311
Total	1,830,583	1,907,556
Impaired loans and advances		
Fully collateralised	36,161	47,384
LTV ratio:		
– Less than 50%	6,386	16,221
– 51% to 60% LTV	2,360	487
– 61% to 70% LTV	8,763	10,574
– 71% to 80% LTV	5,360	2,735
– 81% to 90% LTV	5,150	8,728
– 91% to 100% LTV	8,142	8,639
Partially collateralised:		
Greater than 100% LTV (B)	55,317	72,466
– 101% to 110% LTV	8,593	9,899
– 111% to 120% LTV	12,218	12,013
– greater than 120% LTV	34,506	50,554
Collateral value on B	47,292	63,196
Total	91,478	119,850
Total residential mortgages	1,922,061	2,027,406

The above table shows residential mortgage lending including off-balance sheet loan commitments by level of collateral. The collateral included in the table above consists of first charges on real estate.

The LTV ratio is calculated as the gross on balance sheet carrying amount of the loan and any off-balance sheet loan commitment at the balance sheet date divided by the value of collateral. The methodologies for obtaining residential property collateral values vary throughout the group, but are typically determined through a combination of professional appraisals, house price indices or statistical analysis. Valuations must be updated on a regular basis and, as a minimum, at intervals of every three years.

Other personal lending

The other personal lending consists primarily of motor vehicle, credit cards and second lien portfolios. Motor vehicle lending is generally collateralised by the motor vehicle financed. Credit cards and overdrafts are generally unsecured. Second lien lending is supported by collateral but the claim on the collateral is subordinate to the first lien charge.

Collateral on loans and advances

Commercial real estate loans and advances

Collateral held is analysed separately below for commercial real estate and for other corporate, commercial and financial (non-bank) lending. The analysis includes off-balance sheet loan commitments, primarily undrawn credit lines.

Commercial real estate loans and advances including loan commitments by level of collateral

	2017 US\$000	2016 US\$000
Rated CRR/EL 1 to 7		
Not collateralised	253,863	328,679
Fully collateralised	51,811	29,897
Total	305,674	358,576
Rated CRR/EL 8 to 10		
Not collateralised	2,508	3,903
Fully collateralised	193,878	193,893
LTV ratio:		
– less than 50%	19,057	19,058
– 51% to 75%	–	–
– 76% to 90%	–	–
– 91% to 100%	174,821	174,835
Partially collateralised (A)	–	–
Collateral value on A	–	–
Total	196,386	197,796
At 31 Dec	502,060	556,372

The collateral included in the table above consists of fixed first charges on real estate and charges over cash for commercial real estate. These facilities are disclosed as not collateralised if they are unsecured or benefit from credit risk mitigation from guarantees, which are not quantified for the purposes of this disclosure.

The value of commercial real estate collateral is determined through a combination of professional and internal valuations and physical inspection. Due to the complexity of valuing collateral for commercial real estate, local valuation policies determine the frequency of review based on local market conditions. Revaluations are sought with greater frequency when, as part of the regular credit assessment of the obligor, material concerns arise in relation to the transaction which may reflect on the underlying performance of the collateral, or in circumstances where an obligor's credit quality has declined sufficiently to cause concern that the principal payment source may not fully meet the obligation (i.e. the obligor's credit quality classification indicates it is at the lower end, that is sub-standard, or approaching impaired). Where such concerns exist the revaluation method selected will depend upon the loan-to-value relationship, the direction in which the local commercial real estate market has moved since the last valuation and, most importantly, the specific characteristics of the underlying commercial real estate which is of concern.

Other corporate, commercial and financial (non-bank) is analysed separately below reflecting the difference in collateral held on the portfolios. For financing activities in corporate and commercial lending that are not predominantly commercial real estate-oriented, 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.

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Other corporate, commercial and non-bank financial institutions loans and advances including loan commitments by level of collateral rated CRR/EL 8 to 10 only

	2017 US\$000	2016 US\$000
Rated CRR/EL 8		
Not collateralised	56,224	10,107
Fully collateralised	168	2,175
LTV ratio:		
– less than 50%	168	1,826
– 51% to 75%	–	–
– 76% to 90%	–	12
– 91% to 100%	–	337
Partially collateralised (A)	31,880	11,372
Collateral value on A	2,433	866
Total	88,272	23,654
Rated CRR/EL 9 to 10		
Not collateralised	663,005	699,543
Fully collateralised	95,409	128,624
LTV ratio:		
– less than 50%	23,027	45,824
– 51% to 75%	863	208
– 76% to 90%	71,109	73,522
– 91% to 100%	410	9,070
Partially collateralised (B)	389,131	416,429
Collateral value on B	56,801	65,552
Total	1,147,545	1,244,596
At 31 Dec	1,235,817	1,268,250

Other credit risk exposures

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

Securities issued by governments, banks and other financial institutions may benefit from additional credit enhancement, notably through government guarantees that reference these assets.

Trading assets include loans and advances held with trading intent, the majority of which consist of reverse repos and stock borrowing which, by their nature, are collateralised.

The group's maximum exposure to credit risk includes financial guarantees and similar arrangements that the group issues or enters into, and loan commitments that the group are irrevocably committed to. Depending on the terms of the arrangement, the group 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 International Swaps and Derivatives Association ('ISDA') Master Agreement is our preferred agreement for documenting derivatives activity. It provides the contractual framework within which dealing activity across a full range of over-the-counter ('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 another pre-agreed termination event occurs. It is common, and our 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 counterparty risk inherent in outstanding positions.

Concentration of exposure

Concentrations of credit risk arise when a number of counterparties or exposures have comparable economic characteristics or such counterparties are engaged in similar activities or operate in the same geographical areas or 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 our portfolios across industry, country and global businesses. These include portfolio and counterparty limits, approval and review controls, and stress testing.

The group provides a diverse range of financial services both in the Middle East and internationally. As a result, its portfolio of financial instruments with credit risk is diversified, with no exposures to individual industries or economic groupings totalling more than 10% of consolidated total assets, except as follows:

- the majority of the group's exposure to credit risk is concentrated in the Middle East. Within the Middle East, the group's credit risk is diversified over a wide range of industrial and economic groupings; and
- the group's position as part of a major international banking group means, that it has a significant concentration of exposure to banking counterparties. The majority of credit risk to the banking industry at 31 December 2017 and 31 December 2016 was concentrated in the Middle East.

Wrong-way risk is an aggravated form of concentration risk and arises when there is a strong correlation between the counterparty's probability of default and the mark-to-market value of the underlying transaction. The group uses 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.

Gross loans and advances to customers by industry sector

	Gross loans and advances to customers	
	Total US\$000	As a % of total gross loans %
At 31 Dec 2017		
Personal		
– residential mortgages	1,922,061	9.91%
– other personal	2,126,199	10.97%
	4,048,260	20.88%
Corporate and commercial		
– commercial, industrial and international trade	8,616,405	44.44%
– commercial real estate	485,073	2.50%
– other property-related	1,583,928	8.17%
– government	1,356,987	7.00%
– other commercial	2,470,570	12.74%
	14,512,963	74.85%
Financial		
– non-bank financial institutions	827,056	4.27%
Total gross loans and advances to customers	19,388,279	100.00%
Impaired loans		
– as a percentage of gross loans and advances to customers	6.88%	
Total impairment allowances		
– as a percentage of gross loans and advances to customers	5.53%	
At 31 Dec 2016		
Personal		
– residential mortgages	2,027,406	9.15%
– other personal	2,303,684	10.40%
	4,331,090	19.55%
Corporate and commercial		
– commercial, industrial and international trade	7,731,352	34.90%
– commercial real estate	538,966	2.43%
– other property-related	1,613,438	7.28%
– government	1,361,029	6.14%
– other commercial	4,206,845	18.99%
	15,451,630	69.74%
Financial		
– non-bank financial institutions	2,372,320	10.71%
Total gross loans and advances to customers	22,155,040	100.00%
Impaired loans		
– as a percentage of gross loans and advances to customers	6.81%	
Total impairment allowances		
– as a percentage of gross loans and advances to customers	5.17%	

Areas of special interest

Although geopolitical risk in the Middle East continued to be high in 2017, the majority of the group's exposures in the region were concentrated in the UAE, where the political landscape remained stable, albeit there have been signs of economic stress resulting from the recent diplomatic and economic sanctions on Qatar and geopolitical tensions in GCC which continue to drive concerns in the region. Elsewhere across the region where the group has presence, economic and political change including social unrest are carefully monitored with risk appetite adjusted accordingly.

With the current level of oil prices, 2018 should offer some relief from the economic stresses that have characterised the GCC over the past three years. As per the economic outlook, the region's pronounced imbalances also set to narrow – moving from budget deficit to surplus over the next 24 months. In addition however, progress with measures such as subsidy reform and VAT constitute important first step towards broadening public finances and reducing reliance upon oil receipts. Awards of infrastructure contracts for Dubai Expo 2020 are expected to pick up. This should lead to increased contracting activity within the region as subcontracts and supply contracts for the main contracts are awarded.

Wholesale lending

Wholesale lending covers the range of credit facilities granted to sovereign borrowers, banks, non-bank financial institutions and corporate entities. The group's wholesale portfolios are well diversified across industry sectors throughout the region, with exposure subject to portfolio controls. Weaker economic activity reflecting lower oil prices has created challenging market conditions across all sectors such as Retail, Automotive Dealership, Commercial Real Estate, and Tourism etc. The Contracting sector continues to experience challenges as paymasters delay payments reflecting slower economic activity. In addition, new projects have slowed with severe competition and reduced margins being seen for any new projects. The current environment has resulted in subdued business confidence given the strategic importance of hydrocarbons in the region and concerns persist around curtailing government spending and unsettling geopolitical developments.

During 2017, the group continued to manage its counterparty exposures in Middle East countries most at risk from the uncertain political environment. A number of measures are taken by conducting portfolio stress testing, updated lending guidelines, monitoring of sector concentration cap, in addition to quarterly portfolio Oil and Gas review. Second order risk continues to be a concern and reviews have been completed on Large Concentration risks, Cross Border exposure, Contracting, Retail and Auto Dealers sectors. Regional Portfolio Oversight Council continues to review both internal and external portfolio trends.

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Commercial real estate

In the light of reduced economic activity in the regional market, Commercial real estate continues to witness a slowdown in performance with reduction in number of transactions, fall in rentals and plateauing of prices. Whilst credit quality across this sector was broadly stable, there is evidence of softening valuations which is in line with overall market sentiment and there remains risk of stress given the cyclical nature of the sector. Accordingly, across the group's portfolios, credit risk is mitigated by long-standing and conservative policies on asset origination which focus on relationships with long-term customers and limited initial leverage. HSBC Group Risk, in conjunction with major subsidiaries, designates real estate as a Specialised Lending/Controlled Sector and, accordingly, implements enhanced exposure approval, monitoring and reporting procedures. For example, the Group monitors risk appetite limits for the sector at regional level to detect and prevent higher risk concentrations. Given the developing legal environment and the region being more prone to volatility, further conservatism is adopted in the Middle East.

Sovereign counterparties

The overall quality of the group's sovereign portfolio remained strong during the period with the large majority of both in-country and cross-border limits extended to countries with strong internal credit risk ratings. Higher oil prices has brought about relief in budget deficits and fiscal measures whilst the upward movement in oil prices should provide a boost to sovereigns' fiscal balances. The group regularly updates its assessment of higher risk countries and adjusts its risk appetite to reflect prevalent market conditions.

Credit quality of financial instruments

Credit Review and Risk Identification teams regularly review exposures and processes in order to provide an independent, rigorous assessment of the credit risk management framework across the HSBC Group, reinforce secondary risk management controls and share best practice. Internal audit, as a tertiary control function, focuses on risks with a global perspective and on the design and effectiveness of primary and secondary controls, carrying out oversight audits via the sampling of global/regional control frameworks, themed audits of key or emerging risks and project audits to assess major change initiatives.

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

There is no direct correlation between the internal and external ratings at granular level, except to the extent each falls within a single quality classification.

Credit quality classification

Quality classification	Debt securities and other bills	Wholesale lending	Retail lending
	External credit rating	Internal credit rating	Internal credit rating ³
Strong	A- and above	CRR ¹ 1 to CRR2	EL ² 1 to EL2
Good	BBB+ to BBB-	CRR3	EL3
Satisfactory	BB+ to B and unrated	CRR4 to CRR5	EL4 to EL5
Sub-standard	B- to C	CRR6 to CRR8	EL6 to EL8
Impaired	Default	CRR9 to CRR10	EL9 to EL10

¹ Customer risk rating.

² Expected loss 'EL'.

³ The group observes the disclosure convention that, in addition to those classified as EL9 to EL10, retail accounts classified EL1 to EL8 that are delinquent by 90 days or more are considered impaired, unless individually they have been assessed as not impaired (see 'Past due but not impaired gross financial instruments').

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.
- 'Impaired' exposures have been assessed as impaired. These also include retail accounts classified as EL1 to EL8 that are delinquent by more than 90 days, unless individually they have been assessed as not impaired; and renegotiated loans that have met the requirements to be disclosed as impaired and have not yet met the criteria to be returned to the unimpaired portfolio.

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 HSBC customers are rated using the 10- or 23-grade scale, depending on the degree of sophistication of the Basel II approach adopted for the exposure.

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. The ratings of Standard and Poor's are cited, with those of other agencies being treated equivalently. Debt securities with short-term issue ratings are reported against the long-term rating of the issuer of those securities. If major rating agencies have different ratings for the same debt securities, a prudent rating selection is made in line with regulatory requirements.

For the purpose of the following disclosure, retail loans that are past due up to 89 days and are not otherwise classified are not disclosed within the expected loss ('EL') grade to which they relate, but are separately classified as past due but not impaired.

Distribution of financial instruments by credit quality

	31 Dec 2017									
	Neither past due not impaired					Past due but not impaired	Impaired	Total gross amount	Impairment allowances	Total
	Strong	Good	Satisfactory	Sub-standard	US\$000					
Cash and balances at central banks	412,471	258,969	–	–	–	–	–	671,440	–	671,440
Items in the course of collection from other banks	–	–	64,419	–	–	–	–	64,419	–	64,419
Trading assets	175,920	52,474	206,757	5,473	–	–	440,624	–	440,624	
Derivatives	786,228	57,088	116,743	3,043	–	–	963,102	–	963,102	
Loans and advances to customers held at amortised cost	8,203,402	4,838,749	3,778,032	582,220	652,199	1,333,677	19,388,279	(1,071,499)	18,316,780	
– personal	3,097,600	659,895	–	–	94,453	196,312	4,048,260	(173,453)	3,874,807	
– corporate and commercial	4,653,931	4,166,531	3,710,618	350,304	542,551	1,089,028	14,512,963	(865,640)	13,647,323	
– non-bank financial institutions	451,871	12,323	67,414	231,916	15,195	48,337	827,056	(32,406)	794,650	
Loans and advances to banks held at amortised cost	4,970,773	1,112,464	119,965	–	–	–	6,203,202	–	6,203,202	
Reverse repurchase agreements – non-trading	927,235	19,242	440,777	–	–	–	1,387,254	–	1,387,254	
Financial investments	1,778,092	–	4,850,179	–	–	–	6,628,271	–	6,628,271	
– treasury and other eligible bills	248,617	–	1,077,695	–	–	–	1,326,312	–	1,326,312	
– debt securities	1,529,475	–	3,772,484	–	–	–	5,301,959	–	5,301,959	
Assets held for sale	–	–	–	–	–	–	–	–	–	
Other assets	19,648	152,263	394,197	4,874	12,110	4,448	587,540	–	587,540	
– endorsements and acceptances	14,380	152,136	273,370	4,874	12,110	4,448	461,318	–	461,318	
– accrued income and other	5,268	127	120,827	–	–	–	126,222	–	126,222	
At 31 Dec 2017	17,273,769	6,491,249	9,971,069	595,610	664,309	1,338,125	36,334,131	(1,071,499)	35,262,632	

	31 Dec 2016									
Cash and balances at central banks	312,761	149,296	–	–	–	–	462,057	–	462,057	
Items in the course of collection from other banks	–	–	47,053	–	–	–	47,053	–	47,053	
Trading assets	93,352	25,012	62,489	1,553	–	–	182,406	–	182,406	
Derivatives	914,292	313,204	88,999	2,756	–	–	1,319,251	–	1,319,251	
Loans and advances to customers held at amortised cost	9,781,824	5,398,238	4,057,746	548,852	859,290	1,509,090	22,155,040	(1,144,467)	21,010,573	
– personal	3,301,608	661,429	–	–	131,176	236,877	4,331,090	(225,209)	4,105,881	
– corporate and commercial	4,510,920	4,736,376	3,969,583	289,778	717,780	1,227,193	15,451,630	(910,883)	14,540,747	
– non-bank financial institutions	1,969,296	433	88,163	259,074	10,334	45,020	2,372,320	(8,375)	2,363,945	
Loans and advances to banks held at amortised cost	5,093,444	474,252	667,317	14,285	–	–	6,249,298	–	6,249,298	
Reverse repurchase agreements – non-trading	564,931	485,912	–	–	–	–	1,050,843	–	1,050,843	
Financial investments	1,650,332	–	4,861,369	–	–	–	6,511,701	–	6,511,701	
– treasury and other eligible bills	–	–	1,274,331	–	–	–	1,274,331	–	1,274,331	
– debt securities	1,650,332	–	3,587,038	–	–	–	5,237,370	–	5,237,370	
Assets held for sale	240,404	69,401	295,159	206,347	14,458	21,810	847,579	(10,615)	836,964	
Other assets	42,951	157,284	319,609	44,134	22,672	16,846	603,496	–	603,496	
– endorsements and acceptances	40,045	157,278	211,278	44,134	21,846	16,846	491,427	–	491,427	
– accrued income and other	2,906	6	108,331	–	826	–	112,069	–	112,069	
At 31 Dec 2016	18,694,291	7,072,599	10,399,741	817,927	896,420	1,547,746	39,428,724	(1,155,082)	38,273,642	

Past due but not impaired gross financial instruments

Past due but not impaired gross financial instruments are those loans where, although customers have failed to make payments in accordance with the contractual terms of their facilities, they have not met the impaired loan criteria. This is typically when a loan is less than 90 days past due and there are no other indicators of impairment.

Further examples of exposures past due but not impaired include individually assessed mortgages that are in arrears more than 90 days, but there are no other indicators of impairment and the value of collateral is sufficient to repay both the principal debt and all potential interest for at least one year or short-term trade facilities past due more than 90 days for technical reasons such as delays in documentation but there is no concern over the creditworthiness of the counterparty. When groups of loans are collectively assessed for impairment, collective impairment allowances are recognised for loans classified as past due but not impaired.

The following table provides an analysis of gross loans and advances to customers held at amortised cost which are past due but not considered impaired. There are no other significant balance sheet items where past due balances are not considered impaired.

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

	Up to 29 days	30-59 days	60-89 days	90-179 days	180 days and over	Total
	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000
Loans and advances to customers held at amortised cost	540,346	52,147	35,541	10,234	13,931	652,199
– personal	51,141	25,815	17,497	–	–	94,453
– corporate and commercial	474,023	26,332	18,036	10,234	13,926	542,551
– non-bank financial institutions	15,182	–	8	–	5	15,195
Assets held for sale	–	–	–	–	–	–
– disposal group	–	–	–	–	–	–
Other assets	3,740	866	1,943	3,261	2,300	12,110
At 31 Dec 2017	544,086	53,013	37,484	13,495	16,231	664,309

Loans and advances to customers held at amortised cost	702,296	65,453	75,859	7,829	7,853	859,290
– personal	74,747	30,868	25,561	–	–	131,176
– corporate and commercial	627,512	30,366	44,220	7,829	7,853	717,780
– non-bank financial institutions	37	4,219	6,078	–	–	10,334
Assets held for sale	8,290	3,341	2,822	3	2	14,458
– disposal group	8,290	3,341	2,822	3	2	14,458
Other assets	17,265	173	1,811	646	2,777	22,672
At 31 Dec 2016	727,851	68,967	80,492	8,478	10,632	896,420

Renegotiated loans and forbearance

Where a loan is modified due to significant concerns about the borrower's ability to meet contractual payments when due, a range of forbearance strategies is employed in order to improve the management of customer relationships, maximise collection opportunities and, if possible, avoid default, foreclosure or repossession.

Identifying renegotiated loans

Loans are identified as renegotiated loans when the group modifies the contractual payment terms due to significant credit distress of the borrower. 'Forbearance' describes concessions made on the contractual terms of a loan in response to an obligor's financial difficulties. The group classifies and report loans on which concessions have been granted under conditions of credit distress as 'renegotiated loans' when their contractual payment terms have been modified because the group has significant concerns about the borrowers' ability to meet contractual payments when due.

When considering modification terms, the borrower's continued ability to repay is assessed and where they are unrelated to payment arrangements, whilst potential indicators of impairment, these loans are not considered as renegotiated loans. Loans that have been identified as renegotiated retain this designation 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 substantially a different financial instrument. Any new loans that arise following derecognition events will continue to be disclosed as renegotiated loans.

Credit Quality of Renegotiated Loans

Under IFRSs, an entity is required to assess whether there is objective evidence that financial assets are impaired at the end of each reporting period. A loan is impaired and an impairment allowance is recognised when there is objective evidence of a loss event that has an effect on the cash flows of the loan which can be reliably estimated.

When the group grants a concession to a customer that the group would not otherwise consider, as a result of their financial difficulty, this is objective evidence of impairment and impairment losses are measured accordingly.

A renegotiated loan is presented as impaired when:

- there has been a change in contractual cash flows as a result of a concession which the lender would otherwise not consider, and;
- it is probable that without the concession, the borrower would be unable to meet contractual payment obligations in full.

This presentation applies unless the concession is insignificant and there are no other indicators of impairment.

The renegotiated loan will continue to be disclosed as impaired until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, and there are no other indicators of impairment.

Renegotiated loans are classified as unimpaired where the renegotiation has resulted from significant concern about a borrower's ability to meet their contractual payment terms but the renegotiated terms are based on current market rates and contractual cash flows are expected to be collected in full following the renegotiation. Unimpaired renegotiated loans also include previously impaired renegotiated loans that have demonstrated satisfactory performance over a period of time or have been assessed based on all available evidence as having no remaining indicators of impairment.

Loans that have been identified as renegotiated retain this designation until maturity or derecognition. When a loan is restructured as part of a forbearance strategy and the restructuring results in derecognition of the existing loan, such as in some debt consolidations, the new loan is disclosed as renegotiated.

When determining whether a loan that is restructured should be derecognised and a new loan recognised, the group considers the extent to which the changes to the original contractual terms result in the renegotiated loan, considered as a whole, being a substantially different financial instrument.

Renegotiated loans and advances to customers by industry sector

	First lien residential mortgages	Other personal lending	Corporate and commercial	Non-bank financial institutions	Renegotiated loans
	US\$000	US\$000	US\$000	US\$000	US\$000
Neither past due nor impaired	23,707	12,986	74,854	248,276	359,823
Past due but not impaired	4,166	638	16,097	—	20,901
Impaired	85,243	14,801	615,884	45,007	760,935
Renegotiated loans At 31 Dec 2017	113,116	28,425	706,835	293,283	1,141,659
Impairment allowances on renegotiated loans					487,889
Neither past due nor impaired	10,439	3,706	368	259,074	273,587
Past due but not impaired	118	1,351	208,634	—	210,103
Impaired	27,756	14,181	754,482	44,841	841,260
Renegotiated loans At 31 Dec 2016	38,313	19,238	963,484	303,915	1,324,950
Impairment allowances on renegotiated loans					443,398

For retail lending, renegotiated loans are segregated from other parts of the loan portfolio for collective impairment assessment to reflect the higher rates of losses often encountered in these segments. When empirical evidence indicates an increased propensity to default and higher losses on such accounts, the use of roll-rate methodology ensures these factors are taken into account when calculating impairment allowances by applying roll rates specifically calculated on the pool of loans subject to forbearance. When the portfolio size is small or when information is insufficient or not reliable enough to adopt a roll-rate methodology, a basic formulaic approach based on historical loss rate experience is used. As a result of our roll-rate methodology, the group recognises collective impairment allowances on homogeneous groups of loans, including renegotiated loans, where there is historical evidence that there is a likelihood that loans in these groups will progress through the various stages of delinquency, and ultimately prove irrecoverable as a result of events occurring before the balance sheet date. This treatment applies irrespective of whether or not those loans are presented as impaired in accordance with our impaired loans disclosure convention. When the group considers that there are additional risk factors inherent in the portfolios that may not be fully reflected in the statistical roll rates or historical experience, these risk factors are taken into account by adjusting the impairment allowances derived solely from statistical or historical experience.

In the corporate and commercial sectors, renegotiated loans are typically assessed individually. Credit risk ratings are intrinsic to the impairment assessment. A distressed restructuring is classified as an impaired loan. The individual impairment assessment takes into account the higher risk of the non-payment of future cash flows inherent in renegotiated loans.

Impaired loans

Impaired loans and advances are those that meet any of the following criteria:

- Wholesale loans and advances classified as Customer Risk Rating ('CRR') 9 or CRR 10. These grades are assigned when the bank considers that either the customer is unlikely to pay their credit obligations in full without recourse to security, or when the customer is more than 90 days past due on any material credit obligation to the group.
- Retail loans and advances classified as Expected Loss ('EL') 9 or EL 10. These grades are typically assigned to retail loans and advances more than 90 days past due unless individually they have been assessed as not impaired.
- Renegotiated loans and advances that have been subject to a change in contractual cash flows as a result of a concession which the lender would not otherwise consider, and where it is probable that without the concession the borrower would be unable to meet its contractual payment obligations in full, unless the concession is insignificant and there are no other indicators of impairment. Renegotiated loans remain classified as impaired until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, and there are no other indicators of impairment.

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

	2017				2016			
	Customers			Total	Customers			Total
	Banks individually assessed	Individually assessed	Collectively assessed		Banks individually assessed	Individually assessed	Collectively assessed	
US\$000	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000	
At 1 Jan	—	946,230	198,237	1,144,467	17,994	950,079	271,098	1,239,171
Amounts written off	—	(131,548)	(108,734)	(240,282)	(17,994)	(105,071)	(123,327)	(246,392)
Recoveries of loans and advances previously written off	—	334	21,022	21,356	—	7,731	21,629	29,360
Charge to income statement	—	87,243	53,985	141,228	—	104,407	20,223	124,630
Exchange and other movements	—	5,401	(671)	4,730	—	(10,916)	8,614	(2,302)
At 31 Dec	—	907,660	163,839	1,071,499	—	946,230	198,237	1,144,467

Liquidity and funding risk management framework

The group has an internal liquidity and funding risk management framework ('LFRF') which aims to allow it to withstand very severe liquidity stresses. It is designed to be adaptable to changing business models, markets and regulations. Liquidity risk is the risk that the group does not have sufficient financial resources to meet its obligations as they fall due, or will have to do so at an excessive cost. The 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.

Structure and organisation of the liquidity risk management function

The management of liquidity and funding is primarily undertaken locally (by country) in the operating entities in compliance with the Group's LFRF, and with practices and limits set by the Group Management Board ('GMB') through the Risk Management Meeting ('RMM') and approved by the Holdings Board for 'RMM operating entities': the UAE branch of the bank is one such operating entity.

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Limits for non-RMM operating entities within the group are established by the intermediate parent company Asset Liability Committee ('ALCO'). The group ALCO is responsible for setting limits for the group non-RMM operating entities. The group's general policy is that each defined operating entity should be self-sufficient in funding its own activities.

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 primary responsibility for managing liquidity and funding within the Group's framework and risk appetite resides with the local operating entities' ALCOs, Holdings ALCO and the RMM. The UAE branch of the bank, being an RMM operating entity, is overseen by HBME ALCO, HSBC Holdings ALCO and the HSBC Group Risk Management Meeting. The remaining smaller operating entities are overseen by HBME ALCO, with appropriate escalation of significant issues to HSBC Holdings ALCO and the HSBC Group Risk Management Meeting. Operating entities are predominately defined on a country basis to reflect the Group's local management of liquidity and funding.

Overall liquidity risk profile

There were no material changes to the policies and practices for the management of liquidity and funding risk in 2017.

The LFRF is delivered using the following key aspects:

- stand-alone management of liquidity and funding by operating entity;
- operating entity classification by inherent liquidity risk ('ILR') categorisation;
- minimum LCR requirement;
- minimum NSFR requirement;
- legal entity depositor concentration limit;
- three-month and 12-month cumulative rolling term contractual maturity limits covering deposits from banks, deposits from non-bank financial institutions and securities issued;
- annual individual liquidity adequacy assessment by principal operating entities;
- minimum LCR requirement by currency;
- intra-day liquidity;
- liquidity funds transfer pricing; and
- forward-looking funding assessments.

Liquidity and funding risk

Liquidity coverage ratio ('LCR')

The 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. For the calculation of the LCR, the group follows the guidelines set by the European Commission.

Net stable funding ratio ('NSFR')

HSBC uses the NSFR as a basis for establishing stable funding, including the group. The NSFR requires institutions to maintain sufficient stable funding and reflects a bank's long-term funding profile (funding with a term of more than one year).

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 challenged if the portfolio of depositors is not large enough to avoid depositor concentration. 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.

At 31 December 2017, the bank was within the risk tolerance levels set for depositor concentration and term funding maturity concentration.

Liquid assets

Liquid assets are held and managed on a stand-alone operating entity basis. Most are held directly by each operating entity's Balance Sheet Management ('BSM') department, primarily for the purpose of managing liquidity risk in line with the LFRF.

Liquid assets also include any unencumbered liquid assets held outside BSM departments for any other purpose. The LFRF gives ultimate control of all unencumbered assets and sources of liquidity to BSM.

Management of liquidity risk

Liquidity coverage ratio ('LCR')

The LCR metric is designed to promote the short-term resilience of a bank's liquidity profile, and became a minimum regulatory standard from 1 October 2015, under European Commission ('EC') Delegated Regulation 2015/61.

Delegated Act ('DA') LCR

Unaudited	2017 %	2016 %
HSBC Bank Middle East Limited	234.6	260.8

The bank additionally computes and reports a DFSA-basis LCR, which differs from the Delegated Act ('DA') LCR primarily with respect to the haircuts applied to liquid securities under DA issued by Gulf Cooperation Council ('GCC') sovereign issuers and outflow percentages applied for off-balance sheet items and retail deposits.

DFSA LCR

Unaudited	2017	2016
	%	%
HSBC Bank Middle East Limited	239.0	221.9

Net stable funding ratio ('NSFR')

The European calibration of NSFR is pending following the Basel Committee's final recommendation in October 2014. The bank calculates NSFR in line with Basel Committee on Banking Supervision's publication number 295 (BCBS295). This calculation requires various interpretations of the text, and therefore the bank's NSFR may not be directly comparable with the ratios of other institutions.

The DFSA has recently issued the final text on their implementation of NSFR, which is effective from 1 January 2018.

NSFR-295

Unaudited	2017	2016
	%	%
HSBC Bank Middle East Limited	146.6	142.2

Primary sources of funding

Customer deposits in the form of current accounts and savings deposits payable on demand or at short notice form a significant part of our funding, and the group places considerable importance on maintaining their stability. For deposits, stability depends upon maintaining depositor confidence in our capital strength and liquidity, and on competitive and transparent pricing.

Of total liabilities of US\$31,365 million at 31 December 2017, funding from customers amounted to US\$22,583 million, of which US\$22,561 million was contractually repayable within one year.

An analysis of cash flows payable by the group under financial liabilities by remaining contractual maturities at the balance sheet date is included in Note 25.

Assets available to meet these liabilities, and to cover outstanding commitments to lend (US\$16,931 million), included cash, central bank balances, items in the course of collection and treasury and other bills (US\$2,062 million); loans to banks (US\$6,203 million, including US\$6,047 million repayable within one year); and loans to customers (US\$18,316 million, including US\$9,956 million repayable within one year). In the normal course of business, a proportion of customer loans contractually repayable within one year will be extended.

The group also access wholesale funding markets by issuing senior secured and unsecured debt securities (publicly and privately) and borrowing from the secured repo markets against high-quality collateral to align asset and liability maturities and currencies and to maintain a presence in local wholesale markets.

Ordinary share capital and retained reserves, non-core capital instruments and intergroup borrowings are also a source of stable funding.

Market risk

Market risk management

Market risk is 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.

The group's exposure to market risk is separated into trading or non-trading portfolios. Trading portfolios comprise positions arising from market-making and warehousing of customer-derived positions. Non-trading portfolios include positions that primarily arise from the interest rate management of the group's retail and commercial banking assets and liabilities and financial investments designated as available-for-sale.

Market risk measures

Monitoring and limiting market risk exposures

The group's objective is to manage and control market risk exposures while maintaining a market profile consistent with the group's risk appetite. The group uses a range of tools to monitor and limit market risk exposures, including:

- sensitivity measures include sensitivity of net interest income and sensitivity for structural foreign exchange, which are used to monitor the market risk positions within each risk type;
- value at risk ('VaR') is a technique that estimates the potential losses that could occur 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; and
- in recognition of VaR's limitations the group augments VaR with stress testing to evaluate the potential impact on portfolio values of more extreme, though plausible, events or movements in a set of financial variables.

Market risk is managed and controlled through limits approved by the Risk Management Meeting of the GMB for HSBC Holdings and our various global businesses. These limits are allocated across business lines and to the HSBC Group's legal entities.

The management of market risk is principally undertaken in Global Markets. VaR limits are set for portfolios, products and risk types, with market liquidity being a primary factor in determining the level of limits set.

VaR limits are set for portfolios, products and risk types, with market liquidity being a primary factor in determining the level of limits set. HSBC Group Risk, an independent unit within HSBC Group, is responsible for our market risk management policies and measurement techniques. The group has an independent market risk management and control function that is responsible for measuring market risk exposures in accordance with the policies defined by HSBC Group Risk, and monitoring and reporting these exposures against the prescribed limits on a daily basis.

The group assesses the market risks arising on each product in its business and to transfer them to either its Global Markets unit for management, or to separate books managed under the supervision of the local ALCO. Our aim is to ensure that all market risks are

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consolidated within operations that 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.

Sensitivity analysis

Sensitivity analysis measures the impact of individual market factor movements on specific instruments or portfolios, including interest rates, foreign exchange rates 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

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 VaR models used by the group are predominantly based 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 assess potential market movements with reference to data from the past two years and calculate VaR to a 99% confidence level and for a one-day holding period.

The group routinely validates the accuracy of its VaR models by back-testing the actual daily profit and loss results, adjusted to remove non-modelled items such as fees and commissions, against the corresponding VaR numbers. Statistically, the group would expect to see losses in excess of VaR only 1% of the time over a one-year period. The actual number of excesses over this period can therefore be used to gauge how well the models are performing.

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

- 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 one-day holding period assumes that all positions can be liquidated or the risks offset in one day. This may not fully reflect the market risk arising at times of severe illiquidity, when a one-day 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;
- VaR is calculated on the basis of exposures outstanding at the close of business and therefore does not necessarily reflect intra-day exposures; and
- VaR is unlikely to reflect loss potential on exposures that only arise under conditions of significant market movement.

Trading and non-trading portfolio

The following table provides an overview of the reporting of the risks within this section:

Risk type	Footnote	Portfolio	
		Trading	Non-trading
Foreign exchange and commodity	1	VaR	VaR
Interest rate		VaR	VaR
Credit spread		VaR	VaR

1 The reporting of commodity risk is consolidated with foreign exchange risk and is not applicable to non-trading portfolios.

Value at risk of the trading and non-trading portfolio

The group VaR, both trading and non-trading, is below:

Value at risk

	2017 US\$000	2016 US\$000
At 31 Dec	10,909	4,201
Average	5,875	3,792
Minimum	3,104	1,376
Maximum	10,979	6,212

Trading portfolios

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

Market-making and position-taking is undertaken within Global Markets. The VaR for such trading intent activity at 31 December 2017 was US\$11 million (2016: US\$1.4 million).

VaR by risk type for the trading intent activities

		Foreign exchange (FX)	Interest rate	Credit spread	Total
	Footnote	US\$000	US\$000	US\$000	US\$000
At 31 Dec 2017	1, 2	11,738	2,852	372	11,011
Average		3,833	2,809	414	4,654
Maximum		11,944	4,248	1,047	11,301
Minimum		201	1,387	122	1,472
At 31 Dec 2016		220	1,440	125	1,373
Average		228	1,523	248	1,558
Maximum		2,690	2,972	513	3,025
Minimum		83	236	76	326

1 The total VaR is non-additive across risk types due to diversification effects.

2 The increase in VaR in 2017 was driven by the volatility in certain currencies, mainly Qatari Riyal (QAR) and Egyptian Pound (EGP). This was a result of the current regional situation and the devaluation of the EGP, respectively.

Gap risk

Certain products are structured in such a way that they give rise to enhanced gap risk, being the risk that loss is incurred upon occurrence of a gap event. A gap event is a significant and sudden change in market price with no accompanying trading opportunity. Such movements may occur, for example, when, in reaction to an adverse event or unexpected news announcement, some parts of the market move far beyond their normal volatility range and become temporarily illiquid.

Given the characteristics, these transactions, they will make little or no contribution to VaR or to traditional market risk sensitivity measures. The group captures the risks for such transactions within the stress testing scenarios and monitor gap risk on an ongoing basis.

The group incurred no material losses arising from gap risk movements in the underlying market price on such transactions in the 12 months ended 31 December 2017.

De-peg risk

For certain currencies (pegged or managed) the spot exchange rate is pegged at a fixed rate (typically to USD), or managed within a predefined band around a pegged rate. De-peg risk is the risk of the peg or managed band changing or being abolished, and moving to a floating regime.

Using stressed scenarios on spot rates, the group is able to analyse how de-peg events would impact the positions held by the group. This complements traditional market risk metrics, such as historical VaR, which may not fully capture the risk involved in holding positions in pegged currencies. Historical VaR relies on past events to determine the likelihood of potential profits or losses. However, pegged or managed currencies may not have experienced a de-peg event during the historical timeframe being considered.

Non-trading portfolios

The principal objective of market risk management of non-trading portfolios is to optimise net interest income.

Interest rate risk in non-trading portfolios arises principally from mismatches between the future yield on assets and their funding cost as a result of interest rate changes. Analysis of this risk is complicated by having to make assumptions on embedded optionality within certain product areas, such as the incidence of mortgage prepayments, and from behavioural assumptions regarding the economic duration of liabilities which are contractually repayable on demand such as current accounts, and the re-pricing behaviour of managed rate products.

The control of market risk in the non-trading portfolios is based on transferring the risks to the books managed by Global Markets and Balance Sheet Management ('BSM') or the local ALCO. The net exposure is typically managed through the use of interest rate swaps within agreed limits. The VaR for these portfolios is included within the group VaR.

Market risk arises on equity securities held as available-for-sale. The fair value of these securities at 31 December 2017 was US\$118 million (2016: US\$70 million).

Structural foreign exchange exposures

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

Exchange differences on structural exposures are recorded in 'Other comprehensive income'. The main operating currencies of the group are UAE dirham and other Gulf currencies that are linked to the US dollar.

The group's policy is to hedge structural foreign currency exposures only in limited circumstances. The group's structural foreign exchange exposures are managed with the primary objective of ensuring, where practical, that the group's capital ratio is protected from the effect of changes in exchange rates. This is usually achieved by ensuring that the rates of structural exposures in a given currency to risk-weighted assets denominated in that currency is broadly equal to the capital ratio. The group considers hedging structural foreign currency exposures only in limited circumstances to protect the capital ratio or the US dollar value of capital invested. Such hedging would be undertaken using forward foreign exchange controls or by financing the borrowings in the same currencies as the functional currencies involved.

Net interest income sensitivity

A principal part of the group's management of market risk in non-trading portfolios is monitoring the sensitivity of projected net interest income under varying interest rate scenarios (simulation modelling). The group aims, through our management of market risk in non-trading portfolios, to mitigate the impact of prospective interest rate movements which could reduce future net interest income, while balancing the cost of hedging such activities on the current net revenue stream.

For simulation modelling, businesses use a combination of scenarios relevant to their local businesses and markets and standard scenarios which are required throughout the HSBC Group. The latter are consolidated to illustrate the combined pro forma effect on the group's consolidated portfolio valuations and net interest income.

Projected net interest income sensitivity figures represent the effect of the pro forma movements in net interest income based on the projected yield curve scenarios and the group's current interest rate risk profile. This effect, however, does not incorporate actions which would probably be taken by Global Markets or in the business units to mitigate the effect of interest rate risk. In reality, Global Markets seeks proactively to change the interest rate risk profile to minimise losses and optimise net revenues. The projections also assume that interest rates of all maturities move by the same amount (although rates are not assumed to become negative in the falling rates scenario) and, therefore, do not reflect the potential impact on net interest income of some rates changing while others remain unchanged. In addition, the projections take account of the effect on net interest income of anticipated differences in changes between interbank interest rates and interest rates linked to other bases (such as Central Bank rates or product rates over which the entity has discretion in terms of the timing and extent of rate changes). The projections make other simplifying assumptions, including that all positions run to maturity.

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.

Operational risk

Operational risk is the risk to achieving the 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 all the group's employees. They are required to manage the operational risks of the business for which they are responsible.

The objective of the group's operational risk management is to manage and control operational risk in a cost-effective manner within targeted levels of operational risk consistent with the group's risk appetite, as defined by the Group Management Board.

Operational risk management framework

The group's Operational Risk Management Framework ('ORMF') defines minimum standards and processes, and the governance structure for the management of operational risk and internal control in our geographical regions, global businesses and global functions. 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.

Business managers throughout the 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 centralised database is used to record the results of the operational risk management process. Operational risk and control self-assessments are inputted and maintained by business units. Business and functional management and business risk and control managers 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 US\$10,000, and to aggregate all other operational risk losses under US\$10,000. Losses are entered into the group operational risk database and reported to the group Risk Management Meeting on a monthly basis.

Key developments in 2017

During 2017 the group implemented a new ORMF and system of record. The new ORMF provides an end-to-end view of non-financial risks, enhancing focus on the risks that matter the most and associated controls. It provides a platform to drive forward looking risk awareness and assist management focus. It also helps the organisation understand the level of risk it is willing to accept. We also maintained activity to continually strengthen our risk culture. In particular, we focused on the use of the three lines of defence model. It sets our roles and responsibilities for managing operational risk on a daily basis.

Three Lines of Defence

The group uses an activity-based three lines of defence model to delineate management accountabilities and responsibilities for risk management and the control environment. This creates a robust control environment to manage risks. The model underpins the approach to risk management by clarifying responsibility, encouraging collaboration, and enabling efficient coordination of risk and control activities.

The three lines of defence 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.

Legal risk

The group implements processes and procedures in place to manage legal risk that conform to HSBC Group standards.

Legal risk falls within the definition of operational risk and includes the risk of a member of the group suffering financial loss, legal or regulatory action or reputational damage due to:

- contractual risk, which is the risk that any group member enters into inadequate or unenforceable customer contracts or ancillary documentation, inadequate or unenforceable non-customer contracts or ancillary documentation and/or contractual fiduciary;
- dispute adjudication risk, which is the risk arising due to an adverse dispute environment or a failure to take appropriate steps to defend, prosecute and/or resolve actual or threatened legal claims brought against or by a group member, including for the avoidance of doubt, regulatory matters;
- legislative risk, which is the risk that a group member fails to or is unable to identify, analyse, track, assess or correctly interpret applicable legislation, case law or regulation, or new regulatory, legislative or doctrinal interpretations of existing laws or regulations, or decisions in the Courts or regulatory bodies;
- non-contractual rights risk, which is the risk that a group member's assets are not properly owned or protected or are infringed by others, or a group member infringes another party's rights; and
- non-contractual obligations risk, which is the risk arising due to infringement of third-party rights and/or breach of common law duties.

The group has a legal function to assist management in controlling legal risk. The function provides legal advice to manage and control legislative, contractual and non-contractual risks and support in managing litigation claims and significant regulatory enforcement against group companies, as well as in respect of non-routine debt recoveries or other litigation against third parties.

The group members must notify the legal department immediately if any litigation, dispute or material regulatory action is either threatened or commenced against the group or an employee (acting in his capacity as an officer or employee of the group). The legal department must be immediately advised of any significant action by a regulatory authority, where the proceedings are criminal, or where the claim might materially affect HSBC Group's reputation.

The legal department will assess each claim that is threatened or commenced against the group or any employee (acting in his capacity as an officer or employee of the group) in order to determine the appropriate action, including appointment of external counsel, consideration of the merits of the claim, consideration of any provision, consideration of any document holds or interviews that may be required and consideration of any immediate reporting to senior management or the bank's regulators as may be necessary.

The legal department must immediately advise the bank's senior management, the HSBC Group of any threatened or actual litigation claims if such claim exceeds US\$5 million or of any significant action by a regulatory authority, where the proceedings are criminal or where a claim might materially affect HSBC Group's reputation. In addition, the legal department submits periodic returns to the bank's risk management meeting and Board Risk Committee meeting, including updates on ongoing litigation and details of any judgements issued against the group. These returns are shared with the bank's regulators on a periodic basis.

Finally, the group is required to submit a quarterly return to HSBC Group detailing outstanding claims where the claim (or group of similar claims) exceeds US\$10 million, where the action is by a regulatory authority, where the proceedings are criminal, where the claim might materially affect the group's reputation, or, where the HSBC Group has requested returns be completed for a particular claim. These returns are used for reporting to the HSBC Group Audit Committee and the Board of HSBC Holdings plc.

Capital management

The Dubai Financial Services Authority ('DFSA') is the lead regulator of the bank.

The bank's objective is to ensure that capital resources are at all times adequate and efficiently used. This implies assessing the bank's capital demand and maintaining the capital supply at the required level. The bank's approach to capital management is driven by strategic and organisational requirements, taking into account the regulatory, economic and commercial environment in which it operates in. The bank's policy on capital management is underpinned by a capital management process and the internal capital adequacy assessment process, which enables it to manage its capital in a consistent manner.

The DFSA supervises the bank and, receives information on the capital adequacy of, and sets capital requirements for, the bank. Individual branches and subsidiaries are directly regulated by their local banking supervisors, where applicable, who set and monitor their capital adequacy requirements.

The DFSA's capital requirements are prescribed in the DFSA Prudential – Investment, Insurance Intermediation and Banking Module ('PIB'). In accordance with the PIB:

1. the capital requirement for an authorised firm is calculated, subject to (2), as the higher of:
 - a. the applicable Base Capital Requirement as set out in the PIB or
 - b. its Risk Capital Requirement as set out in the PIB.
2. where 1(b) is the higher and the authorised firm has an Individual Capital Requirement ('ICR') imposed on it then the Capital Requirement is its ICR plus Risk Capital Requirement.

An authorised firm must calculate its Risk Capital Requirement as the sum of the following:

- the Credit Risk Capital Requirement;
- the Market Risk Capital Requirement;
- the Operational Risk Capital Requirement; and
- the Displaced Commercial Risk Capital Requirement, where applicable.

Further, the bank is subject to a Capital Conservation Buffer of 25% of Risk Capital Requirements.

The PIB requires an authorised firm to:

- appropriately apply a risk-weight to all on-balance sheet assets and off-balance sheet exposures for capital adequacy purposes. A risk-weight is based on a Credit Quality Grade aligned with the likelihood of counterparty default;

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- calculate the Credit Risk Capital Requirement for its on-balance sheet assets and off-balance sheet exposures; and
- reduce the Credit Risk Capital Requirement for its on-balance sheet assets and off-balance sheet exposures where the exposure is covered fully or partly by some form of eligible Credit Risk mitigant.

The DFSA has granted approval to the bank to use HSBC Group internal models for the purposes of calculating Market Risk Requirements.

The bank uses the Standardised Approach for the calculation of Operational Risk Capital Requirement.

The bank's regulatory capital is divided into two tiers:

- Tier 1 capital comprises equity share capital, share premium, retained earnings, other comprehensive income and other reserves. This is adjusted for the amount of cash flow hedge reserve related to gains or losses on cash flow hedges of financial instruments, all unrealised gains or losses on liabilities which result from changes in the bank's own credit quality and deduction for intangible assets.
- Tier 2 capital comprises qualifying non-equity preference share capital, share premium and collective impairment allowances with certain limitations.

The bank maintains its capital requirements at all times in accordance with the DFSA requirements.

Capital structure at 31 December (solo basis)

Unaudited	2017 US\$000	2016 US\$000
Composition of regulatory capital		
Common Equity Tier 1 capital	4,317,311	4,169,394
Additional Tier 1 capital	–	–
Total Tier 1 capital	4,317,311	4,169,394
Tier 2 capital	1,098,121	1,117,270
Total regulatory capital	5,415,432	5,286,664
Risk-weighted assets		
Credit and counterparty risk	25,477,895	27,682,596
Market risk	2,074,120	656,910
Operational risk	3,190,290	3,341,285
	30,742,305	31,680,791
Capital ratio		
Capital adequacy ratio	17.62%	16.69%

31 Contingent liabilities, contractual commitments and guarantees

	2017 US\$000	2016 US\$000
Guarantees and other contingent liabilities		
Guarantees	14,361,374	14,815,185
Commitments		
Documentary credits and short-term trade-related transactions	620,512	326,826
Undrawn formal standby facilities, credit lines and other commitments to lend	16,310,919	16,699,583
At 31 Dec	16,931,431	17,026,409

The above table discloses the nominal principal amounts which represents the maximum amounts at risk should 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 these nominal principal amounts is not representative of future liquidity requirements.

Included in the above are the following contingent liabilities on account of other members of the HSBC Group:

	2017 US\$000	2016 US\$000
Guarantees and assets pledged by the bank as collateral security	2,626,646	2,400,860
Documentary credits and short-term trade-related transactions	75,909	57,866
At 31 Dec	2,702,555	2,458,726

Guarantees

The group provides guarantees and similar undertakings on behalf of both third-party customers and other entities within the group. These guarantees are generally provided in the normal course of the group's banking business. The principal types of guarantees provided, and the maximum potential amount of future payments which the group could be required to make at 31 December were as follows:

	Footnotes	2017		2016	
		Guarantees in favour of third parties US\$000	Guarantees by the group in favour of other HSBC Group entities US\$000	Guarantees in favour of third parties US\$000	Guarantees by the group in favour of other HSBC Group entities US\$000
Financial guarantees	1	1,808,159	665,281	1,943,339	504,734
Credit-related guarantees	2	3,739,796	603,104	4,102,406	524,878
Other guarantees		6,186,773	1,358,261	6,368,580	1,371,248
At 31 Dec		11,734,728	2,626,646	12,414,325	2,400,860

1 Financial guarantees 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.

2 Credit-related guarantees are contracts that have similar features to financial guarantee contracts but fail to meet the strict definition of a financial guarantee contracts under IAS 39.

The amounts disclosed in the above table are nominal principal amounts and reflect the group's maximum exposure under a large number of individual guarantee undertakings. The risks and exposures arising from guarantees are captured and managed in accordance with the group's overall credit risk management policies and procedures. Guarantees with terms of more than one year are subject to the group's annual credit review process.

Other commitments

In addition to the commitments disclosed above, at 31 December 2017 the group had capital commitments to purchase, within one year, land and building and other fixed assets for a value of US\$222 million (2016: US\$222 million).

Associates

The group and its operations are contingently liable with respect to lawsuits and other matters that arise in the normal course of business. Management is of the opinion that the eventual outcome of the legal and financial liability is not expected to materially affect the group's financial position and operations.

32 Lease commitments

Operating lease commitments

At 31 December 2017, the group was obligated under a number of non-cancellable operating leases for properties, plant and equipment for which the future minimum lease payments extend over a number of years.

	Land and buildings	
	2017 US\$000	2016 US\$000
Future minimum lease payments under non-cancellable operating leases expiring:		
– no later than one year	18,600	34,455
– later than one year and no later than five years	20,610	50,589
– later than five years	1,707	3,951
At 31 Dec	40,917	88,995

In 2017, US\$25.0 million (2016: US\$31.2 million) was charged to 'General and administrative expenses' in respect of lease agreements related to minimum lease payments.

Finance lease receivables

The group leases a variety of assets to third parties under finance leases. 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.

	2017			2016		
	Total future minimum payments US\$000	Unearned finance income US\$000	Present value US\$000	Total future minimum payments US\$000	Unearned finance income US\$000	Present value US\$000
Lease receivables:						
– no later than one year	135,247	(1,975)	133,272	272,766	(1,533)	271,233
– later than one year and no later than	15,869	(6,284)	9,585	17,759	(5,808)	11,951
– later than five years	69,748	(2,732)	67,016	61,291	(1,418)	59,873
At 31 Dec	220,864	(10,991)	209,873	351,816	(8,759)	343,057

33 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. 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 2017. Where an individual provision is material, the fact that a provision has been made is stated and quantified, except to the extent 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.

Anti-money laundering and sanctions-related

(Matters relevant to the group as a subsidiary of HSBC operating in the Middle East)

In October 2010, HSBC Bank USA entered into a consent order with the Office of the Comptroller of the Currency (the 'OCC'), and HSBC North America Holdings Inc. ('HNAH') entered into a consent order with the Federal Reserve Board (the 'FRB') (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. HSBC Bank USA is not currently in compliance with the OCC Order. Steps are being taken to address the requirements of the Orders.

In December 2012, HSBC Holdings, HNAH and HSBC Bank USA entered into agreements with US and UK government agencies regarding past inadequate compliance with the BSA, AML and sanctions laws. Among those agreements, HSBC Holdings and HSBC Bank USA entered into a five-year deferred prosecution agreement with, among others, the DoJ (the 'US DPA'); and HSBC Holdings consented to a cease-and-desist order, and HSBC Holdings and HNAH consented to a civil money penalty order with the FRB.

HSBC Holdings also entered into an agreement with the Office of Foreign Assets Control ('OFAC') regarding historical transactions involving parties subject to OFAC sanctions, as well as an undertaking with the UK FCA to comply with certain forward-looking AML and sanctions-related obligations. In addition, HSBC Bank USA entered into civil money penalty orders with the Financial Crimes Enforcement Network of the US Treasury Department and the OCC.

Under these agreements, HSBC Holdings and HSBC Bank USA made payments totalling US\$1.9 billion to US authorities and undertook various further obligations, including, among others, to continue to cooperate fully with the DoJ in any and all investigations, not to commit any crime under US federal law subsequent to the signing of the agreement, and to retain an independent compliance monitor (the 'Monitor'). In February 2017, the Monitor delivered his third annual follow-up review report. The Monitor will deliver a fourth annual follow-up review report shortly.

Through his country-level reviews, the Monitor identified potential anti-money laundering and sanctions compliance issues that the DoJ and HSBC are reviewing further with the DoJ, FRB and/or FCA. In December 2017, the US DPA entered into in December 2012 expired. HSBC fulfilled its commitments, and, therefore, under the terms of the DPA, the Department of Justice will file a motion with the US District Court for the Eastern District of New York seeking the dismissal of the charges deferred by the agreement. The Monitor overseeing HSBC's progress under the US DPA has also been serving since July 2013 as HSBC's Skilled Person under a 2012 direction issued by the UK Financial Conduct Authority and will continue in that capacity for a period of time at the discretion of the UK FCA. Additionally, HSBC is the subject of other ongoing investigations and reviews by the DoJ. HSBC Bank plc is also the subject of an investigation by the FCA into its compliance with UK money laundering regulations and financial crime systems and controls requirements.

These settlements with US and UK authorities have led to private litigation, and do not preclude further private litigation related to HSBC's compliance with applicable BSA, AML and sanctions laws or other regulatory or law enforcement actions for BSA, AML, sanctions or other matters not covered by the various agreements.

Since November 2014, four lawsuits, the details of which are below, have been filed in federal court in New York and Illinois, against various HSBC companies (including the group) and others, on behalf of plaintiffs who are, or are related to, victims of terrorist attacks in Iraq and Jordan. 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. These actions are all at early stages.

In November 2014, a complaint was filed in the US District Court for the Eastern District of New York on behalf of representatives of US persons alleged to have been killed or injured in Iraq between April 2004 and November 2011. The complaint was filed against HSBC Holdings, HSBC Bank plc, HSBC Bank USA and HSBC Bank Middle East Limited, as well as other non-HSBC banks and the Islamic Republic of Iran (together, the 'Defendants'). The plaintiffs allege that Defendants violated the US Anti-Terrorism Act ('US ATA') by altering or falsifying payment messages involving Iran, Iranian parties and Iranian banks for transactions processed through the US. The Defendants filed a Motion to Dismiss in May 2015 and an amended Motion to Dismiss in September 2017, following the filing by the Plaintiffs of a Second Amended Complaint in July 2017. In July 2017, the various motions before the Court were referred for review and for the issuance of a judicial report and recommendations prior to being decided.

In November 2015, a complaint was filed in the US District Court for the Northern District of Illinois on behalf of representatives of US persons alleged to have been killed or injured in terrorist attacks on three hotels in Amman, Jordan in 2005. The complaint was filed against HSBC Holdings, HSBC Bank USA, HNAH, HSI, HSBC Finance, HSBC USA Inc. and HSBC Bank Middle East Limited, as well as non-HSBC bank, Al Rajhi Bank (together the 'Defendants'). The plaintiffs allege that the HSBC defendants violated the US ATA by failing to enforce due diligence methods to prevent its financial services from being used to support the terrorist attacks. In early January 2017, the Defendants filed various Motions, including a Motion to Dismiss from the Plaintiffs' Complaint HSBC Bank Middle East Limited and another HSBC defendant. In August 2017, the Court issued a favourable decision by dismissing the claim filed against the group for the lack of personal jurisdiction over it. The proceedings continue against other HSBC defendants.

In November 2016, a complaint was filed in the Southern District of Illinois on behalf of representatives of US soldiers killed or injured whilst serving in Iraq. The complaint was filed against HSBC Holdings plc, HSBC Bank plc, HSBC Bank Middle East Limited, HSBC Bank USA, N.A and other non-HSBC banks, Deutsche Bank AG, Barclays Bank plc, Standard Chartered Bank, Royal Bank of Scotland, N.V., Credit Suisse AG, Bank Saderat plc and Commerzbank AG (together the 'Defendants'). The plaintiffs allege that the HSBC defendants violated the US ATA by altering or falsifying payment messages involving Iran, Iranian parties and Iranian banks for transactions processed through the US. In December 2017, the Defendants filed a Motion to Transfer the action to the Eastern District of New York which was granted in April 2017. In January 2017, the Plaintiffs filed a First Amended Complaint which named an additional HSBC defendant, HSBC North America Holdings Inc. In October 2017 the Plaintiffs voluntarily withdrew the case against all defendants [but remain at liberty to refile].

In November 2017, a complaint was filed in the Southern District of New York on behalf of representatives of US soldiers killed or injured whilst serving in Iraq. The complaint was filed against HSBC Holdings plc, HSBC Bank plc, HSBC Bank Middle East Limited, HSBC Bank USA, N.A, HSBC North America Holdings Inc. and other non-HSBC Banks, Deutsche Bank AG, Barclays Bank plc, Standard Chartered Bank, Royal Bank of Scotland, N.V., Royal Bank of Scotland plc, Credit Suisse AG, Bank Saderat plc and Commerzbank AG, Commerzbank AG, New York Branch, BNP Paribas S.A., Credit Agricole S.A., Credit Agricole Corporate & Investment Bank (together the 'Defendants'). The plaintiffs allege that the HSBC defendants violated the US ATA by altering or falsifying payment messages involving Iran, Iranian parties and Iranian banks for transactions processed through the US and also allege breaches of US Justice Against Sponsors of Terrorism Act ('JASTA'). The proceedings are at the very early stage of service upon the defendants.

Based on the facts currently known, it is not practicable at this time for HSBC to predict the resolution of these lawsuits, including the timing or any possible impact on HSBC, which could be significant.

Foreign exchange rate investigations and litigation

Various regulators and competition and law enforcement authorities around the world, including in the EU, Switzerland, Brazil, South Korea and South Africa, are conducting civil and criminal investigations and reviews into trading by HSBC and others on the foreign exchange markets. HSBC is cooperating with these investigations and reviews and settlements relevant to the group are detailed below.

In May 2015, the DoJ resolved its investigations with respect to five non-HSBC financial institutions, four of whom agreed to plead guilty to criminal charges of conspiring to manipulate prices in the foreign exchange spot market, and resulting in the imposition of criminal fines in the aggregate of more than US\$2.5 billion. Additional penalties were imposed at the same time by the FRB and other banking regulators. HSBC was not a party to these resolutions. In August 2016, the DoJ indicted two now-former HSBC employees and charged them with wire fraud and conspiracy relating to a 2011 foreign exchange transaction. One of the former employees was found guilty in October 2017 of one count of conspiracy to commit wire fraud and eight counts of wire fraud. HSBC was not named as a defendant in the indictment.

In September 2017, HSBC Holdings and HNAH consented to a civil money penalty order with the FRB in connection with its investigation into HSBC's historic foreign exchange activities. Under the terms of the order, HSBC Holdings and HNAH agreed to pay a civil money penalty of US\$175 million to the FRB.

In January 2018, HSBC Holdings entered into a three-year deferred prosecution agreement with the Criminal Fraud Division of the DoJ, covering conduct in 2010 and 2011, and received a declination from the Antitrust Division of the DoJ, concluding its investigation into HSBC's historic foreign exchange activities. Under the terms of the deferred prosecution agreement, HSBC agreed to pay a penalty and restitution of US\$101.5 million and undertook various further obligations, including, among others, to continue to cooperate fully with the DoJ in any and all investigations, not to commit any crime under US federal law subsequent to the signing of the agreement.

34 Related party transactions

The ultimate parent company of the group is HSBC Holdings plc, which is incorporated in England.

Copies of the HSBC Holdings plc financial statements may be obtained from the following address:

HSBC Holdings plc
8 Canada Square
London
E14 5HQ

Related parties of the group include the parent, fellow subsidiaries, associates, joint ventures, post-employment benefit plans for HSBC employees, Key Management Personnel as defined by IAS 24 'Related Party Disclosures', close family members of Key Management Personnel and entities which are controlled, jointly controlled or significantly influenced by Key Management Personnel or their close family members. Key Management Personnel are defined as those persons having authority and responsibility for planning, directing and controlling the activities of HSBC Bank Middle East Limited and the group and includes members of the Boards of Directors of HSBC Bank Middle East Limited.

Particulars of transactions with related parties are tabulated below. The disclosure of the year-end balance and the highest amounts outstanding during the year is considered to be the most meaningful information to represent the amount of the transactions and outstanding balances during the year.

Key Management Personnel

The emoluments of a number of the Key Management Personnel are paid by other HSBC Group companies who make no recharge to the group. The Directors are also Directors of a number of other HSBC Group companies and it is not possible to make a reasonable apportionment of their emoluments in respect of each of the companies. Accordingly, no emoluments in respect of the Directors paid by other HSBC Group companies and applicable to the group has been included in the following disclosure.

Transactions, arrangements and agreements including Key Management Personnel

Compensation of Key Management Personnel

	2017 US\$000	2016 US\$000
Remuneration (wages and bonus)	6,516	8,959
Post-employment benefits	231	793
Share-based payments	2,357	2,221
Year ended 31 Dec	9,104	11,973

The table below sets out transactions which fall to be disclosed under IAS 24 between the group and the Key Management Personnel of both the bank and its parent company, HSBC Holdings plc, and their connected persons or controlled companies.

Transactions and balances during the year with Key Management Personnel

	2017		2016	
	Balance at 31 Dec US\$000	Highest amounts outstanding during year US\$000	Balance at 31 Dec US\$000	Highest amounts outstanding during year US\$000
Key Management Personnel				
Loans	861	1,239	875	875
Credit cards	271	271	47	197

¹ Includes Key Management Personnel, close family members of Key Management Personnel and entities that are controlled or jointly controlled by Key Management Personnel or their close family members.

Notes on the Financial Statements

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.

Transactions with other related parties

Associates

Transactions and balances during the year with associates

	2017		2016	
	Highest balance during the year	Balance at 31 Dec	Highest balance during the year	Balance at 31 Dec
	US\$000	US\$000	US\$000	US\$000
Amounts due from associates	–	–	31,552	–
Amounts due to associates	1,088	1,088	30,039	567

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.

Transactions of the group with HSBC Holdings plc and fellow subsidiaries of HSBC Holdings plc

Transactions detailed below include amounts due to/from HSBC Holdings plc

	2017		2016	
	Highest balance during the year	Balance at 31 Dec	Highest balance during the year	Balance at 31 Dec
	US\$000	US\$000	US\$000	US\$000
Assets				
Loans and advances to customers	1,400	1,021	2,283	1,400
Liabilities				
Customer accounts	9,069	7,362	15,814	9,069
			For the year ended 31 Dec 2017	For the year ended 31 Dec 2016
			US\$000	US\$000
Income statement				
Fee expense			–	1,455
Other operating income			884	2,060
General and administrative expenses			18,885	17,786

Transactions detailed below include amounts due to/from fellow subsidiaries of HSBC Holdings plc

	2017		2016	
	Highest balance during the year	Balance at 31 Dec	Highest balance during the year	Balance at 31 Dec
	US\$000	US\$000	US\$000	US\$000
Assets				
Trading assets	279,991	53,231	207,798	24,843
Derivatives	741,414	681,295	718,846	718,846
Loans and advances to banks (including reverse repos)	2,318,277	2,114,401	2,401,705	957,266
Financial investments: available for sale	61,346	59,630	–	–
Liabilities				
Trading liabilities	217,003	6,457	275,026	4,963
Deposits by banks	2,846,052	1,614,023	3,049,560	2,846,052
Derivatives	1,250,075	783,896	1,254,957	1,250,075
Subordinated amounts due	950,000	950,000	950,000	950,000
Off-balance sheet				
Guarantees	2,626,646	2,626,646	2,443,865	2,400,861
Documentary credit and short-term trade-related transactions	108,402	75,909	133,107	57,866
			For the year ended 31 Dec 2017	For the year ended 31 Dec 2016
			US\$000	US\$000
Income Statement				
Interest income			5,317	12,490
Interest expense			63,506	63,803
Fee income			61,716	58,913
Fee expense			21,142	12,358
Other operating income			46,304	42,794
General and administrative expenses			111,407	100,549

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.

Transactions between HSBC Bank Middle East Limited and its subsidiaries

Transactions detailed below include amounts due to/from HSBC Bank Middle East Limited and its subsidiaries

	2017		2016	
	Highest balance during the year	Balance at 31 Dec	Highest balance during the year	Balance at 31 Dec
	US\$000	US\$000	US\$000	US\$000
Assets				
Loans and advances to customers	300,347	5,535	349,233	296,545
Liabilities				
Customer accounts	49,015	49,015	29,336	28,511

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.

35 Events after the balance sheet date

A fourth interim dividend for 2017 of US\$0.1504 per ordinary share (a distribution of US\$140 million) was declared by the Directors on 13 February 2018.

These accounts were approved by the Board of Directors on 18 February 2018 and authorised for issue.

HSBC Bank Middle East Limited and other HSBC Group Offices in the Region

HSBC Bank Middle East Limited

Head Office

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Dubai International Financial Centre

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Middle East Management Office

HSBC Building

Emaar Square

P O Box 66

Dubai

United Arab Emirates

ALGERIA

El Mohammadia branch

Hydra branch

Oran branch

BAHRAIN

Seef – Main Branch

Adliya

Manama – Batelco Building

Sanad

KUWAIT

Kuwait City – Sharq Area

QATAR

Doha – Airport Road (Main Branch)

Doha – City Centre

Doha – Salwa Road

UNITED ARAB EMIRATES

Abu Dhabi – Old Airport Road

Dubai – Deira Al Muraqqabat

Dubai – Bur Dubai

Dubai – Jumeirah

Jebel Ali – Free Trade Zone

Fujairah – Hamad Bin Abdulla St

Ras Al Khaimah – Corniche Rd

Sharjah – King Faisal Road

7 Customer Service Units and 2 Management Offices

Principal Subsidiary Companies

HSBC Financial Services (Middle East) Limited

HSBC Middle East Securities LLC

HSBC Middle East Finance Company Limited

HSBC Bank Middle East Representative Office Morocco
S.A.R.L.

Associated Companies

MENA Infrastructure Fund (GP) Limited

Special Connections With These Members Of The HSBC Group

HSBC Bank Oman S.A.O.G.

HSBC Bank Egypt S.A.E.

HSBC Bank International Limited

HSBC Securities (Egypt) S.A.E.

HSBC Electronic Data Service Delivery (Egypt) S.A.E.

HSBC Saudi Arabia Limited

The Saudi British Bank

SABB Takaful Limited

HSBC Private Bank (Suisse) SA (DIFC Branch)

HSBC Middle East Leasing Partnership

HSBC Bank A.S.

HSBC BANK MIDDLE EAST LIMITED

Incorporated in the Dubai International Financial Centre number – 2199

Regulated by the Dubai Financial Services Authority.

REGISTERED OFFICE

Level 1, Building No. 8, Gate Village, Dubai International Financial Centre, Dubai, United Arab Emirates.

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