HSBC Bank plc

Pillar 3 Disclosures at 31 December 2017

HSBC

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Certain defined terms

Unless the context requires otherwise, 'HSBC Holdings' means HSBC Holdings plc, and 'HSBC' and the 'Group' refer to HSBC Holdings together with its subsidiaries; similarly, 'HSBC Bank' and the 'bank' mean HSBC Bank plc, and the 'group' refers to HSBC Bank together with its subsidiaries. When used in the terms 'shareholders' equity' and 'total shareholders' equity', 'shareholders' means holders of HSBC Holdings ordinary shares and those preference shares and capital securities issued by HSBC Holdings classified as equity. The abbreviations '£m' and '£bn' represent millions and billions (thousands of millions) of GB pounds respectively.

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Introduction

Table 1: Pillar 1 overview

	Footnotes	RWAs 2017 £m	RWAs 2016 £m	Capital required[1] 2017 £m	Capital required[1] 2016 £m
Credit risk	2	**164,767**	168,936	**13,182**	13,515
Counterparty credit risk		**24,018**	28,593	**1,921**	2,287
Market risk		**20,978**	24,975	**1,678**	1,998
Operational risk		**23,310**	22,733	**1,865**	1,819
At 31 Dec		**233,073**	245,237	**18,646**	19,619

Table 2: RWAs by global business[3]

	RWAs 2017 £m	RWAs 2016 £m	Capital required[1] 2017 £m	Capital required[1] 2016 £m
Retail Banking and Wealth Management ('RBWM')	**26,676**	25,849	**2,134**	2,068
Commercial Banking ('CMB')	**85,448**	81,958	**6,836**	6,557
Global Banking and Markets ('GB&M')	**97,397**	105,932	**7,792**	8,474
Global Private Banking ('GPB')	**3,540**	3,509	**283**	281
Corporate Centre	**20,012**	27,989	**1,601**	2,239
At 31 Dec	**233,073**	245,237	**18,646**	19,619

1 *'Capital required', here and in all tables where the term is used, represents the Pillar 1 capital charge at 8% of RWAs.*
2 *'Credit Risk', here and in all tables where the term is used, excludes counterparty credit risk.*
3 *Please refer to pages 4 and 5 of the HSBC Bank plc* Annual Report and Accounts 2017 *for a description of the activities of our global businesses.*

Regulatory framework for disclosures

HSBC is supervised on a consolidated basis in the UK by the Prudential Regulatory Authority ('PRA'), which receives information on the capital adequacy of, and sets capital requirements for, the Group as a whole. Individual banking subsidiaries are directly regulated by their local banking supervisors, including the PRA itself in certain circumstances (for example, the bank), who set and monitor local capital adequacy requirements. In most jurisdictions, non-banking financial subsidiaries are also subject to the supervision and capital requirements of local regulatory authorities.

At the consolidated HSBC and bank level, we calculated capital for prudential regulatory reporting purposes throughout 2017 using the Basel III framework of the Basel Committee on Banking Supervision ('BCBS') as implemented by the EU in the amended Capital Requirements Directive and Regulation, collectively known as CRD IV, and in the PRA's rulebook for the UK banking industry. The regulators of HSBC banking entities outside the EU are at varying stages of implementation of the BCBS' framework, so local regulation in 2017 may have been on the basis of a previous framework.

The Basel Committee's framework is structured around three 'pillars': Pillar 1 minimum capital requirements and Pillar 2 supervisory review process are complemented by Pillar 3 market discipline. The aim of Pillar 3 is to produce disclosures that allow market participants to assess the scope of application by banks of the Basel Committee's framework and the rules in their jurisdiction, their capital condition, risk exposures and risk management processes, and hence their capital adequacy.

Pillar 3 requires all material risks to be disclosed, enabling a comprehensive view of a bank's risk profile.

The PRA's final rules adopted national discretions in order to accelerate significantly the transition timetable to full 'end point' CRD IV compliance.

Pillar 3 disclosures

The HSBC Bank *Pillar 3 Disclosures 2017* comprise all information required under Pillar 3, both quantitative and qualitative. They are made in accordance with Part 8 of the Capital Requirements Regulation within CRD IV, supplemented by any specific additional requirements of the PRA and discretionary disclosures on our part.

In our disclosures, to give insight into movements during the year, we provide comparative figures for the previous year. Key ratios and figures are reflected throughout the *Pillar 3 Disclosures 2017* and are also available on page 56 of the HSBC Bank plc *Annual Report and Accounts 2017*. Where disclosures have been enhanced or are new, we do not generally restate or provide prior year comparatives. The own funds disclosure in Table 4 tracks the position from a CRD IV transitional to an end-point basis.

Information relating to the rationale for withholding certain disclosures is provided in Appendix I.

We publish comprehensive Pillar 3 disclosures annually on the HSBC website, www.hsbc.com, simultaneously with the release of our HSBC Bank plc *Annual Report and Accounts*. Our Interim Reports include regulatory information complementing the financial and risk information presented there and in line with the new requirements on the frequency of regulatory disclosures.

Pillar 3 requirements may be met by inclusion in other disclosure media. Where we adopt this approach, references are provided to the relevant pages of the *Annual Report and Accounts 2017* or other location.

We continue to engage in the work of the UK authorities and industry associations to improve the transparency and comparability of UK banks' Pillar 3 disclosures.

Regulatory developments

Basel Committee

In December, the Basel Committee ('Basel') published the revisions to the Basel III framework (sometimes referred to as 'Basel IV'). The final package includes:

- widespread changes to the risk weights under the standardised approach to credit risk;
- a change in the scope of application of the internal rating based ('IRB') approach to credit risk, together with changes to the IRB methodology;
- the replacement of the operational risk approaches with a single methodology;
- an amended set of rules for the credit valuation adjustment ('CVA') capital framework;
- an aggregate output capital floor that ensures that banks' total risk-weighted assets ('RWAs') are no lower than 72.5% of those generated by the standardised approaches; and
- changes to the exposure measure for the leverage ratio, together with the imposition of a leverage ratio buffer for global systemically important institutions ('G-SIB'). This will take the form of a Tier 1 capital buffer set at 50% of the GSIB's RWA capital buffer.

Basel has announced that the package will be implemented on 1 January 2022, with a 5 year transitional provision for the output floor from that date, commencing at a rate of 50%.

HSBC is currently evaluating the final package. Given that the package contains a significant number of national discretions and that Basel has committed to re-calibrate the market risk elements of the final framework during 2018, significant uncertainty remains as to the impact.

In all instances, the final standards will have to be transposed into the relevant local law before coming into effect.

In addition, during 2017, Basel proposed other revisions to the regulatory capital framework. In particular, it published:

- a discussion paper on the treatment of sovereign exposures;
- the final guidelines regarding the identification and management of step-in risk;
- the interim regulatory treatment and transitional requirements for International Financial Reporting Standard 9, Financial Instruments ('IFRS 9') provisions;
- the final phase 2 Pillar 3 standards; and
- proposals to revise the G-SIB assessment framework.

Financial Stability Board

In July, the Financial Stability Board ('FSB') expanded its resolution reform policy framework with the publication of its 'Guiding Principles on the Internal Total Loss-absorbing Capacity of G-SIBs ('Internal TLAC')'. These guidelines supplement the FSB's TLAC standard published in November 2015. In addition, the FSB published consultations on other outstanding issues related to its resolution framework. Again, these need to be incorporated into the relevant local law before coming into effect.

European Union

In the European Union ('EU'), elements of Basel's and the FSB's reforms are being implemented through revisions to the Capital Requirements Regulation and Capital Requirements Directive (collectively referred to as 'CRR2') and the EU resolution framework. The key components of CRR2 include changes to the market risk framework under the Fundamental Review of the Trading Book, the counterparty credit risk framework and a binding leverage ratio. It also includes details of the minimum requirements for TLAC, which in the EU is known as the 'Minimum Requirements for own funds and Eligible Liabilities' ('MREL'). The CRR2 changes are expected to be finalised in 2018 and apply from 1 January 2021, although certain elements, such as MREL, are expected to apply from 1 January 2019.

In December, the EU's IFRS 9 transitional capital arrangements were formally published and the European Banking Authority ('EBA') published its final guidelines on the IFRS 9 disclosures. Separately, the final changes to the capital rules on securitisation were also published formally by the EU with implementation expected on 1 January 2019 for new transactions and on 1 January 2020 for existing positions. In addition, during 2017 the EBA published a consultation on the methods of prudential consolidation under the EU's rules.

Also in December, in line with the EU's rules, the requirement to have a Basel I floor lapsed and the PRA confirmed that its application is no longer required. A new output floor will be implemented as part of the Basel IV amendments.

Bank of England

In March, HSBC received from the Bank of England ('BoE') its indicative MREL requirement applicable to HSBC Holdings plc and its European Resolution Group (comprised of HSBC Bank plc and its subsidiaries). This includes interim MREL requirements effective from 1 January 2019 and final requirements effective from 1 January 2022. The BoE also confirmed formally that 'multiple-point-of-entry' ('MPE') is the preferred resolution strategy for HSBC. In May, the BoE published the quantum of MREL requirements for major UK banks.

In addition, during 2017, the BoE and the PRA proposed other revisions to the regulatory capital and MREL frameworks. In particular, they published proposals and/or final rules setting out:

- the approach to setting internal MREL and the setting of MREL for MPE groups;
- the interaction of MREL with both the capital and leverage ratio buffers;
- changes to the groups and double leverage policy;
- the policy refining the PRA's Pillar 2A capital requirements and disclosure; and
- the policy to ensure that valuation processes do not impede resolvability.

Lastly, in June, the Financial Policy Committee raised the countercyclical buffer rate for UK exposures to 0.5%, to apply from June 2018, and in November, increased it further to 1% with binding effect from November 2018.

Linkage to the *Annual Report and Accounts 2017*

Structure of the regulatory group

Subsidiaries engaged in insurance activities are excluded from the regulatory consolidation by excluding assets, liabilities and post-acquisition reserves. The group's investments in these insurance subsidiaries are recorded at cost and deducted from common equity tier 1 ('CET1') capital (subject to thresholds).

The regulatory consolidation also excludes special purpose entities ('SPEs') where significant risk has been transferred to third parties. Exposures to these SPEs are risk-weighted as securitisation positions for regulatory purposes.

Participating interests in banking associates are proportionally consolidated for regulatory purposes by including our share of assets, liabilities, profit and loss, and risk-weighted assets ('RWAs') in accordance with the PRA's application of EU legislation. Non-participating significant investments, along with non-financial associates, are deducted from capital (subject to thresholds).

Table 3: Reconciliation of balance sheets – financial accounting to regulatory scope of consolidation

	Ref †	Accounting balance sheet	Deconsolidation of insurance/ other entities	Consolidation of banking associates	Regulatory balance sheet
		£m	£m	£m	£m
Assets					
Cash and balances at central banks		**97,601**	**–**	**109**	**97,710**
Items in the course of collection from other banks		**2,023**	**–**	**–**	**2,023**
Trading assets		**145,725**	**94**	**127**	**145,946**
Financial assets designated at fair value		**9,266**	**(9,219)**	**–**	**47**
Derivatives		**143,335**	**(54)**	**–**	**143,281**
Loans and advances to banks		**14,149**	**(124)**	**1**	**14,026**
Loans and advances to customers		**280,402**	**(2,564)**	**–**	**277,838**
– of which: impairment allowances on IRB portfolios	*h*	***(1,871)***	**–**	**–**	***(1,871)***
Reverse repurchase agreements – non-trading		**45,808**	**–**	**–**	**45,808**
Financial investments		**58,000**	**(11,771)**	**157**	**46,386**
Capital invested in insurance and other entities		**–**	**630**	**–**	**630**
Prepayments, accrued income and other assets		**16,026**	**(1,446)**	**23**	**14,603**
– of which: retirement benefit assets	*i*	***6,066***	**–**	**–**	***6,066***
Current tax assets		**140**	**(3)**	**–**	**137**
Interests in associates and joint ventures		**327**	**(3)**	**(313)**	**11**
Goodwill and intangible assets	*e*	**5,936**	**(591)**	**–**	**5,345**
Deferred tax assets	*f*	**130**	**129**	**–**	**259**
Total assets at 31 Dec 2017	*o*	**818,868**	**(24,922)**	**104**	**794,050**
Liabilities and equity					
Liabilities					
Deposits by banks		**29,349**	**(48)**	**92**	**29,393**
Customer accounts		**381,546**	**535**	**–**	**382,081**
Repurchase agreements – non-trading		**37,775**	**–**	**–**	**37,775**
Items in the course of transmission to other banks		**1,089**	**–**	**–**	**1,089**
Trading liabilities		**106,496**	**635**	**–**	**107,131**
Financial liabilities designated at fair value		**18,249**	**(537)**	**–**	**17,712**
– of which:					
included in tier 1	*k*	***339***	**–**	**–**	***339***
included in tier 2	*l, m*	***1,751***	**–**	**–**	***1,751***
Derivatives		**140,070**	**34**	**–**	**140,104**
Debt securities in issue		**13,286**	**(2,480)**	**–**	**10,806**
Accruals, deferred income and other liabilities		**6,615**	**(1,288)**	**12**	**5,339**
Current tax liabilities		**88**	**(38)**	**–**	**50**
Liabilities under insurance contracts		**21,033**	**(21,033)**	**–**	**–**
Provisions		**1,796**	**(6)**	**–**	**1,790**
– of which: credit-related contingent liabilities and contractual commitments on IRB portfolios	*h*	***53***	**–**	**–**	***53***
Deferred tax liabilities		**933**	**–**	**–**	**933**
Subordinated liabilities		**16,494**	**–**	**–**	**16,494**
– of which:					
included in tier 1	*k*	***700***	**–**	**–**	***700***
included in tier 2	*l, m, n*	***5,690***	**–**	**–**	***5,690***
Total liabilities at 31 Dec 2017		**774,819**	**(24,226)**	**104**	**750,697**
Equity					
Called up share capital	*a*	**797**	**–**	**–**	**797**
Other equity instruments	*j*	**3,781**	**–**	**–**	**3,781**
Other reserves	*c, g*	**2,744**	**–**	**–**	**2,744**
Retained earnings	*b, c*	**36,140**	**(696)**	**–**	**35,444**
Total shareholders' equity		**43,462**	**(696)**	**–**	**42,766**
Non-controlling interests	*d, k*	**587**	**–**	**–**	**587**
– of which: non-cumulative preference shares issued by subsidiaries included in tier 1 capital	*k*	**–**	**–**	**–**	**–**
Total equity at 31 Dec 2017		**44,049**	**(696)**	**–**	**43,353**
Total liabilities and equity at 31 Dec 2017		**818,868**	**(24,922)**	**104**	**794,050**

Table 3: Reconciliation of balance sheets – financial accounting to regulatory scope of consolidation (continued)

	Ref †	Accounting balance sheet	Deconsolidation of insurance/ other entities	Consolidation of banking associates	Regulatory balance sheet
		£m	£m	£m	£m
Assets					
Cash and balances at central banks		54,278	—	69	54,347
Items in the course of collection from other banks		1,363	—	—	1,363
Trading assets		125,069	74	106	125,249
Financial assets designated at fair value		8,345	(8,329)	—	16
Derivatives		199,419	(117)	—	199,302
Loans and advances to banks		21,363	(102)	7	21,268
Loans and advances to customers		272,760	(2,345)	—	270,415
– *of which: impairment allowances on IRB portfolios*	*h*	*(1,735)*	—	—	*(1,735)*
Reverse repurchase agreements – non-trading		31,660	297	—	31,957
Financial investments		83,135	(12,032)	110	71,213
Capital invested in insurance and other entities		—	613	—	613
Prepayments, accrued income and other assets		13,215	(898)	29	12,346
– *of which: retirement benefit assets*	*i*	*3,480*	—	—	*3,480*
Current tax assets		114	(6)	—	108
Interests in associates and joint ventures		266	(3)	(231)	32
Goodwill and intangible assets	*e*	5,735	(595)	5	5,145
Deferred tax assets	*f*	107	150	4	261
Total assets at 31 Dec 2016	*o*	816,829	(23,293)	99	793,635
Liabilities and equity					
Liabilities					
Deposits by banks		23,682	(21)	61	23,722
Customer accounts		375,252	1,159	—	376,411
Repurchase agreements – non-trading		19,709	—	—	19,709
Items in the course of transmission to other banks		657	—	—	657
Trading liabilities		93,934	519	1	94,454
Financial liabilities designated at fair value		18,486	(1,080)	—	17,406
– *of which:*					
included in tier 1	*k*	*333*	—	—	*333*
included in tier 2	*l, m*	*1,685*	—	—	*1,685*
Derivatives		190,092	151	—	190,243
Debt securities in issue		16,140	(3,144)	—	12,996
Accruals, deferred income and other liabilities		6,792	(480)	28	6,340
Current tax liabilities		400	(46)	1	355
Liabilities under insurance contracts		19,724	(19,724)	—	—
Provisions		2,431	(5)	2	2,428
– *of which: credit-related contingent liabilities and contractual commitments on IRB portfolios*	*h*	*50*	—	—	*50*
Deferred tax liabilities		484	—	—	484
Subordinated liabilities		8,421	—	—	8,421
– *of which:*					
included in tier 1	*k*	*700*	—	—	*700*
included in tier 2	*l, m, n*	*6,939*	—	—	*6,939*
Total liabilities at 31 Dec 2016		776,204	(22,671)	93	753,626
Equity					
Called up share capital	*a*	797	—	—	797
Share premium account	*a, k*	20,733	—	—	20,733
Other equity instruments	*j*	3,781	—	—	3,781
Other reserves	*c, g*	1,882	—	—	1,882
Retained earnings	*b, c*	12,737	(622)	6	12,121
Total shareholders' equity		39,930	(622)	6	39,314
Non-controlling interests	*d, k*	695	—	—	695
– *of which: non-cumulative preference shares issued by subsidiaries included in tier 1 capital*	*k*	150	—	—	*150*
Total equity at 31 Dec 2016		40,625	(622)	6	40,009
Total liabilities and equity at 31 Dec 2016		816,829	(23,293)	99	793,635

† *The references (a) – (n) identify balance sheet components which are used in the calculation of regulatory capital on page 8.*

Capital and Leverage

Capital management

Approach and policy

Our approach to capital management is driven by our strategic and organisational requirements, taking into account the regulatory, economic and commercial environment in which we operate.

It is our objective to maintain a strong capital base to support the development of our business and to exceed regulatory capital requirements at all times. To achieve this, we manage our capital within the context of an annual capital plan that is approved by the Board and determines the optimal amount and mix of capital required to support planned business growth and meet local regulatory capital requirements.

Our policy on capital management is underpinned by the capital management framework and our internal capital adequacy assessment process, which enable the group to manage its capital in a consistent manner. The framework incorporates a number of different capital measures that govern the management and allocation of capital within the group. These capital measures are defined by the group as follows:

- invested capital is the equity capital provided to the bank by HSBC;
- economic capital is the internally calculated capital requirement that is deemed necessary by the group to support the risks to which it is exposed; and
- regulatory capital is the minimum level of capital that the group is required to hold in accordance with the rules established by the PRA for the bank and the group, and by the local regulators for individual subsidiary companies.

The following risks managed through the capital management framework have been identified as material: credit, market, operational, interest rate risk in the banking book, pensions, insurance and residual risks.

Stress testing

Stress testing is incorporated into the capital management framework, and is an important component of understanding the sensitivity of the core assumptions in the group's capital plans to the adverse effect of extreme, but plausible, events. Stress testing allows senior management to formulate its response, including risk mitigating actions, in advance of conditions starting to reflect the stress scenarios identified. The actual market stresses experienced by the financial system in recent years have been used to inform the capital planning process and further develop the scenarios employed by the group in its internal stress tests.

Other stress tests are also carried out, both at the request of regulators and by the regulators themselves, using their prescribed assumptions. The group takes into account the results of all such regulatory stress testing when assessing its internal capital requirements.

Risks to capital

Outside the stress testing framework, a list of principal risks is regularly evaluated for their effect on our capital ratios. In addition, other risks may be identified that have the potential to affect our RWAs and/or capital position. The downside or upside scenarios are assessed against our capital management objectives and mitigating actions are assigned as necessary.

The group's approach to managing its capital position has been to ensure the bank, its regulated subsidiaries and the group exceed current regulatory requirements, and it is well placed to meet expected future capital requirements.

Risk-weighted asset targets

RWA targets for our global businesses are established in accordance with the Group's strategic direction and risk appetite, and approved through the Group's annual planning process. As these targets are deployed to lower levels of management, action plans for implementation are developed. These may include growth strategies; active portfolio management; restructuring; business and/or customer-level reviews; RWA accuracy and allocation initiatives and risk mitigation.

Business performance against RWA targets is monitored through regular reporting to the Asset & Liability Management Committee.

Capital generation

HSBC Holdings plc is the sole provider of equity capital to the group and also provides non-equity capital where necessary. Capital generated in excess of planned requirements is returned to HSBC Holdings plc in the form of dividends.

Overview of regulatory capital framework

Main features of CET1, AT1 and T2 instruments issued by the group

All capital securities included in the regulatory capital base of the group have been issued either in accordance with the rules and guidance in the PRA's General Prudential Sourcebook ('GENPRU') and have been included in the capital base by virtue of the application of the CRD IV grandfathering provisions, or issued as fully compliant CRD IV securities. For regulatory purposes, the group's capital base is divided into three main categories, namely Common Equity Tier 1, Additional Tier 1 and Tier 2, depending on the degree of permanence and loss absorbency exhibited. The main features of capital securities issued by the group are described below.

Non-CRD IV compliant Additional Tier 1 and Tier 2 instruments benefit from a grandfathering period. This progressively reduces the eligible amount by 10% annually, following an initial reduction of 20% on 1 January 2014, until they are fully phased out by 1 January 2022.

Tier 1 capital ('T1')

Tier 1 capital comprises shareholders' equity, related non-controlling interests (subject to limits) and qualifying capital instruments, after certain regulatory adjustments.

Common Equity Tier 1 ('CET1')

Called up ordinary shares issued by the bank to its parent are fully paid up and the proceeds of issuance are immediately and fully available. There is no obligation to pay a coupon or dividend to the shareholder arising from this type of capital. The share capital is available for unrestricted and immediate use to cover any risks and losses.

Additional Tier 1 capital ('AT1')

Preference shares and related premium

Preference shares are securities that rank higher than ordinary shares for dividend payments, and in the event of a winding up, but generally carry no voting rights. These instruments have no stated maturity date but may be called and redeemed by the issuer, subject to prior consent from the PRA and, where applicable, the local banking regulator. There must also be no obligation to pay a dividend, and (if not paid) the dividend may not cumulate.

Further details of the HSBC Bank plc non-cumulative third dollar preference share capital can be found in Note 27 – Called up share capital and other equity instruments of the Notes on the Financial Statements on pages 130 to 131 of the HSBC Bank plc Annual Report and Accounts 2017.

Other Tier 1 capital securities

Other Tier 1 capital securities are deeply subordinated securities with some equity features that may be included as Tier 1 capital. Other Tier 1 capital securities are instruments for which there is no obligation to pay a coupon, and (if not paid) the coupon is not

cumulative. Such securities do not generally carry voting rights and rank higher than ordinary shares for coupon payments and in the event of a winding up. The securities may be called and redeemed by the issuer, subject to prior consent from the PRA and, where applicable, the local banking regulator. If not redeemed, coupons payable may step up and become floating rate related to interbank offered rates.

Further details of these instruments can be found in Note 24 – Subordinated Liabilities of the Notes on the Financial Statements on pages 125 to 126 of the HSBC Bank plc Annual Report and Accounts 2017.

Qualifying CRD IV Additional Tier 1 instruments are perpetual securities on which there is no obligation to apply a coupon and, if not paid, the coupon is not cumulative. Such securities do not carry voting rights but rank higher than ordinary shares for coupon payments and in the event of a winding up. Fully compliant CRD IV Additional Tier 1 instruments issued by the bank include a provision whereby the instrument will be written down in whole in the event the group's Common Equity Tier 1 ratio falls below 7.00%.

These instruments are accounted for as equity. Further details of qualifying CRD IV Additional Tier 1 instruments can be found in Note 27 – Called up share capital and other equity instruments of the Notes on the Financial Statements on pages 130 to 131 of the HSBC Bank plc Annual Report and Accounts 2017.

Tier 2 capital ('T2')

Tier 2 capital comprises eligible capital securities and any related share premium and other qualifying Tier 2 capital securities subject to limits. Holdings of Tier 2 capital of financial sector entities are deducted.

Perpetual and term subordinated debt

Tier 2 capital securities are either perpetual subordinated securities or dated securities on which there is an obligation to pay coupons.

These instruments or subordinated loans comprise dated loan capital repayable at par on maturity and must have an original maturity of at least five years. Some subordinated loan capital may be called and redeemed by the issuer subject to prior consent from the PRA and, where applicable, the consent of the local banking regulator. If not redeemed, interest coupons payable may step up or become floating rate related to interbank offered rates. For regulatory purposes, it is a requirement that Tier 2 instruments are amortised on a straight-line basis in their final five years to maturity, thus reducing the amount of capital that is recognised for regulatory purposes.

Further details of these instruments can be found in Note 24 – Subordinated Liabilities of the Notes on the Financial Statements on pages 125 to 126 of the HSBC Bank plc Annual Report and Accounts 2017.

A list of the features of our capital instruments in accordance with Annex III of the Commission Implementing Regulation 1423/2013 is also being published on HSBC's website with reference to our balance sheet on 31 December 2017.

Table 4: Own funds disclosure

Ref*		Ref †	At 31 Dec 2017 £m	CRD IV prescribed residual amount £m	Final CRD IV text £m
	Common equity tier 1 ('CET1') capital: instruments and reserves				
1	Capital instruments and the related share premium accounts		797		797
	– ordinary shares	a	797		797
2	Retained earnings	b	32,601		32,601
3	Accumulated other comprehensive income (and other reserves)	c	4,341		4,341
5	Minority interests (amount allowed in consolidated CET1)	d	337		337
5a	Independently reviewed interim net profits net of any foreseeable charge or dividend	b	217		217
6	**Common equity tier 1 capital before regulatory adjustments**		38,293		38,293
	Common equity tier 1 capital: regulatory adjustments				
7	Additional value adjustments		(587)		(587)
8	Intangible assets (net of related deferred tax liability)	e	(5,337)		(5,337)
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability)	f	(39)		(39)
11	Fair value reserves related to gains or losses on cash flow hedges	g	41		41
12	Negative amounts resulting from the calculation of expected loss amounts	h	(864)		(864)
14	Gains or losses on liabilities at fair value resulting from changes in own credit standing		452		452
15	Defined benefit pension fund assets	i	(4,550)		(4,550)
28	**Total regulatory adjustments to common equity tier 1**		(10,884)		(10,884)
29	**Common equity tier 1 capital**		27,409		27,409
	Additional tier 1 ('AT1') capital: instruments				
30	Capital instruments and the related share premium accounts		3,781		3,781
31	– classified as equity under IFRSs	j	3,781		3,781
33	Amount of qualifying items and the related share premium accounts subject to phase out from AT1	k	1,083	(1,083)	–
34	Qualifying tier 1 capital included in consolidated AT1 capital (including minority interests not included in CET1) issued by subsidiaries and held by third parties		44	(24)	20
36	**Additional tier 1 capital before regulatory adjustments**		4,908	(1,107)	3,801
	Additional tier 1 capital: regulatory adjustments				
37	Direct and indirect holdings of own AT1 instruments		(45)		(45)
41b	Residual amounts deducted from AT1 capital with regard to deduction from tier 2 ('T2') capital during the transitional period		(29)	29	–
	– direct and indirect holdings by the institution of the T2 instruments and subordinated loans of financial sector entities where the institution has a significant investment in those entities		(29)	29	–
43	**Total regulatory adjustments to additional tier 1 capital**		(74)	29	(45)
44	**Additional tier 1 capital**		4,834	(1,078)	3,756
45	**Tier 1 capital (T1 = CET1 + AT1)**		32,243	(1,078)	31,165

Table 4 : Own funds disclosure (continued)

Ref*		Ref †	At 31 Dec 2017 £m	CRD IV prescribed residual amount £m	Final CRD IV text £m
	Tier 2 capital: instruments and provisions				
46	Capital instruments and the related share premium accounts	l	**5,977**		**5,977**
47	Amount of qualifying items and the related share premium accounts subject to phase out from T2	m	**1,194**	**(1,194)**	**–**
48	Qualifying own funds instruments included in consolidated T2 capital (including minority interests and AT1 instruments not included in CET1 or AT1) issued by subsidiaries and held by third parties		**169**	**(141)**	**28**
49	– *of which: instruments issued by subsidiaries subject to phase out*	n	***146***	***(146)***	**–**
51	**Tier 2 capital before regulatory adjustments**		**7,340**	**(1,335)**	**6,005**
	Tier 2 capital: regulatory adjustments				
52	Direct and indirect holdings of own T2 instruments		**(30)**		**(30)**
55	Direct and indirect holdings by the institution of the T2 instruments and subordinated loans of financial sector entities where the institution has a significant investment in those entities (net of eligible short positions)		**(265)**	**(29)**	**(294)**
57	**Total regulatory adjustments to tier 2 capital**		**(295)**	**(29)**	**(324)**
58	**Tier 2 capital**		**7,045**	**(1,364)**	**5,681**
59	**Total capital (TC = T1 + T2)**		**39,288**	**(2,442)**	**36,846**
60	**Total risk-weighted assets**		**233,073**		**233,073**
	Capital ratios and buffers				
61	Common equity tier 1		**11.8%**		
62	Tier 1		**13.8%**		
63	Total capital		**16.9%**		
64	Institution specific buffer requirement		**1.27%**		
65	– capital conservation buffer requirement		**1.25%**		
66	– countercyclical buffer requirement		**0.02%**		
68	Common equity tier 1 available to meet buffers[1]		**7.3%**		
	Amounts below the threshold for deduction (before risk weighting)				
72	Direct and indirect holdings of the capital of financial sector entities where the institution does not have a significant investment in those entities (amount below 10% threshold and net of eligible short positions)		**2,127**		
73	Direct and indirect holdings by the institution of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities (amount below 10% threshold and net of eligible short positions)		**685**		
75	Deferred tax assets arising from temporary differences (amount below 10% threshold, net of related tax liability)		**774**		
	Applicable caps on the inclusion of provisions in tier 2				
77	Cap on inclusion of credit risk adjustments in T2 under standardised approach		**385**		
79	Cap for inclusion of credit risk adjustments in T2 under internal ratings-based approach		**844**		
	Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2013 and 1 Jan 2022)				
82	Current cap on AT1 instruments subject to phase-out arrangements		**1,158**		
83	Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)		**365**		
84	Current cap on T2 instruments subject to phase-out arrangements		**1,437**		
85	Amount excluded from T2 due to cap (excess over cap after redemptions and maturities)		**218**		

* *The references identify the lines prescribed in the EBA template that are applicable and where there is a value.*
† *The references (a) – (n) identify balance sheet components on page 5 that are used in the calculation of regulatory capital.*
1 *Common equity tier 1 available to meet buffers after Pillar 1 capital requirements.*

Leverage ratio

The leverage ratio was introduced into the Basel III framework as a non-risk-based limit, to supplement risk-based capital requirements. It aims to constrain the build-up of excess leverage in the banking sector, introducing additional safeguards against model risk and measurement errors. The Basel III leverage ratio is a volume-based measure calculated as tier 1 capital divided by total on- and off-balance sheet exposures. This ratio has been implemented in the EU for reporting and disclosure purposes but, at this stage, has not been set as a binding requirement.

The PRA's leverage ratio requirement applies at the highest level of UK consolidation. For HSBC, this applies at the Group level and not at the HSBC Bank plc level.

Although there is currently no binding leverage ratio requirement on the group, the risk of excess leverage is managed as part of HSBC's global risk appetite framework and monitored using a leverage ratio metric within our Risk Appetite Statement ('RAS'). The RAS articulates the aggregate level and types of risk that HSBC is willing to accept in its business activities in order to achieve its strategic business objectives. The RAS is monitored via the risk appetite profile report, which includes comparisons of actual performance against the risk appetite and tolerance thresholds assigned to each metric, to ensure that any excessive risk is highlighted, assessed and mitigated appropriately. The risk appetite profile report is presented monthly to the Risk Management Meeting ('RMM').

For the group, the leverage exposure measure is also calculated and presented to the Asset & Liability Management Committee every month.

Our fully phased-in CRD IV leverage ratio was 4.0% at 31 December 2017, up from 3.9% at 31 December 2016. Growth in tier 1 capital was partly offset by a rise in the leverage exposure measure, primarily due to a growth in on balance sheet exposures.

Table 5: Summary reconciliation of accounting assets and leverage ratio exposures

Ref*		Ref †	At 31 Dec 2017 £m	At 31 Dec 2016 £m
1	Total assets as per published financial statements	o	**818,868**	816,829
	Adjustments for:			
2	– entities which are consolidated for accounting purposes but are outside the scope of regulatory	o	**(24,818)**	(23,194)
4	– derivative financial instruments		**(68,615)**	(125,721)
5	– securities financing transactions ('SFT')		**4,860**	4,706
6	– off-balance sheet items (i.e. conversion to credit equivalent amounts of off-balance sheet exposures)		**63,229**	66,400
EU-6a	– intragroup exposures excluded from the leverage ratio exposure measure		**(3,230)**	(6,095)
7	– other		**(3,074)**	490
8	**Total leverage ratio exposure**		**787,220**	733,415

* *The references identify the lines prescribed in the EBA template. Lines represented in this table are those lines which are applicable and where there is a value.*

Table 6: Leverage ratio common disclosure

Ref*		At 31 Dec 2017 £m	31 Dec 2016 £m
	On-balance sheet exposures (excluding derivatives and SFTs)		
1	On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	**601,675**	565,731
2	(Asset amounts deducted in determining Tier 1 capital)	**(10,790)**	(9,785)
3	**Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets)**	**590,885**	555,946
	Derivative exposures		
4	Replacement cost associated with all derivatives transactions (i.e. net of eligible cash variation margin)	**14,616**	19,939
5	Add-on amounts for potential future exposure ('PFE') associated with all derivatives transactions (mark-to-market method)	**71,031**	68,336
6	Gross-up for derivatives collateral provided where deducted from the balance sheet assets pursuant to IFRSs	**3,428**	4,406
7	(Deductions of receivables assets for cash variation margin provided in derivatives transactions)	**(15,245)**	(20,962)
8	(Exempted central counterparty ('CCP') leg of client-cleared trade exposures)	**(3,031)**	(2,331)
9	Adjusted effective notional amount of written credit derivatives	**141,679**	168,700
10	(Adjusted effective notional offsets and add-on deductions for written credit derivatives)	**(137,811)**	(164,507)
11	**Total derivative exposures**	**74,667**	73,581
	Securities financing transaction exposures		
12	Gross SFT assets (with no recognition of netting), after adjusting for sales accounting transactions	**113,493**	84,114
13	(Netted amounts of cash payables and cash receivables of gross SFT assets)	**(56,684)**	(45,237)
14	Counterparty credit risk exposure for SFT assets	**4,860**	4,706
16	**Total securities financing transaction exposures**	**61,669**	43,583
	Other off-balance sheet exposures		
17	Off-balance sheet exposures at gross notional amount	**175,514**	187,969
18	(Adjustments for conversion to credit equivalent amounts)	**(112,285)**	(121,569)
19	**Total off-balance sheet exposures**	**63,229**	66,400
	Exempted exposures		
EU-19	(Exemption of intragroup exposures (solo basis))	**(3,230)**	(6,095)
	Capital and total exposures		
20	**Tier 1 capital**	**31,165**	28,853
21	**Total leverage ratio exposure**	**787,220**	733,415
22	**Leverage ratio (%)**	**4.0**	3.9
EU-23	Choice of transitional arrangements for the definition of the capital measure	**Fully phased-in**	Fully phased-in

* *The references identify the lines prescribed in the EBA template. Lines represented in this table are those lines which are applicable and where there is a value.*
† *The reference (o) identifies balance sheet components on page 5.*
1 *From 31 Dec 2017 the bank is required to report leverage ratio on a fully phased-in basis; a comparative on this basis for 31 Dec 2016 is provided.*

Capital buffers

The geographical breakdown and institution specific countercyclical buffer disclosure is published annually on the HSBC website www.hsbc.com.

Pillar 1

Pillar 1 covers the capital resources requirements for credit risk, market risk and operational risk. Credit risk includes Counterparty credit risk ('CCR') and securitisation requirements. These requirements are expressed in terms of RWAs.

Risk category	Scope of permissible approaches	Approach adopted by HSBC
Credit risk	The BCBS framework applies three approaches of increasing sophistication to the calculation of Pillar 1 credit risk capital requirements. The most basic level, the standardised approach, requires banks to use external credit ratings to determine the risk weightings applied to rated counterparties. Other counterparties are grouped into broad categories and standardised risk weightings are applied to these categories. The next level, the IRB foundation approach, allows banks to calculate their credit risk capital requirements on the basis of their internal assessment of a counterparty's probability of default ('PD'), but subjects their quantified estimates of exposure at default ('EAD') and loss given default ('LGD') to standard supervisory parameters. Finally, the IRB advanced approach allows banks to use their own internal assessment in both determining PD and quantifying EAD and LGD.	For consolidated group reporting, we have adopted the advanced IRB approach for the majority of our business. Some portfolios remain on the standardised or foundation IRB approaches: • pending the issuance of local regulations or model approval; • following the supervisory prescription of a non-advanced approach; or • under exemptions from IRB treatment.
Counterparty credit risk	Four approaches to calculating CCR and determining exposure values are defined by the BCBS: mark-to-market, original exposure, standardised and Internal Model Method ('IMM'). These exposure values are used to determine capital requirements under one of the credit risk approaches; standardised, IRB foundation or IRB advanced.	We use the mark-to-market and IMM approaches for CCR. Details of the IMM permission we have received from the PRA can be found in the Financial Services Register on the PRA website. Our aim is to increase the proportion of positions on IMM over time.
Equity	For the non-trading book, equity exposures can be assessed under standardised or IRB approaches.	For Group reporting purposes, all equity exposures are treated under the standardised approach.
Securitisation	The BCBS Framework specifies two methods for calculating credit risk requirements for securitisation positions in the non-trading book: the standardised approach and the IRB approach, which incorporates the Ratings Based Method ('RBM'), the Internal Assessment Approach ('IAA') and the Supervisory Formula Method ('SFM'). Securitisation positions in the trading book are treated within market risk, using the CRD IV standard rules.	For the majority of the securitisation non-trading book positions, we use the IRB approach, and within this principally the RBM, with lesser amounts on the IAA and the SFM. We also use the standardised approach for an immaterial amount of non-trading book positions.
Market risk	Market risk capital requirements can be determined under either the standard rules or the Internal Models Approach ('IMA'). The latter involves the use of internal Value at Risk ('VaR') models to measure market risks and determine the appropriate capital requirement. In addition to the VaR models, other internal models include Stressed VaR, Incremental Risk Charge ('IRC') and Comprehensive Risk Measure.	The market risk capital requirement is measured using internal market risk models, where approved by the PRA, or under the standard rules. Our internal market risk models comprise VaR, stressed VaR and IRC. Non-proprietary details of the scope of our IMA permission are available in the Financial Services Register on the PRA website. We are in compliance with the requirements set out in Articles 104 and 105 of the Capital Requirements Regulation.
Operational risk	The BCBS framework allows firms to calculate their operational risk capital requirement under the basic indicator approach, the standardised approach or the advanced measurement approach.	We have currently used the standardised approach in determining our operational risk capital requirement. We are in the process of implementing an operational risk model, which we will use for economic capital calculation purposes.

Pillar 2 and ICAAP

Pillar 2

We conduct an annual internal capital adequacy assessment process ('ICAAP') to determine a forward-looking assessment of our capital requirements given our business strategy, risk profile, risk appetite and capital plan. This process incorporates the group's risk management processes and governance framework. As part of our ICAAP, a range of stress tests are applied to our base capital plan. Coupled with our economic capital framework and other risk management practices, these are used to assess our internal capital adequacy requirements and inform our view of our internal capital planning buffer. The ICAAP is formally approved by the Board, which has the ultimate responsibility for the effective management of risk and approval of HSBC's risk appetite.

The ICAAP is reviewed by the PRA as part of its supervisory review and evaluation process ('SREP'), which occurs periodically to enable the regulator to define the individual capital guidance ('ICG') or minimum capital requirements for the group, and to define the PRA buffer, where required. Under the PRA's revised Pillar 2 regime the capital planning buffer has been replaced with a PRA buffer. This is not intended to duplicate the CRD IV buffers and, where necessary will be set according to the vulnerability of a bank in a stress scenario, as assessed through the annual PRA stress testing exercise.

The processes of internal capital adequacy assessment and supervisory review lead to a final determination by the PRA of ICG and any PRA buffer that may be required.

Within Pillar 2, Pillar 2A considers, in addition to the minimum capital requirements for Pillar 1 risks described above, any supplementary requirements for those risks and any requirements for risk categories not captured by Pillar 1. The risk categories to be covered under Pillar 2A depend on the specific circumstances of a firm and the nature and scale of its business.

Pillar 2B consists of guidance from the PRA on the capital buffer a firm would require in order to remain above its ICG in adverse circumstances that may be largely outside the firm's normal and direct control, for example during a period of severe but plausible downturn stress, when asset values and the firm's capital surplus may become strained. This is quantified via any PRA buffer requirement the PRA may consider necessary. The assessment of this is informed by stress tests and a rounded judgement of a firm's business model, also taking into account the PRA's view of a firm's options and capacity to protect its capital position under stress, for instance through capital generation. Where the PRA assesses a firm's risk management and governance to be significantly weak, it may also increase the PRA buffer to cover the risks posed by those weaknesses until they are addressed. The PRA buffer is intended to be drawn upon in times of stress, and its use is not of itself a breach of capital requirements that would trigger automatic restrictions on distributions. In specific circumstances, the PRA should agree a plan with a firm for its restoration over an agreed timescale.

Internal capital adequacy assessment

The Board approves the group ICAAP, and together with RMM, it examines the group's risk profile from both regulatory and economic capital viewpoints, aiming to ensure that capital resources:

- remain sufficient to support our risk profile and outstanding commitments;
- exceed current regulatory requirements, and that the group is well placed to meet those expected in the future;
- allow the bank to remain adequately capitalised in the event of a severe economic downturn stress scenario; and
- remain consistent with our strategic and operational goals, and our shareholder and investor expectations.

The minimum regulatory capital that we are required to hold is determined by the rules and guidance established by the PRA for the consolidated group and by local regulators for individual group companies. These capital requirements are a primary influence shaping the business planning process, in which RWA targets are established for our global businesses in accordance with the group's strategic direction and risk appetite.

The economic capital assessment is a more risk-sensitive measure than the regulatory minimum, as it covers a wider range of risks and takes account of the substantial diversification of risk accruing from our operations. Both the regulatory and the economic capital assessments rely upon the use of models that are integrated into our management of risk. Our economic capital models are calibrated to quantify the level of capital that is sufficient to absorb potential losses over a one-year time horizon to a 99.95% level of confidence for our banking and trading activities, and to a 99.5% level of confidence for our insurance activities and pension risks.

The ICAAP and its constituent economic capital calculations are examined by the PRA as part of its supervisory review and evaluation process. This examination informs the regulator's view of our Pillar 2 capital requirements.

A strong level of integration between our risk and our capital management framework helps to optimise our response to business demand for regulatory and economic capital. Risks that are explicitly assessed through economic capital are credit risk, including CCR, market and operational risk, non-trading book interest rate risk, insurance risk, pension risk, residual risk and structural foreign exchange risk.

Credit risk

Overview

Credit risk is the risk of financial loss if a customer or counterparty fails to meet a payment obligation under a contract. It arises principally from direct lending, trade finance and leasing business, but also from off-balance sheet products, such as guarantees and credit derivatives, and from the group's holdings of debt and other securities.

The tables below set out details of the group's credit risk exposures by exposure class and approach. Further explanation of the group's approach to managing credit risk (including details of the group's past due and impaired exposure, and its approach to credit risk impairment) can be found:

- on pages 36 to 45 of the HSBC Bank plc *Annual Report and Accounts 2017*;
- on pages 72 to 91 of the HSBC Holdings plc *Annual Report and Accounts 2017*; and
- on pages 20 to 48 of the HSBC Holdings plc *Pillar 3 Disclosures 2017*.

Table 7: Credit risk exposure – summary

	Footnotes	Exposure value	Average exposure value[4]	RWAs	Capital required
		£m	£m	£m	£m
IRB advanced approach		**334,031**	**329,171**	**110,034**	**8,803**
– central governments and central banks		**19,345**	**19,781**	**2,297**	**184**
– institutions		**11,472**	**11,738**	**3,455**	**276**
– corporates	1	**149,279**	**147,969**	**84,049**	**6,724**
– total retail		**153,935**	**149,683**	**20,233**	**1,619**
– *of which:*					
secured by mortgages on immovable property – small – and medium – sized enterprises ('SME')		***490***	***507***	***301***	***24***
secured by mortgages on immovable property non-SME		***102,203***	***99,107***	***5,287***	***423***
qualifying revolving retail		***23,277***	***22,870***	***5,026***	***402***
other SME		***6,755***	***6,720***	***4,309***	***345***
other non-SME		***21,210***	***20,479***	***5,310***	***425***
IRB securitisation positions		**19,149**	**21,281**	**9,620**	**770**
IRB non-credit obligation assets		**6,009**	**6,360**	**3,845**	**308**
IRB foundation approach		**22,755**	**22,408**	**13,950**	**1,116**
– central governments and central banks		**12**	**12**	**4**	**–**
– institutions		**7**	**21**	**2**	**–**
– corporates		**22,736**	**22,375**	**13,944**	**1,116**
Standardised approach		**163,471**	**153,437**	**27,318**	**2,185**
– central governments and central banks	2	**126,800**	**110,395**	**1,990**	**159**
– international organisations		**1,614**	**1,939**	**–**	**–**
– institutions		**6,838**	**8,334**	**1,764**	**141**
– corporates		**19,447**	**23,436**	**16,868**	**1,349**
– retail		**1,044**	**1,838**	**745**	**60**
– secured by mortgages on immovable property		**3,063**	**3,008**	**1,125**	**90**
– exposures in default		**731**	**810**	**965**	**77**
– items associated with particularly high risk		**863**	**889**	**1,294**	**104**
– securitisation positions		**194**	**39**	**206**	**16**
– claims in the form of collective investments undertakings		**30**	**39**	**30**	**2**
– equity	3	**834**	**894**	**1,862**	**149**
– other items		**2,013**	**1,816**	**469**	**38**
At 31 Dec 2017		**545,415**	**532,657**	**164,767**	**13,182**

Table 7: Credit risk exposure – summary (continued)

	Footnotes	Exposure value	Average exposure value[4]	RWAs	Capital required
		£m	£m	£m	£m
IRB advanced approach		326,096	323,898	101,726	8,137
– central governments and central banks		22,344	21,422	3,141	251
– institutions		10,717	12,800	2,565	205
– corporates	1	147,245	146,746	78,640	6,291
– total retail		145,790	142,930	17,380	1,390
– *of which:*					
secured by mortgages on immovable property SME		*507*	*1,053*	*150*	*12*
secured by mortgages on immovable property non-SME		*96,123*	*93,700*	*4,837*	*387*
qualifying revolving retail		*22,700*	*22,461*	*4,422*	*354*
other SME		*6,782*	*7,446*	*3,593*	*287*
other non-SME		*19,678*	*18,270*	*4,378*	*350*
IRB securitisation positions		23,517	23,854	16,573	1,326
IRB non-credit obligation assets		6,182	6,971	3,787	303
IRB foundation approach		21,177	20,913	13,059	1,045
– central governments and central banks		10	2	3	—
– institutions		28	28	7	1
– corporates		21,139	20,883	13,049	1,044
Standardised approach		151,440	143,015	33,791	2,704
– central governments and central banks	2	102,394	95,076	1,593	127
– international organisations		2,229	2,048	—	—
– institutions		9,938	10,326	2,630	210
– corporates		27,052	25,503	21,877	1,750
– retail		2,644	3,017	1,910	153
– secured by mortgages on immovable property		3,045	2,894	1,113	89
– exposures in default		924	847	1,203	96
– items associated with particularly high risk		678	695	1,017	81
– securitisation positions		—	—	—	—
– claims in the form of collective investments undertakings		43	42	43	3
– equity	3	1,028	1,029	2,031	164
– other items		1,465	1,538	374	31
At 31 Dec 2016		528,412	518,651	168,936	13,515

For footnotes, see page 19.

Table 8: Credit risk exposure – by region

	Footnotes	United Kingdom £m	Continental Europe £m	Other £m	Total £m
IRB advanced approach		**280,738**	**50,336**	**2,957**	**334,031**
– central governments and central banks		**13,342**	**4,154**	**1,849**	**19,345**
– institutions		**8,978**	**2,147**	**347**	**11,472**
– corporates	1	**123,944**	**24,574**	**761**	**149,279**
– total retail		**134,474**	**19,461**	**—**	**153,935**
– *of which:*					
secured by mortgages on immovable property SME		***21***	***469***	***—***	***490***
secured by mortgages on immovable property non-SME		***99,454***	***2,749***	***—***	***102,203***
qualifying revolving retail		***23,276***	***1***	***—***	***23,277***
other SME		***5,067***	***1,688***	***—***	***6,755***
other non-SME		***6,656***	***14,554***	***—***	***21,210***
IRB securitisation positions		**17,305**	**1,844**	**—**	**19,149**
IRB non-credit obligation assets		**4,939**	**1,051**	**19**	**6,009**
IRB foundation approach		**7,267**	**15,488**	**—**	**22,755**
– central governments and central banks		**—**	**12**	**—**	**12**
– institutions		**7**	**—**	**—**	**7**
– corporates		**7,260**	**15,476**	**—**	**22,736**
Standardised approach		**77,932**	**83,761**	**1,778**	**163,471**
– central governments and central banks	2	**58,122**	**68,611**	**67**	**126,800**
– international organisations		**—**	**1,614**	**—**	**1,614**
– institutions		**6,131**	**569**	**138**	**6,838**
– corporates		**9,413**	**8,635**	**1,399**	**19,447**
– retail		**387**	**646**	**11**	**1,044**
– secured by mortgages on immovable property		**936**	**2,102**	**25**	**3,063**
– exposures in default		**80**	**516**	**135**	**731**
– items associated with particularly high risk		**561**	**302**	**—**	**863**
– securitisation positions		**—**	**194**	**—**	**194**
– claims in the form of CIU		**—**	**30**	**—**	**30**
– equity	3	**750**	**84**	**—**	**834**
– other items		**1,552**	**458**	**3**	**2,013**
At 31 Dec 2017		**388,181**	**152,480**	**4,754**	**545,415**
IRB advanced approach		277,219	44,934	3,943	326,096
– central governments and central banks		16,862	2,923	2,559	22,344
– institutions		8,280	1,810	627	10,717
– corporates	1	124,727	21,761	757	147,245
– total retail		127,350	18,440	—	145,790
– *of which:*					
secured by mortgages on immovable property SME		*9*	*498*	*—*	*507*
secured by mortgages on immovable property non-SME		*93,290*	*2,833*	*—*	*96,123*
qualifying revolving retail		*22,699*	*1*	*—*	*22,700*
other SME		*4,944*	*1,838*	*—*	*6,782*
other non-SME		*6,408*	*13,270*	*—*	*19,678*
IRB securitisation positions		21,185	2,332	—	23,517
IRB non-credit obligation assets		5,136	924	122	6,182
IRB foundation approach		6,691	14,486	—	21,177
– central governments and central banks		—	10	—	10
– institutions		12	16	—	28
– corporates		6,679	14,460	—	21,139
Standardised approach		90,998	55,172	5,270	151,440
– central governments and central banks	2	62,424	39,903	67	102,394
– international organisations		—	2,229	—	2,229
– institutions		9,303	550	85	9,938
– corporates		15,702	7,899	3,451	27,052
– retail		480	1,017	1,147	2,644
– secured by mortgages on immovable property		755	2,019	271	3,045
– exposures in default		110	573	241	924
– items associated with particularly high risk		369	308	1	678
– securitisation positions		—	—	—	—
– claims in the form of CIU		—	43	—	43
– equity	3	845	183	—	1,028
– other items		1,010	448	7	1,465
At 31 Dec 2016		401,229	117,848	9,335	528,412

For footnotes, see page 19.

Table 9: Credit risk exposure – by industry sector

	Footnotes	Personal	Manufacturing	International trade and services	Property and other business activities	Government and public administration	Other commercial	Financial	Non-customer assets	Total
		£m	£m	£m	£m	£m	£m	£m	£m	£m
IRB advanced approach		149,749	24,628	31,531	49,916	21,561	21,324	35,322	–	334,031
– central governments and central banks		–	–	–	–	14,493	–	4,852	–	19,345
– institutions		–	–	–	–	11	–	11,461	–	11,472
– corporates	1	–	24,214	30,315	48,871	6,680	20,243	18,956	–	149,279
– total retail		149,749	414	1,216	1,045	377	1,081	53	–	153,935
– *of which:*										
secured by mortgages on immovable property SME		*14*	*7*	*15*	*439*	*5*	*6*	*4*	–	*490*
secured by mortgages on immovable property non-SME		*102,203*	–	–	–	–	–	–	–	*102,203*
qualifying revolving retail		*23,277*	–	–	–	–	–	–	–	*23,277*
other SME		*3,045*	*407*	*1,201*	*606*	*372*	*1,075*	*49*	–	*6,755*
other non-SME		*21,210*	–	–	–	–	–	–	–	*21,210*
IRB securitisation positions		–	–	–	–	–	–	19,149	–	19,149
IRB non-credit obligation assets		–	–	–	–	–	–	3	6,006	6,009
IRB foundation approach		115	9,377	4,731	3,121	507	2,384	2,520	–	22,755
– central governments and central banks		–	–	–	–	–	–	12	–	12
– institutions		–	–	–	–	–	–	7	–	7
– corporates		115	9,377	4,731	3,121	507	2,384	2,501	–	22,736
Standardised approach		3,901	4,546	3,740	4,151	23,091	1,539	121,182	1,321	163,471
– central governments and central banks	2, 5	–	–	191	–	20,991	–	104,844	774	126,800
– international organisations		–	–	–	–	1,614	–	–	–	1,614
– institutions		–	–	–	–	–	–	6,838	–	6,838
– corporates		98	4,183	3,382	3,348	466	1,492	6,478	–	19,447
– retail		739	2	5	268	12	5	13	–	1,044
– secured by mortgages on immovable property		2,872	–	–	187	–	4	–	–	3,063
– exposures in default		183	162	162	154	6	38	26	–	731
– items associated with particularly high risk		9	–	–	142	–	–	712	–	863
– securitisation positions		–	–	–	–	–	–	194	–	194
– claims in the form of CIU		–	–	–	–	–	–	30	–	30
– equity	3	–	75	–	52	2	–	705	–	834
– other items		–	124	–	–	–	–	1,342	547	2,013
At 31 Dec 2017		153,765	38,551	40,002	57,188	45,159	25,247	178,176	7,327	545,415

Table 9: Credit risk exposure – by industry sector (continued)

	Footnotes	Personal	Manufacturing	International trade and services	Property and other business activities	Government and public administration	Other commercial	Financial	Non-customer assets	Total
		£m	£m	£m	£m	£m	£m	£m	£m	£m
IRB advanced approach		138,501	24,409	30,967	49,478	24,988	23,265	34,488	—	326,096
– central governments and central banks		—	—	—	—	18,761	—	3,583	—	22,344
– institutions		—	—	—	—	1	161	10,555	—	10,717
– corporates	1	—	24,148	30,402	43,439	6,107	22,829	20,320	—	147,245
– total retail		138,501	261	565	6,039	119	275	30	—	145,790
– *of which:*										
secured by mortgages on immovable property SME		—	*7*	*17*	*469*	*4*	*6*	*4*	—	*507*
secured by mortgages on immovable property non-SME		*96,123*	—	—	—	—	—	—	—	*96,123*
qualifying revolving retail		*22,700*	—	—	—	—	—	—	—	*22,700*
other SME		—	*254*	*548*	*5,570*	*115*	*269*	*26*	—	*6,782*
other non-SME		*19,678*	—	—	—	—	—	—	—	*19,678*
IRB securitisation positions		—	—	—	—	—	—	23,517	—	23,517
IRB non-credit obligation assets		—	—	—	—	—	—	—	6,182	6,182
IRB foundation approach		122	8,546	4,783	2,740	398	2,401	2,187	—	21,177
– central governments and central banks		—	—	—	—	—	—	10	—	10
– institutions		—	—	—	—	—	—	28	—	28
– corporates		122	8,546	4,783	2,740	398	2,401	2,149	—	21,139
Standardised approach		5,395	6,501	3,782	4,140	43,348	3,712	84,562	—	151,440
– central governments and central banks	2	—	—	115	—	40,471	18	61,790	—	102,394
– international organisations		—	—	—	—	2,229	—	—	—	2,229
– institutions		—	—	—	—	—	—	9,938	—	9,938
– corporates		269	6,084	3,562	3,206	594	3,408	9,929	—	27,052
– retail		1,969	28	20	534	16	19	58	—	2,644
– secured by mortgages on immovable property		2,968	9	12	—	—	56	—	—	3,045
– exposures in default		189	263	73	113	38	210	38	—	924
– items associated with particularly high risk		—	—	—	175	—	1	502	—	678
– securitisation positions		—	—	—	—	—	—	—	—	—
– claims in the form of CIU		—	—	—	—	—	—	43	—	43
– equity	3	—	12	—	112	—	—	904	—	1,028
– other items		—	105	—	—	—	—	1,360	—	1,465
At 31 Dec 2016		144,018	39,456	39,532	56,358	68,734	29,378	144,754	6,182	528,412

For footnotes, see page 19.

Table 10: Credit risk exposure – by maturity

	Footnotes	Less than 1 year	Between 1 and 5 years	More than 5 years	Undated	Total
		£m	£m	£m	£m	£m
IRB advanced approach		**94,788**	**104,296**	**134,947**	**—**	**334,031**
– central governments and central banks		**7,834**	**8,178**	**3,333**	**—**	**19,345**
– institutions		**5,963**	**4,849**	**660**	**—**	**11,472**
– corporates	1	**54,972**	**77,062**	**17,245**	**—**	**149,279**
– total retail		**26,019**	**14,207**	**113,709**	**—**	**153,935**
– *of which:*						
secured by mortgages on immovable property SME		***21***	***99***	***370***	**—**	***490***
secured by mortgages on immovable property non-SME		***744***	***2,336***	***99,123***	**—**	***102,203***
qualifying revolving retail		***23,277***	**—**	**—**	**—**	***23,277***
other SME		***1,365***	***3,919***	***1,471***	**—**	***6,755***
other non-SME		***612***	***7,853***	***12,745***	**—**	***21,210***
IRB securitisation positions		**7,735**	**5,225**	**6,189**	**—**	**19,149**
IRB non-credit obligation assets		**—**	**47**	**6**	**5,956**	**6,009**
IRB foundation approach		**8,767**	**12,219**	**1,769**	**—**	**22,755**
– central governments and central banks		**—**	**—**	**12**	**—**	**12**
– institutions		**—**	**7**	**—**	**—**	**7**
– corporates		**8,767**	**12,212**	**1,757**	**—**	**22,736**
Standardised approach		**114,936**	**30,031**	**14,747**	**3,757**	**163,471**
– central governments and central banks	2,5	**95,951**	**21,153**	**8,922**	**774**	**126,800**
– international organisations		**295**	**956**	**363**	**—**	**1,614**
– institutions		**5,693**	**250**	**895**	**—**	**6,838**
– corporates		**12,450**	**5,652**	**1,345**	**—**	**19,447**
– retail		**134**	**740**	**170**	**—**	**1,044**
– secured by mortgages on immovable property		**96**	**384**	**2,583**	**—**	**3,063**
– exposures in default		**216**	**397**	**118**	**—**	**731**
– items associated with particularly high risk		**101**	**478**	**157**	**127**	**863**
– securitisation positions		**—**	**—**	**194**	**—**	**194**
– claims in the form of CIU		**—**	**—**	**—**	**30**	**30**
– equity	3	**—**	**2**	**—**	**832**	**834**
– other items		**—**	**19**	**—**	**1,994**	**2,013**
At 31 Dec 2017		**226,226**	**151,818**	**157,658**	**9,713**	**545,415**
IRB advanced approach		108,088	88,815	129,193	—	326,096
– central governments and central banks		6,988	9,739	5,617	—	22,344
– institutions		7,099	3,126	492	—	10,717
– corporates	1	67,280	63,395	16,570	—	147,245
– total retail		26,721	12,555	106,514	—	145,790
– *of which:*						
secured by mortgages on immovable property SME		*14*	*86*	*407*	—	*507*
secured by mortgages on immovable property non-SME		*1,148*	*1,847*	*93,128*	—	*96,123*
qualifying revolving retail		*22,700*	—	—	—	*22,700*
other SME		*1,513*	*3,901*	*1,368*	—	*6,782*
other non-SME		*1,346*	*6,721*	*11,611*	—	*19,678*
IRB securitisation positions		6,056	5,282	12,179	—	23,517
IRB non-credit obligation assets		91	35	4	6,052	6,182
IRB foundation approach		9,313	10,623	1,241	—	21,177
– central governments and central banks		—	—	10	—	10
– institutions		16	12	—	—	28
– corporates		9,297	10,611	1,231	—	21,139
Standardised approach		96,284	33,081	19,407	2,668	151,440
– central governments and central banks	2	65,610	23,523	13,261	—	102,394
– international organisations		331	1,639	259	—	2,229
– institutions		8,150	80	1,708	—	9,938
– corporates		20,229	5,510	1,313	—	27,052
– retail		1,118	1,293	233	—	2,644
– secured by mortgages on immovable property		77	545	2,423	—	3,045
– exposures in default		435	318	171	—	924
– items associated with particularly high risk		228	131	39	280	678
– securitisation positions		—	—	—	—	—
– claims in the form of CIU		—	—	—	43	43
– equity	3	—	—	—	1,028	1,028
– other items		106	42	—	1,317	1,465
At 31 Dec 2016		219,832	137,836	162,024	8,720	528,412

1 *'Corporates' includes specialised lending exposures subject to supervisory slotting approach of £14,374m (2016: £13,650m) and RWAs of £9,401m (2016: £9,202m).*
2 *'Central governments and central banks' under the standardised approach includes exposures to regional governments and public sector entities.*
3 *'Equity' includes investment in insurance companies that are risk weighted at 250%.*
4 *'Average exposures' are calculated by aggregating exposure value of the last five quarters and dividing by five.*
5 *Current period deferred tax assets are reported in 'Non-customer assets' column in Table 9 and in 'Undated' column in Table 10.*

Table 11: Wholesale IRB exposures under the slotting approach

	Exposure	
	2017	2016
	£m	£m
Supervisory Category		
Category 1 – Strong	**10,588**	8,948
Category 2 – Good	**2,359**	2,721
Category 3 – Satisfactory	**603**	823
Category 4 – Weak	**139**	229
Category 5 – Default	**685**	929
At 31 Dec	**14,374**	13,650

Past due but not impaired exposures, impaired exposures and credit risk adjustments ('CRA')

We analyse past due but not impaired, impaired exposures and impairment allowances, and other credit risk provisions using accounting values on a regulatory consolidation basis.

Our approach for determining impairment allowances is explained on pages 28 and 71 of the HSBC Bank plc Annual Report and Accounts 2017, *and HSBC's definitions for accounting purposes of 'past due' and 'impaired' are set out on page 40.*

Under the accounting standards currently adopted by HSBC, impairment allowances, value adjustments and credit-related provisions for off-balance sheet amounts are treated as specific CRAs.

Table 12: Amount of impaired exposures and related allowances by industry sector and geographical region

	United Kingdom	Continental Europe	Other	Total
	£m	£m	£m	£m
At 31 Dec 2017				
Past due but not impaired exposures	**608**	**363**	**6**	**977**
– personal	**491**	**116**	**—**	**607**
– corporate and commercial	**114**	**240**	**1**	**355**
– financial	**3**	**7**	**5**	**15**
Impaired exposures	**4,612**	**1,598**	**148**	**6,358**
– personal	**1,051**	**405**	**2**	**1,458**
– corporate and commercial	**2,885**	**1,191**	**146**	**4,222**
– financial	**676**	**2**	**—**	**678**
Impairment allowances and other credit risk provisions	**(1,485)**	**(791)**	**(20)**	**(2,296)**
– personal	**(297)**	**(138)**	**(2)**	**(437)**
– corporate and commercial	**(1,055)**	**(652)**	**(18)**	**(1,725)**
– financial	**(133)**	**(1)**	**—**	**(134)**
At 31 Dec 2016				
Past due but not impaired exposures	580	385	216	1,181
– personal	453	168	177	798
– corporate and commercial	124	210	34	368
– financial	3	7	5	15
Impaired exposures	5,306	1,882	462	7,650
– personal	1,105	402	232	1,739
– corporate and commercial	3,213	1,409	230	4,852
– financial	988	71	—	1,059
Impairment allowances and other credit risk provisions	(1,307)	(973)	(330)	(2,610)
– personal	(285)	(136)	(237)	(658)
– corporate and commercial	(913)	(769)	(93)	(1,775)
– financial	(109)	(68)	—	(177)

Table 13: Movement in specific credit risk adjustments by industry sector and by geographical region

	Footnotes	United Kingdom £m	Continental Europe £m	Other £m	Total £m
Specific credit risk adjustments at 1 Jan 2017		**1,307**	**973**	**330**	**2,610**
Amounts written off		**(581)**	**(300)**	**(30)**	**(911)**
– personal		**(328)**	**(13)**	**—**	**(341)**
– corporate and commercial		**(235)**	**(247)**	**(30)**	**(512)**
– financial		**(18)**	**(40)**	**—**	**(58)**
Recoveries of amounts written off in previous years		**254**	**5**	**—**	**259**
– personal		**229**	**1**	**—**	**230**
– corporate and commercial		**24**	**4**	**—**	**28**
– financial		**1**	**—**	**—**	**1**
Charge to income statement		**494**	**104**	**34**	**632**
– personal		**100**	**12**	**10**	**122**
– corporate and commercial		**343**	**94**	**24**	**461**
– financial		**51**	**(2)**	**—**	**49**
Exchange and other movements		**11**	**9**	**(314)**	**(294)**
Specific credit risk adjustments at 31 Dec 2017		**1,485**	**791**	**20**	**2,296**
Specific credit risk adjustments at 1 Jan 2016		1,500	856	275	2,631
Amounts written off		(683)	(143)	(82)	(908)
– personal		(284)	(19)	(44)	(347)
– corporate and commercial		(398)	(124)	(38)	(560)
– financial		(1)	—	—	(1)
Recoveries of amounts written off in previous years	1	188	5	5	198
– personal		165	1	5	171
– corporate and commercial		22	4	—	26
– financial		1	—	—	1
Charge to income statement	1	239	122	132	493
– personal		90	22	81	193
– corporate and commercial		155	69	51	275
– financial		(6)	31	—	25
Exchange and other movements		63	133	—	196
Specific credit risk adjustments at 31 Dec 2016		1,307	973	330	2,610

1 *The prior period comparison for 'Recoveries of amounts written off in previous years' and 'Charge to income statement' has been restated.*

Expected loss ('EL') and credit risk adjustments

We analyse credit loss experience in order to assess the performance of our risk measurement and control processes. Through this analysis we are able to understand changes occurring in the risk profile of our exposures and the implications of these changes for risk and capital management.

When comparing EL with measures of credit losses under IFRS, it is necessary to take into account differences in the definition and scope of each. Below are examples of matters that can give rise to material differences in the way economic, business and methodological drivers are reflected quantitatively in the accounting and regulatory measures of loss.

In 2018 IFRS 9 changes the way credit losses are measured for accounting purposes. IFRS 9 is conceptually more aligned with the IRB measurement of expected loss and uses similar building blocks such as Probability of Default, Loss Given Default and expected loss. Significant differences between regulatory and accounting measures of expected loss will continue under IFRS 9 due to factors such as: the removal of regulatory conservatism and supervisory set parameters under IFRS, point in time and forward - looking measurements under IFRS compared to through the cycle measures under regulatory, 12 month expected losses under regulatory versus lifetime expected losses under IFRS.

Tables 14 and 15 set out, for IRB credit exposures, the EL, CRA balances and the actual loss experience reflected in the charges for CRAs.

CRA balances represent management's best estimate of losses incurred in the loan portfolios at the balance sheet date. Charges for CRAs represent a movement in the CRA balance during the year, reflecting loss events that occurred during the financial year and changes in estimates of losses arising on events that occurred prior to the current year. EL represents the one-year regulatory expected loss accumulated in the book at the balance sheet date.

Examples of differences in definition and scope between EL and CRA balances:

- Under IAS 39, our estimates of loss in impairment allowances are required to reflect the current circumstances and specific cash flow expectations of a customer. EL is based on modelled estimates and, although the estimates may be individually assigned to specific exposures, the statistical nature of these models means that they are influenced by the behaviour of the overall portfolio;
- EL is based on exposure values that incorporate expected future drawings of committed credit lines, while CRAs are recognised in respect of financial assets recognised on the balance sheet and in respect of committed credit lines where a loss is probable;
- EL is generally based on through-the-cycle ('TTC') estimates of PD over a one-year future horizon, determined via statistical analysis of historical default experience. CRAs are recognised for losses that have been incurred at the balance sheet date;
- in the majority of cases, EL is based on economic downturn estimates of LGD, while CRAs are measured using estimated future cash flows at the balance sheet date;
- EL incorporates LGD, which may discount recoveries at a different rate from the effective interest rate employed in discounted cash flow analysis for CRAs;
- LGDs typically include all costs associated with recovery, whereas the accounting measurement considers only the costs of obtaining and selling collateral;
- in the foundation IRB approach, LGD and the conversion factors used to calculate EAD are set by regulations, and may differ significantly from the accounting assumptions about estimated cash flows;
- for EL, certain exposures are subject to regulatory minimum thresholds for one or more parameters, whereas credit losses under IFRSs are determined using management's judgement about estimated future cash flows; and
- in the case of EL, to meet regulatory prudential standards, HSBC's model philosophy favours the incorporation of conservative estimation to accommodate uncertainty; for instance, where modelling portfolios with limited data. Under IFRSs, uncertainty is considered when forming management's estimates of future cash flows, using balanced and neutral judgement.

Table 14: IRB expected loss and CRA – by exposure class

		CRA[1]	
	Expected loss[1]	Balances	Charge for the year
	£m	£m	£m
IRB exposure classes			
Central governments and central banks	4	1	–
Institutions	10	1	1
Corporates	1,820	1,385	463
Retail	948	602	132
– secured by mortgages on immovable property SME	8	3	–
– secured by mortgages on immovable property non-SME	117	157	20
– qualifying revolving retail	235	116	98
– other SME	391	205	5
– other non-SME	197	121	9
At 31 Dec 2017	2,782	1,989	596

Table 14: IRB expected loss and CRA – by exposure class (continued)

	Expected loss[1]	CRA[1] Balances	CRA[1] Charge for the year
	£m	£m	£m
IRB exposure classes			
Central governments and central banks	6	1	–
Institutions	10	1	–
Corporates	1,915	1,191	178
Retail	931	592	99
– secured by mortgages on immovable property SME	9	3	–
– secured by mortgages on immovable property non-SME	117	146	(16)
– qualifying revolving retail	205	99	63
– other SME	441	226	8
– other non-SME	159	118	44
At 31 Dec 2016	2,862	1,785	277

Table 15: IRB expected loss and CRA – by region

	Expected loss[1]	**CRA[1] Balances**	**CRA[1] Charge for the year**
	£m	**£m**	**£m**
United Kingdom	**2,114**	**1,452**	**505**
Continental Europe	**664**	**537**	**91**
Other	**4**	**–**	**–**
At 31 Dec 2017	**2,782**	**1,989**	**596**
United Kingdom	2,172	1,207	223
Continental Europe	685	578	54
Other	5	–	–
At 31 Dec 2016	2,862	1,785	277

1 *Excludes securitisation exposures because EL is not calculated for this exposure class.*

Risk mitigation

Mitigation of credit risk is a key aspect of effective risk management. Specific, detailed policies cover the acceptability, structuring and terms of various types of business with regard to the availability of credit risk mitigation; for example in the form of collateral security. These policies, together with the setting of suitable valuation parameters, are subject to regular review to ensure that they are supported by empirical evidence and continue to fulfil their intended purpose.

Collateral

The most common method of mitigating credit risk is to take collateral. In our retail residential and commercial real estate ('CRE') businesses, a mortgage over the property is usually taken to help secure claims. Physical collateral is also taken in various forms of specialised lending and leasing transactions where income from the physical assets that are financed is also the principal source of facility repayment. In the commercial and industrial sectors, charges are created over business assets such as premises, stock and debtors. Loans to private banking clients may be made against a pledge of eligible marketable securities, cash or real estate.

Further information regarding charges held over residential and commercial property is provided on pages 92 and 97 of the HSBC Holdings plc Annual Report and Accounts 2017.

Financial collateral

In the institutional sector, trading facilities are supported by charges over financial instruments such, as cash, debt securities and equities. Financial collateral in the form of marketable securities is used in much of the group's over-the-counter ('OTC') derivatives activities, and in SFTs such as repos, reverse repos, securities lending and borrowing. Netting is used extensively and is a prominent feature of market standard documentation.

In the non-trading book, we provide customers with working capital management products. Some of these products have loans and advances to customers and customer accounts where we have rights of offset, and comply with the regulatory requirements for on-balance sheet netting. Under on-balance sheet netting, the customer accounts are treated as cash collateral and the effects of this collateral are incorporated in our LGD estimates. For risk management purposes, the net exposures are subject to limits that are monitored, and the relevant customer agreements are subject to review and update, as necessary, to ensure the legal right of offset remains appropriate.

Other forms of Credit Risk Mitigation

Facilities to SMEs are commonly granted against guarantees given by their owners and/or directors. Guarantees may be taken from third parties where the group extends facilities without the benefit of any alternative form of security, e.g. where it issues a bid or performance bond in favour of a non-customer at the request of another bank.

Our GB&M business utilises credit risk mitigation to manage the credit risk of its portfolios, with the goal of reducing concentrations in individual names, sectors or portfolios. The techniques in use include credit default swap ('CDS') purchases, structured credit notes and securitisation structures. Buying credit protection creates credit exposure against the protection provider, which is monitored as part of the overall credit exposure to them. Where applicable, the transaction is entered into directly with a central clearing house counterparty, otherwise our exposure to CDS protection providers is diversified among mainly banking counterparties with strong credit ratings.

In our corporate lending, we also take guarantees from corporates and Export Credit Agencies. Corporates normally provide guarantees as part of a parent/subsidiary or common parent relationship and span a number of credit grades. Export Credit Agencies will normally be investment grade.

Policy and procedures

Policies and procedures govern the protection of our position from the outset of a customer relationship; for instance, in requiring standard terms and conditions or specifically agreed

documentation permitting the offset of credit balances against debt obligations, and through controls over the integrity, current valuation and, if necessary, realisation of collateral security.

Valuing collateral

Valuation strategies are established to monitor collateral mitigants to ensure that they continue to provide the anticipated secure secondary repayment source. Market trading activities, such as collateralised OTC derivatives and SFTs, typically include daily valuations in support of margining arrangements. In the residential mortgage business, HSBC policy prescribes revaluation at intervals of up to three years, or more frequently where market conditions are subject to significant change. Residential property collateral values are determined through a combination of professional appraisals, house price indices or statistical analysis.

Local market conditions determine the frequency of valuation for CRE. Revaluations are sought where, for example, as part of the regular credit assessment of the obligor, material concerns arise in relation to the performance of the collateral. CRE revaluation also commonly occurs where a decline in the obligor's credit quality gives cause for concern that the principal payment source may not fully meet the obligation.

Recognition of risk mitigation under the IRB approach

Within an IRB approach, risk mitigants are considered in two broad categories: first, those that reduce the intrinsic PD of an obligor; and second, those that affect the estimated recoverability of obligations and thus LGD.

The first typically include full parental guarantees – where one obligor within a group of companies guarantees another. This is usually factored into the estimate of the latter's PD, as it is expected that the guarantor will intervene to prevent a default. PD estimates are also subject to a 'sovereign ceiling', constraining the risk ratings assigned to obligors in higher risk countries if only partial parental support exists. In certain jurisdictions, typically those on the Foundation IRB approach, certain types of third-party guarantee are also recognised through substitution of the obligor's PD by the guarantor's PD.

In the second category, LGD estimates are affected by a wider range of collateral, including cash, charges over real estate property, fixed assets, trade goods, receivables and floating charges such as mortgage debentures. Unfunded mitigants, such as third-party guarantees, are also taken into consideration in LGD estimates where there is evidence that they reduce loss expectation.

The main providers of guarantees are banks, other financial institutions and corporates, the latter typically in support of subsidiaries of their company group. Across HSBC, the nature of such customers and transactions is very diverse and the creditworthiness of guarantors accordingly spans a wide spectrum. The creditworthiness of providers of unfunded credit risk mitigation is taken into consideration as part of the guarantor's risk profile when; for example, assessing the risk of other exposures such as direct lending to the guarantor. Internal limits for such contingent exposure are approved in the same way as direct exposures.

EAD and LGD values, in the case of individually assessed exposures, are determined by reference to regionally approved internal risk parameters based on the nature of the exposure. For retail portfolios, credit risk mitigation data is incorporated into the internal risk parameters for exposures and feeds into the calculation of the EL band value summarising both customer delinquency and product or facility risk. Credit and credit risk mitigation data form inputs submitted by all HSBC offices to centralised databases. A range of collateral recognition approaches are applied to IRB capital treatments:

- unfunded protection, which includes credit derivatives and guarantees, is reflected through adjustment or determination of PD or LGD;
- eligible financial collateral is taken into account in LGD models (under Advanced IRB) or by adjusting regulatory LGD values (under Foundation IRB). The adjustment to LGD for the latter is based on the degree to which the exposure value would be adjusted if the Financial Collateral Comprehensive Method ('FCCM') were applied; and
- for all other types of collateral, including real estate, the LGD for exposures calculated under the IRB advanced approach is calculated by models. For IRB foundation, base regulatory LGDs are adjusted depending on the value and type of the asset taken as collateral relative to the exposure. The types of eligible mitigant recognised under the IRB foundation approach are more limited.

Table 16 below sets out, for IRB exposures, the exposure value and the effective value of credit risk mitigation expressed as the exposure value covered by the credit risk mitigant.

Recognition of risk mitigation under the standardised approach

Where credit risk mitigation is available in the form of an eligible guarantee, non-financial collateral or credit derivatives, the exposure is divided into covered and uncovered portions. The covered portion, which is determined after applying an appropriate 'haircut' for currency and maturity mismatches (and for omission of restructuring clauses for credit derivatives, where appropriate) to the amount of the protection provided, attracts the risk weight of the protection provider. The uncovered portion attracts the risk weight of the obligor. For exposures fully or partially covered by eligible financial collateral, the value of the exposure is adjusted under the financial collateral comprehensive method using supervisory volatility adjustments, including those arising from currency mismatch, which are determined by the specific type of collateral (and, in the case of eligible debt securities, their credit quality) and its liquidation period. The adjusted exposure value is subject to the risk weight of the obligor.

Table 17 sets out the credit risk mitigation for exposures under the standardised approach, expressed as the exposure value covered by the credit risk mitigant.

Table 16: IRB exposure – credit risk mitigation

	2017			2016		
	Exposure value covered by eligible financial and other collateral	**Exposure value covered by credit derivatives or guarantees**	**Total exposure value**	Exposure value covered by eligible financial and other collateral	Exposure value covered by credit derivatives or guarantees	Total exposure value
	£m	**£m**	**£m**	£m	£m	£m
Exposures under the IRB advanced approach		**24,510**	**24,510**		15,002	15,002
– central governments and central banks		**553**	**553**		43	43
– institutions		**1**	**1**		1	1
– corporates		**11,952**	**11,952**		4,450	4,450
– retail		**12,004**	**12,004**		10,508	10,508
Exposures under the IRB foundation approach	**603**	**1,265**	**1,868**	344	403	747
– Institutions	**—**	**—**	**—**	—	—	—
– Corporates	**603**	**1,265**	**1,868**	344	403	747
At 31 Dec	**603**	**25,775**	**26,378**	344	15,405	15,749

Table 17: Standardised exposure – credit risk mitigation

	2017			2016		
	Exposure value covered by eligible financial and other collateral	**Exposure value covered by credit derivatives or guarantees**	**Total exposure value**	Exposure value covered by eligible financial and other collateral	Exposure value covered by credit derivatives or guarantees	Total Exposure value
	£m	**£m**	**£m**	£m	£m	£m
Exposures under the standardised approach						
Central governments and central banks	**217**	**637**	**854**	108	424	532
Institutions	**—**	**—**	**—**	—	—	—
Corporates	**850**	**2,637**	**3,487**	2,428	1,191	3,619
Retail	**319**	**825**	**1,144**	1,276	—	1,276
Secured by mortgages on immovable property	**106**	**10**	**116**	7	—	7
Exposures in default	**16**	**13**	**29**	106	—	106
Items associated with particularly high risk	**8**	**—**	**8**	49	—	49
At 31 Dec	**1,516**	**4,122**	**5,638**	3,974	1,615	5,589

Counterparty credit risk

Overview

Counterparty credit risk is the risk that the counterparty to a transaction may default before completing the satisfactory settlement of the transaction. It arises on derivatives, securities financing transactions and exposures to central counterparties ('CCP') in both the trading and non-trading books.

The table below sets out details of the group's counterparty credit risk exposures by exposure class and approach. Further explanation of the group's approach to managing counterparty credit risk can be found:

- on page 47 of the HSBC Bank plc *Annual Report and Accounts 2017*;
- on page 94 of the HSBC Holdings plc *Annual Report and Accounts 2017*; and
- on pages 50 to 53 of the HSBC Holdings plc *Pillar 3 Disclosures 2017*.

Table 18: Counterparty credit risk – RWAs by exposure class and product

		2017		2016	
		RWAs	**Capital required**	RWAs	Capital required
	Footnotes	**£m**	**£m**	£m	£m
By exposure class					
IRB advanced approach		**15,680**	**1,254**	17,280	1,382
– central governments and central banks		**539**	**43**	773	62
– institutions		**5,218**	**417**	6,534	523
– corporates		**9,923**	**794**	9,973	797
IRB foundation approach		**1,245**	**100**	1,361	109
– corporates		**1,245**	**100**	1,361	109
Standardised approach		**3,237**	**259**	3,585	287
– central governments and central banks		**—**	**—**	—	—
– institutions		**2,820**	**226**	2,895	232
– corporates		**417**	**33**	690	55
CVA advanced		**2,294**	**184**	3,318	265
CVA standardised		**1,083**	**86**	2,492	199
CCP standardised		**479**	**38**	557	45
By product					
– derivatives (OTC and Exchange traded derivatives)		**14,842**	**1,187**	17,134	1,370
– SFTs		**4,333**	**347**	4,035	323
– other	1	**1,215**	**97**	1,269	102
– CVA advanced		**2,294**	**184**	3,318	265
– CVA standardised		**1,083**	**86**	2,492	199
– CCP default funds	2	**251**	**20**	345	28
At 31 Dec		**24,018**	**1,921**	28,593	2,287

1 *Includes free deliveries not deducted from regulatory capital.*
2 *Default fund contributions are cash balances posted to CCPs by all members. These cash balances are not included in the total reported exposure.*

Market risk

Overview

Market risk is the risk that movements in market risk factors, including foreign exchange rates, commodity prices, interest rates, credit spreads and equity prices, will reduce the group's income or the value of its portfolios. Market risk is measured using internal market risk models where approved by the PRA, PRA approved local VaR models or the standardised approach for position risk under CRD IV.

The table below sets out details of the bank's market risk exposures by type and approach.

Further explanation of the group's approach to managing market risk can be found:

- on pages 50 and 52 of the HSBC Bank plc *Annual Report and Accounts 2017*;
- on pages 105 to 111 of the HSBC Holdings plc *Annual Report and Accounts 2017*; and
- on pages 56 to 61 of the HSBC Holdings plc *Pillar 3 Disclosures 2017*.

Table 19: Market risk – RWA and capital required

		2017		2016	
		RWAs	**Capital required**	RWAs	Capital required
	Footnotes	**£m**	**£m**	£m	£m
Internal model based	*1*	**18,962**	**1,517**	21,745	1,740
– VaR		**4,880**	**390**	6,010	481
– stressed VaR		**8,559**	**685**	10,831	867
– incremental risk charge		**4,878**	**390**	3,538	283
– other		**645**	**52**	1,366	109
Standardised approach	*2*	**2,016**	**161**	3,230	258
– interest rate position risk		**673**	**54**	804	63
– equity position risk		**—**	**—**	1,307	105
– commodity position risk		**51**	**4**	8	1
– securitisations		**1,292**	**103**	1,111	89
At 31 Dec		**20,978**	**1,678**	24,975	1,998

1 *The breakdown of internal model based RWAs have been revised to group together all VaR and SVaR calculations including amounts which are aggregated rather than consolidated. The prior period comparison has been restated for consistency.*
2 *RWAs for products and sites that are not in the scope of the approved model permissions from the regulator are calculated using the Standardised approach specified in CRD IV.*

Operational risk

Overview

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

Operational risk is relevant to every aspect of our business. It covers a wide spectrum of issues, in particular legal, compliance, security and fraud. Losses arising from breaches of regulation and law, unauthorised activities, error, omission, inefficiency, fraud, systems failure or external events all fall within the definition of operational risk.

We have historically experienced operational risk losses in the following major categories:

- mis-selling of payment protection insurance;
- external criminal activities, including fraud;
- breakdowns in processes/procedures due to human error, misjudgement or malice;
- system failure or non-availability; and
- breach of regulatory and/or legislative requirements.

Further explanation of the group's approach to managing operational risk can be found:

- on page 32 of the HSBC Bank plc *Annual Report and Accounts 2017*;
- on page 77 of the HSBC Holdings plc *Annual Report and Accounts 2017*; and
- on pages 61 to 62 of the HSBC Holdings plc *Pillar 3 Disclosures 2017*.

Table 20: Operational risk RWA

	2017		2016	
	RWAs	Capital required	RWAs	Capital required
	£m	£m	£m	£m
Own funds requirement for operational risk	23,310	1,865	22,733	1,819

Other risks

Interest rate risk in the banking book

The Interest Rate Risk in the Banking Book ('IRRBB') arises from timing mismatches in the repricing of non-traded assets and liabilities and is the potential adverse impact of changes in interest rates on earnings and capital. The component of IRRBB that can be economically neutralised in the market is transferred to the BSM to manage, in accordance with internal transfer pricing rules. In its management of IRRBB, the group aims to balance mitigating the effect of future interest rate movements which could reduce net interest income against the cost of hedging. The monitoring of the projected net interest income and economic value of equity ('EVE') sensitivity under varying interest rate scenarios is a key part of this.

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

Further details on our IRRBB may be found on page 31 of the HSBC Bank plc Annual Report and Accounts 2017.

Pension risk

We operate a number of pension plans throughout Europe for our employees. Our plans are either defined benefit or defined contribution plans, which expose the Group to different types of risks. We have a global pension risk management framework, and accompanying global policies on the management of these risks, which is overseen at the European level by the European Pensions Oversight Forum.

Details of our management of pension risk can be found in 'Pension risk management' on page 35 of the HSBC Bank plc Annual Report and Accounts 2017.

Risk management of insurance operations

We operate an integrated bancassurance model which provides insurance products principally for customers with whom we have a banking relationship. Insurance products are sold through all global businesses, but predominantly by RBWM and CMB through our branches and direct channels worldwide.

The insurance contracts we sell relate to the underlying needs of our banking customers, which we can identify from our point-of-sale contacts and customer knowledge. The majority of sales are of savings and investment products and term and credit life contracts. By focusing largely on personal and SME lines of business we are able to optimise volumes and diversify individual insurance risks.

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

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

We distribute insurance products in all of our geographical regions. We have life insurance manufacturing subsidiaries in nine countries including the UK.

We measure the risk profile of our insurance manufacturing businesses using an economic capital approach, where assets and liabilities are measured on a market value basis and a capital requirement is held to ensure that there is less than a one in 200 chance of insolvency over the next year, given the risks that the businesses are exposed to. The methodology for the economic capital calculation is largely aligned to the new pan-European Solvency II insurance capital regulations, which are applicable from 2016.

Subsidiaries engaged in insurance activities are excluded from the regulatory consolidation by excluding assets, liabilities and post-acquisition reserves, leaving the investment of these insurance subsidiaries to be recorded at cost and deducted from CET1 subject to thresholds (amounts below the thresholds are risk-weighted).

Further details of the management of financial risks and insurance risk arising from the insurance operations are provided from page 34 of the HSBC Bank plc Annual Report and Accounts 2017.

Liquidity and funding risk

Strategies and processes in the management of liquidity risk

HSBC 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. The management of liquidity and funding is primarily undertaken locally in compliance with the Group's LFRF, and with practices and limits set by the GMB through the RMM and approved by the Board. The group's policy is that it should be self-sufficient in funding its own activities.

Structure and organisation of the liquidity risk management function

The Group Treasurer, who reports to the Group CFO, has responsibility for the oversight of the LFRF. Asset, Liability and Capital Management ('ALCM') team are responsible for the application of the LFRF with HBEU.

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

- Asset and liability management committees ('ALCOs'); and
- Annual individual liquidity adequacy assessment process ('ILAAP') used to validate risk tolerance and set risk appetite.

Group Treasury/Asset, Liability & Capital Management ('ALCM')

The Group Treasury team is responsible for setting the Group's policy, proposing risk tolerance and providing review and challenge of the operating entities implementation. Regional and local ALCM teams are responsible for the implementation of group-wide and local regulatory policy at a legal entity level.

Balance Sheet Management

Along with the Group's Global Business Lines, Balance Sheet Management ('BSM') teams form the first line of defence in the management of liquidity risk, ensuring continuous compliance with the firm's risk appetite operating within their risk mandates.

Hedging and mitigating liquidity risk at HSBC Group

Management of liquidity and funding risk

Liquidity coverage ratio

The Liquidity Coverage Ratio ('LCR') aims to ensure that a bank has sufficient unencumbered high-quality liquid assets ('HQLA') to meet its liquidity needs in a 30 calendar day liquidity stress scenario. For the calculation of the LCR, HSBC follows the guidelines set by the European Commission.

The calculation of the LCR metric, involves an assumption on operational deposits. Operational deposits are principally defined as transactional accounts arising from the provision of custody services by HSBC Security Services or Global Liquidity and Cash Management. To make an assessment of operational deposits both the balance history as well as the values of debits and credits over an account over a period time are referenced.

Net stable funding ratio

HSBC uses the NSFR as a basis for establishing stable funding within 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).

Liquid assets

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

The liquid asset buffer may also include securities in held-to maturity portfolios. To qualify as part of the liquid asset buffer, held-to-maturity portfolios must have a deep and liquid repo market in the underlying security.

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.

Overall adequacy of liquidity risk management

All operating entities are required to manage liquidity risk and funding risks on a stand-alone basis in accordance with the LFRF, which includes the preparation of an Individual Liquidity Adequacy Assessment ('ILAA') document, to ensure that:

- liquidity resources are adequate, both as to the amount and quality;
- there is no significant risk that liabilities cannot be met as they fall due;
- a prudent structural funding profile is maintained;
- adequate liquidity resources continue to be maintained; and
- that the operating entity's liquidity risk framework is adequate and robust.

The two key objectives of the ILAA process are to:

1. demonstrate that all material liquidity and funding risks are captured within the internal framework; and
2. validate the operating entity's risk tolerance/appetite by demonstrating that reverse stress testing scenarios are acceptably remote; and vulnerabilities have been assessed through the use of severe stress scenarios.

The final conclusion of the ILAA, approved by the Board of Directors, is that each operating entity:

- maintains liquidity resources which are adequate in both amount and quality at all times, and ensures that
- there is no significant risk that its liabilities cannot be met as they fall due; and
- ensures its liquidity resources contain an adequate amount of high quality liquid assets ('HQLA') and maintains a prudent funding profile.

Liquidity stress testing

The group undertakes liquidity stress testing to test that its risk appetite is correct, to validate that it can continue to operate under various stress scenarios and to test whether the stress assumptions within the LCR scenario are appropriate and conservative enough for the group's business. The group also conducts reverse stress testing with the specific aim of reviewing the remoteness of the scenarios that would lead the group to exhaust its liquidity resources. If the scenarios are not deemed remote enough, then corrective action is taken.

Several different stress testing scenarios are run that test the quality of liquidity resources under stresses of varying durations and nature. As part of this exercise, various assumptions are used which are approved by the relevant ALCO and Board and the results of the stress testing are presented through the ILAAP to the Board and on a quarterly basis to the relevant ALCO.

Liquidity management across the group

The structure of the group means that liquidity and funding risk cannot practically be managed on a consolidated group basis and can only be managed by entity on a stand-alone basis. The group's liquidity and funding risk framework requires all operating entities to manage liquidity and funding risk on a stand-alone basis in accordance with the Group's liquidity and funding risk management framework and the liquidity and funding risk tolerances set out in the Risk Appetite Statement.

The group's internal liquidity and funding risk management framework does not therefore seek to manage liquidity and funding risk on a consolidated basis, other than to ensure that the position of the consolidated group meets the minimum regulatory requirements.

HSBC Group's business strategy and overall liquidity risk profile

The key aspects of the LFRF are:

- stand-alone management of liquidity and funding by operating entity;
- operating entity classification by inherent liquidity risk ('ILR') categorisation;
- minimum LCR requirement depending on ILR categorisation;
- minimum NSFR requirement depending on ILR categorisation;
- 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 entity;
- minimum LCR requirement by currency;
- intra-day liquidity;
- liquidity funds transfer pricing; and
- forward-looking funding assessments.

The internal LFRF and the risk tolerance limits were approved by the RMM and the Board on the basis of recommendations made by the Group Risk Committee.

Structural foreign exchange exposures

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

The group's structural foreign exchange exposures are managed with the primary objective of ensuring, where practical, that the group's consolidated capital ratios and the capital ratios of individual banking subsidiaries are largely protected from the effect of changes in exchange rates. This is usually achieved by ensuring that, for each subsidiary bank, the ratio of structural exposures in a given currency to risk-weighted assets denominated in that currency is broadly equal to the capital ratio of the subsidiary in question.

Details of our structural foreign exchange exposures are provided on page 52 of the HSBC Bank plc Annual Report and Accounts 2017*.*

Reputational risk

Reputational risk is the risk of failing to meet stakeholder expectations as a result of any event, behaviour, action or inaction, either by HSBC, our employees or those with whom we are associated. This might cause stakeholders to form a negative view of the Group and result in financial or non-financial effects, loss of confidence in the Group. Reputational risk relates to stakeholders' perceptions, whether fact-based or otherwise. Stakeholders' expectations change constantly and so reputational risk is dynamic and varies between geographical regions, groups and individuals. We have an unwavering commitment to operating at the high standards we set for ourselves in every jurisdiction. Any material lapse in standards of integrity, compliance, customer service or operating efficiency may represent a potential reputational risk.

For further details, please refer to the Reputational Risk section on page 79 of the HSBC Holdings plc Annual Report and Accounts 2017*.*

Sustainability risk

Sustainability risk arises from the provision of financial services to companies or projects which indirectly result in unacceptable impacts on people or on the environment. Sustainability risk is:

- measured by assessing the potential sustainability effect of a customer's activities and assigning a Sustainability Risk Rating to all high-risk transactions;
- monitored quarterly by the RMM and monthly by the Group's Sustainability Risk function; and
- managed using sustainability risk policies covering project finance lending and sector-based sustainability policies for sectors and themes with potentially large environmental or social impacts.

For further details on sustainability risk management, see page 80 of the HSBC Holdings plc Annual Report and Accounts 2017*.*

Business risk

The PRA specifies that banks, as part of their ICAAP, should review their exposure to business risk.

Business risk is the potential negative effect on profits and capital from the group not meeting our strategic objectives, as a result of unforeseen changes in the business and regulatory environment, exposure to economic cycles and technological changes.

We manage and mitigate business risk through our risk appetite, business planning and stress testing processes. This ensures that our business model and planned activities are monitored, resourced and capitalised consistent with the commercial, economic and risk environment in which the group operates. Consequently any potential vulnerabilities of our business plans are identified at an early stage so that mitigating actions can be taken.

Dilution risk

Dilution risk is the risk that an amount receivable is reduced through cash or non-cash credit to the obligor, and arises mainly from factoring and invoice discounting transactions.

Where there is recourse to the seller, we treat these transactions as loans secured by the collateral of the debts purchased and do not report dilution risk for them. For our non-recourse portfolio, we do not report any dilution risk as we obtain an indemnity from the seller that indemnifies us against this risk. Moreover, factoring transactions involve lending at a discount to the face value of the receivables that provides protection against dilution risk.

Remuneration

As a wholly-owned subsidiary, HSBC Bank plc is subject to the remuneration policy established by HSBC. Details of HSBC's remuneration policy, including details on the Remuneration Committee membership and its activities, our remuneration strategy, and tables showing the remuneration details of HSBC's Identified Staff and Material Risk-Takers ('MRT') may be found in the Remuneration Policy on our website (http://www.hsbc.com/investor-relations/governance) and in the Directors' Remuneration Report on pages 141 to 157 of the HSBC Holdings plc *Annual Report and Accounts 2017*.

The following tables show the remuneration awards made to Identified Staff and MRTs in HSBC Bank plc for 2017. Individuals have been identified as MRTs based on the qualitative and quantitative criteria set out in the Regulatory Technical Standard EU 604/2014 which came into force in June 2014 and was subsequently adopted in full for the purposes of the PRA's and the Financial Conduct Authority's ('FCA') Remuneration Code. The tables below include the total remuneration of HSBC Bank plc senior management and other individuals identified as HSBC Bank MRTs based on their role and professional activities. This also includes certain individuals employed by the Group who have broader roles within HSBC, for example those with global roles.

These disclosures reflect the requirements of the FCA's Prudential Sourcebook for Banks.

Table 21: Senior management remuneration – fixed and variable amounts

	Executive Directors	Non-executive Directors	Senior management	Total
Number of MRTs	1	16	19	36
	£m	£m	£m	£m
Total fixed	1.5	4.6	13.6	19.7
Cash-based[1]	1.5	4.6	13.6	19.7
– of which: deferred cash	–	–	–	–
Share-based	–	–	–	–
– of which: deferred shares	–	–	–	–
Total variable[2]	2.2	0.2	11.9	14.3
Cash-based	1.0	0.1	5.7	6.8
– of which: deferred cash	*0.6*	*0.1*	*3.1*	*3.8*
Share-based[3]	1.2	0.1	6.2	7.5
– of which: deferred shares[3]	*0.8*	*0.1*	*3.6*	*4.5*
Other forms	–	–	–	–
– of which: deferred	–	–	–	–
Total remuneration	3.7	4.8	25.5	34.0

1 *Cash-based fixed remuneration is paid immediately.*
2 *Variable pay awarded in respect of 2017. In accordance with shareholder approval received on 23 May 2014 (98% in favour), for each MRT the variable component of remuneration for any one year is limited to 200% of fixed component of the total remuneration of the MRT.*
3 *Share-based awards are made in HSBC shares. Vested shares are subject to a retention period of up to one year.*

Table 22: Senior management guaranteed bonus, sign-on and severance payments

	Executive Directors	Non-executive Directors	Senior management	Total
Guaranteed bonus and sign-on payments[1]				
Made during year (£m)	–	–	–	–
Number of beneficiaries	–	–	–	–
Severance payments[2]				
Awarded and made during year (£m)	–	–	0.8	0.8
Number of beneficiaries	–	–	1	1
Highest such award to a single person (£m)	–	–	0.8	0.8
Made during year (£m)	–	–	0.8	0.8
Number of beneficiaries	–	–	1	1

1 *No sign-on payments were made in 2017. A guaranteed bonus is awarded in exceptional circumstances for new hires, and in the first year only. The circumstances where HSBC would offer a guaranteed bonus would typically involve a critical new hire and would also depend on factors such as the seniority of the individual, whether the new hire candidate has any competing offers and the timing of the hire during the performance year.*
2 *Includes payments such as payment in lieu of notice, statutory severance, outplacement service, legal fees, ex-gratia payments and settlements (excludes pre-existing benefits triggered on termination).*

Table 23: Senior management deferred remuneration[1]

£m	Executive Directors	Non-executive Directors	Senior management	Total
Cash				
Total outstanding deferred remuneration[2]	**1.0**	**0.3**	**5.3**	**6.6**
– of which: Unvested	***1.0***	***0.3***	***5.3***	***6.6***
– of which: Total amount of outstanding deferred and retained remuneration exposed to ex post explicit and/or implicit adjustment	***1.0***	***0.3***	***5.3***	***6.6***
Total amount of amendment during the year due to ex post implicit adjustment	–	–	–	–
Total amount of amendment during the year due to ex post explicit adjustment[3]	–	–	–	–
Total amount of deferred remuneration paid out in the financial year	**0.4**	**0.1**	**3.3**	**3.8**
Shares				
Total outstanding deferred remuneration[2]	**2.7**	**0.8**	**11.3**	**14.8**
– of which: Unvested	***2.7***	***0.8***	***11.3***	***14.8***
– of which: Total amount of outstanding deferred and retained remuneration exposed to ex post explicit and/or implicit adjustment	***2.7***	***0.8***	***11.3***	***14.8***
Total amount of amendment during the year due to ex post implicit adjustment	**0.4**	**0.1**	**1.7**	**2.2**
Total amount of amendment during the year due to ex post explicit adjustment[3]	–	–	–	–
Total amount of deferred remuneration paid out in the financial year[4]	**1.1**	**0.3**	**7.7**	**9.1**
Other forms				
Total outstanding deferred remuneration[2]	–	–	–	–
– of which: Unvested	–	–	–	–
– of which: Total amount of outstanding deferred and retained remuneration exposed to ex post explicit and/or implicit adjustment	–	–	–	–
Total amount of amendment during the year due to ex post implicit adjustment	–	–	–	–
Total amount of amendment during the year due to ex post explicit adjustment[3]	–	–	–	–
Total amount of deferred remuneration paid out in the financial year[4]	–	–	–	–

1 *This table provides details of adjustments during performance year 2017. For details of variable pay awards granted for 2017, please refer to both the remuneration tables above. Deferred remuneration is made in cash and/or shares. Share-based awards are made in HSBC shares.*
2 *Includes unvested deferred awards, and vested awards subject to retention period as at 31 December 2017.*
3 *Includes any amendments due to malus or clawback.*
4 *Shares are considered as paid when they vest. Vested shares are valued using the sale price or the closing share price on the business day immediately preceding the vesting day.*

Table 24: Other MRTs remuneration – fixed and variable amounts

	Investment banking	Retail banking	Asset management	Corporate functions	Independent control functions	All other	Total
Number of MRTs	**282**	**46**	**2**	**25**	**56**	**25**	**436**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Total fixed	**150.7**	**16.8**	**1**	**14.4**	**17.4**	**12.8**	**213.1**
Cash-based[1]	**150.7**	**16.8**	**1.0**	**13.4**	**16.4**	**11.1**	**209.4**
– of which: deferred cash	–	–	–	–	–	–	–
Share-based	–	–	–	**1.0**	**1.0**	**1.7**	**3.7**
– of which: deferred shares	–	–	–	***1.0***	***1.0***	***1.7***	***3.7***
Total variable[2]	**174.3**	**16.5**	**1.1**	**20.0**	**19.5**	**11.4**	**242.8**
Cash-based	**84.5**	**8.0**	**0.5**	**7.5**	**7.5**	**4.4**	**112.4**
– of which: deferred cash	***46.3***	***4.0***	***0.2***	***4.1***	***3.4***	***2.2***	***60.2***
Share-based[3]	**89.8**	**8.5**	**0.4**	**12.5**	**12.0**	**7.0**	**130.2**
– of which: deferred shares[3]	***52.0***	***4.8***	***0.2***	***8.0***	***7.2***	***4.3***	***76.5***
Other forms[3]	–	–	**0.2**	–	–	–	**0.2**
– of which: deferred[3]	–	–	***0.1***	–	–	–	***0.1***
Total remuneration	**325.0**	**33.3**	**2.1**	**34.4**	**36.9**	**24.2**	**455.9**

1 *Cash-based fixed remuneration is paid immediately.*
2 *Variable pay awarded in respect of 2017. In accordance with shareholder approval received on 23 May 2014 (98% in favour), for each MRT the variable component of remuneration for any one year is limited to 200% of the fixed component of the total remuneration of the MRT.*
3 *Share-based awards are made in HSBC shares. Vested shares are subject to a retention period of up to one year.*

Table 25: Other MRTs guaranteed bonus, sign-on and severance payments

	Investment banking	Retail banking	Asset management	Corporate functions	Independent control functions	All other	Total
Guaranteed bonus and sign-on payments[1]							
Made during year (£m)	0.7	—	—	—	—	—	0.7
Number of beneficiaries	1	—	—	—	—	—	1
Severance payments[2]							
Awarded and made during year (£m)	7.0	1.7	—	1.1	—	1.0	10.8
Number of beneficiaries	14	4	—	2	—	3	23
Highest such award to a single person (£m)	1.5	0.6	—	0.9	—	0.4	1.5
Made during year (£m)	6.8	1.6	—	1.1	—	1.0	10.5
Number of beneficiaries	14	4	—	2	—	3	23

1 *No sign-on payments were made in 2017. A guaranteed bonus is awarded in exceptional circumstances for new hires, and in the first year only. The circumstances where HSBC would offer a guaranteed bonus would typically involve a critical new hire and would also depend on factors such as the seniority of the individual, whether the new hire candidate has any competing offers and the timing of the hire during the performance year.*
2 *Includes payments such as payment in lieu of notice, statutory severance, outplacement service, legal fees, ex-gratia payments and settlements (excludes pre-existing benefits triggered on termination).*

Table 26: Other MRTs deferred remuneration[1]

	Investment banking	Retail banking	Asset management	Corporate functions	Independent control functions	All other	Total
£m							
Cash							
Total outstanding deferred remuneration[2]	70.7	6.3	0.4	6.9	5.6	4.5	94.4
– of which: Unvested	*70.7*	*6.3*	*0.4*	*6.9*	*5.6*	*4.5*	*94.4*
Total amount of outstanding deferred and retained remuneration exposed to ex post explicit and/or implicit adjustment	70.7	6.3	0.4	6.9	5.6	4.5	94.4
Total amount of amendment during the year due to ex post implicit adjustment	—	—	—	—	—	—	—
Total amount of amendment during the year due to ex post explicit adjustment[3]	—	—	—	—	—	—	—
Total amount of deferred remuneration paid out in the financial year	32.0	2.3	0.3	2.7	2.3	1.7	41.3
Shares							
Total outstanding deferred remuneration[2]	124.9	13.4	0.6	26.9	22.8	30.7	219.3
– of which: Unvested	*124.8*	*13.4*	*0.6*	*26.9*	*22.8*	*30.7*	*219.2*
Total amount of outstanding deferred and retained remuneration exposed to ex post explicit and/or implicit adjustment	124.9	13.4	0.6	26.9	22.8	30.7	219.3
Total amount of amendment during the year due to ex post implicit adjustment	18.9	2.0	0.1	4.2	3.4	4.5	33.1
Total amount of amendment during the year due to ex post explicit adjustment[3]	—	—	—	—	—	—	—
Total amount of deferred remuneration paid out in the financial year[4]	95.3	8.4	0.4	10.6	11.1	12.4	138.2
Other forms							
Total outstanding deferred remuneration[2]	—	—	0.2	—	—	—	0.2
– of which: Unvested	—	—	*0.2*	—	—	—	*0.2*
Total amount of outstanding deferred and retained remuneration exposed to ex post explicit and/or implicit adjustment	—	—	0.2	—	—	—	0.2
Total amount of amendment during the year due to ex post implicit adjustment	—	—	—	—	—	—	—
Total amount of amendment during the year due to ex post explicit adjustment[3]	—	—	—	—	—	—	—
Total amount of deferred remuneration paid out in the financial year	—	—	0.2	—	—	—	0.2

1 *This table provides details of adjustments during performance year 2017. For details of variable pay awards granted for 2017, please refer to both the remuneration tables above. Deferred remuneration is made in cash and/or shares. Share-based awards are made in HSBC shares and/or linked to notional fund units in the HSBC World Selection Balanced Portfolio.*
2 *Includes unvested deferred awards, and vested deferred awards subject to retention period as at 31 December 2017.*
3 *Includes any amendments due to malus or clawback.*
4 *Shares are considered as paid when they vest. Vested shares are valued using the sale price or the closing share price on the business day immediately preceding the vesting day.*

Table 27: Material risk takers' remuneration by band[1]

	Management body	All other	Total
€0 – 1,000,000	15	285	300
€1,000,000 – 1,500,000	—	69	69
€1,500,000 – 2,000,000	—	35	35
€2,000,000 – 2,500,000	1	23	24
€2,500,000 – 3,000,000	—	16	16
€3,000,000 – 3,500,000	—	8	8
€3,500,000 – 4,000,000	—	5	5
€4,000,000 – 4,500,000	1	2	3
€4,500,000 – 5,000,000	—	2	2
€5,000,000 – 6,000,000	—	2	2
€6,000,000 – 7,000,000	—	7	7
€7,000,000 – 8,000,000	—	—	—
€8,000,000 – 9,000,000	—	—	—
€9,000,000 – 10,000,000	—	—	—
€10,000,000 – 11,000,000	—	1	1

1 *Table prepared in euros in accordance with Article 450 of the European Union Capital Requirements Regulation, using the exchange rates published by the European Commission for financial programming and budget for December of the reported year as published on its website.*

Appendix I

Summary of disclosures withheld

CRD IV reference	Description	Rationale
448(a)	Key assumptions (including assumptions regarding loan prepayments and behaviour of non-maturity deposits) on exposure to interest rate risk on positions not included in the trading book.	Proprietary Assumptions regarding fixed term loan repayments and term behaviouralisation of non-maturity deposits and capital drive HSBC's structural interest rates positioning and market hedging requirements. Disclosure could give key business strategy information to our competitors.

Appendix II

Abbreviations

The following abbreviated terms are used throughout this document.

Abbreviation	Term
A	
AFS[1]	Available-for-sale
ALCM	Asset, Liability and Capital Management
ALCO	Asset and Liability Management Committee
AT1 capital	Additional tier 1 capital
B	
BCBS	Basel Committee on Banking Supervision
BSM	Balance Sheet Management
C	
CCP	Central counterparty
CCR[1]	Counterparty credit risk
CDS[1]	Credit default swap
CET1[1]	Common equity tier 1
CIU	Collective investment undertakings
CRA[1]	Credit risk adjustment
CRD IV[1]	Capital Requirements Regulation and Directive
CRE[1]	Commercial real estate
CRM	Credit risk mitigation/mitigant
CVA	Credit valuation adjustment
E	
EAD[1]	Exposure at default
EBA	European Banking Authority
EC	European Commission
EEA	European Economic Area
EL[1]	Expected loss
EU	European Union
EVE[1]	Economic value of equity
F	
FPC[1]	Financial Policy Committee (UK)
FSB	Financial Stability Board
G	
GB&M	Global Banking and Markets, a global business
GPB	Global Private Banking, a global business
Group	HSBC Holdings together with its subsidiary undertakings
H	
HSBC	HSBC Holdings together with its subsidiary undertakings
I	
IAA[1]	Internal Assessment Approach
ICAAP[1]	Internal Capital Adequacy Assessment Process
ICG	Individual capital guidance
IFRSs	International Financial Reporting Standards
ILAA	Individual Liquidity Adequacy Assessment
ILR	Inherent Liquidity Risk
IMA	Internal Models Approach
IMM[1]	Internal Model Method
IRB[1]	Internal ratings based approach
IRC[1]	Incremental risk charge
IMA	Internal Models Approach
IMM[1]	Internal Model Method
IRB[1]	Internal ratings based approach
IRC[1]	Incremental risk charge
L	
LCR	Liquidity Coverage Ratio
LFRF	Liquidity and Funding Risk Management Framework
LGD[1]	Loss given default
M	
MREL	Minimum requirements for own funds and eligible liabilities
N	
NQH	Non Qualifying Hedge
NSFR	Net Stable Funding Ratio
O	
OTC[1]	Over-the-counter
P	
PD[1]	Probability of default
PFE[1]	Potential future exposure
PRA[1]	Prudential Regulation Authority (UK)
R	
RAS	Risk appetite statement
RBM[1]	Ratings Based Method
RBWM	Retail Bank and Wealth Management, a global business
RMM	Risk Management Meeting of the Group Management Board
RNIV	Risks not in VaR
RWA[1]	Risk-weighted asset
S	
S&P	Standard and Poor's rating agency
STD[1]	Standardised approach
CCR	Standardised approach for counterparty credit risk
SFM[1]	Supervisory Formula Method
SFT[1]	Securities Financing Transactions
SME	Small- and medium-sized enterprise
T	
TLAC[1]	Total Loss Absorbing Capacity
TTC[1]	Through-the-cycle
T1 capital	Tier 1 capital
T2 capital	Tier 2 capital
U	
UK	United Kingdom
V	
VaR[1]	Value at risk

1 *Full definition included in Glossary on the HSBC website www.hsbc.com.*

Appendix III

Cautionary statement regarding forward-looking statements

The Pillar 3 Disclosures at 31 December 2017 contains certain forward-looking statements with respect to HSBC's financial condition, results of operations, capital position and business.

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

Written and/or oral forward-looking statements may also be made in the periodic reports to the US Securities and Exchange Commission, summary financial statements to shareholders, proxy statements, offering circulars and prospectuses, press releases and other written materials, and in oral statements made by HSBC's Directors, officers or employees to third parties, including financial analysts.

Forward-looking statements involve inherent risks and uncertainties. Readers are cautioned that a number of factors could cause actual results to differ, in some instances materially, from those anticipated or implied in any forward-looking statement. These include, but are not limited to:

- changes in general economic conditions in the markets in which we operate, such as continuing or deepening recessions and fluctuations in employment beyond those factored into consensus forecasts; changes in foreign exchange rates and interest rates; volatility in equity markets; lack of liquidity in wholesale funding markets; illiquidity and downward price pressure in national real estate markets; adverse changes in central banks' policies with respect to the provision of liquidity support to financial
- markets; heightened market concerns over sovereign creditworthiness in over-indebted countries; adverse changes in the funding status of public or private defined benefit pensions; and consumer perception as to the continuing availability of credit and price competition in the market segments we serve;
- changes in government policy and regulation, including the monetary, interest rate and other policies of central banks and other regulatory authorities; initiatives to change the size, scope of activities and interconnectedness of financial institutions in connection with the implementation of stricter regulation of financial institutions in key markets worldwide; revised capital and liquidity benchmarks which could serve to deleverage bank balance sheets and lower returns available from the current business model and portfolio mix; imposition of levies or taxes designed to change business mix and risk appetite; the practices, pricing or responsibilities of financial institutions serving their consumer markets; expropriation, nationalisation, confiscation of assets and changes in legislation relating to foreign ownership; changes in bankruptcy legislation in the principal markets in which we operate and the consequences thereof; general changes in government policy that may significantly influence investor decisions; extraordinary government actions as a result of current market turmoil; other unfavourable political or diplomatic developments producing social instability or legal uncertainty which in turn may affect demand for our products and services; the costs, effects and outcomes of product regulatory reviews, actions or litigation, including any additional compliance requirements; and the effects of competition in the markets where we operate including increased competition from non-bank financial services companies, including securities firms; and
- factors specific to HSBC, including discretionary RWA growth and our success in adequately identifying the risks we face, such as the incidence of loan losses or delinquency, and managing those risks (through account management, hedging and other techniques). Effective risk management depends on, among other things, our ability through stress testing and other techniques to prepare for events that cannot be captured by the statistical models it uses; and our success in addressing operational, legal and regulatory, and litigation challenges..

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