

News Release

20 February 2018

THE HONGKONG AND SHANGHAI BANKING CORPORATION LIMITED 2017 CONSOLIDATED RESULTS – HIGHLIGHTS

- Profit before tax up 13% to HK\$115,619m (HK\$102,707m in 2016)
- Attributable profit up 13% to HK\$88,530m (HK\$78,646m in 2016)
- Return on average ordinary shareholders' equity of 13.7% (13.0% in 2016)
- Total assets up 5% to HK\$7,943bn (HK\$7,549bn at 31 December 2016)
- Common equity tier 1 ratio of 15.9%, total capital ratio of 18.9% (16.0% and 19.0% in 2016)
- Cost efficiency ratio of 43.5% (44.5% in 2016)

This document is issued by The Hongkong and Shanghai Banking Corporation Limited ('the Bank') and its subsidiaries (together 'the group'). References to 'HSBC', 'the Group' or 'the HSBC Group' within this document mean HSBC Holdings plc together with its subsidiaries. Within this document the Hong Kong Special Administrative Region of the People's Republic of China is referred to as 'Hong Kong'. The abbreviations 'HK\$m' and 'HK\$bn' represent millions and billions (thousands of millions) of Hong Kong dollars respectively.



Comment by Stuart Gulliver, Chairman

Asia's economies strengthened during 2017, with volumes of exports and trade both picking up pace. Mainland China experienced robust growth, driven by investment, infrastructure and exports. Japan saw its fastest growth for four years, led by an upturn in exports. Hong Kong performed strongly, with domestic demand holding up well, alongside investment and demand from mainland China. In ASEAN countries, growth accelerated, notably in Malaysia and Singapore. India's economy is seeing signs of improvement led by a recovery in demand, while Australia experienced increased growth and investment in the second half of the year.

The Hongkong and Shanghai Banking Corporation Limited recorded profit before tax in 2017 of HK\$115,619m, compared with HK\$102,707m in 2016, an increase of 13%. Net operating income before loan impairment charges increased by 11%, driven by strong performances in Retail Banking and Wealth Management ('RBWM') and Commercial Banking ('CMB'). Cost growth at 8% was less than revenue growth, leading to an improvement in the cost efficiency ratio to 43.5%. Loan impairment charges and other credit risk provisions of HK\$4,437m were 20% lower than in 2016, remaining low in relation to average customer advances.

Loans and advances to customers grew by 17% during 2017, with growth in all businesses, and particularly in Global Banking and Markets ('GB&M'). Customer deposits increased by 5%, and at the end of December 2017 the advances-to-deposits ratio stood at 64.8%. The net interest margin increased by 13 basis points from 1.75% in 2016 to 1.88% in 2017, primarily from wider customer deposit spreads and from a change in asset portfolio mix due to growth in customer lending. Our capital position remained strong, with a common equity tier 1 ratio of 15.9% at the end of the year.

In RBWM, we grew our market shares in mortgages and personal loans in Hong Kong. Our focus on introducing new digital channels to enhance customers' experience continued, with launches during the year in Hong Kong of PayMe, a new social payment application, and Easy Invest, a mobile stock trading application. We also introduced Voice ID for phone banking. In mainland China, we were the first foreign bank to introduce facial recognition technology for customers, as we continued to expand our presence and invest in the Pearl River Delta. We also launched 'Jade by HSBC Premier' for high net-worth customers in mainland China.

In CMB, our Global Liquidity and Cash Management business performed strongly, benefiting from improved deposit spreads. We grew loans in a number of markets, notably Hong Kong, mainland China, Australia, India and Singapore, and continued to increase market share for trade finance in Hong Kong. We launched the mobile Trade Transaction Tracker across eight countries, allowing customers to view the status of their trade transactions on a real-time basis. We continued to enhance our services through digital technology, and HSBC was the first bank to offer Voice ID biometric security technology to its business customers in Hong Kong.

In GB&M, our new majority-owned securities joint venture in mainland China, HSBC Qianhai Securities Limited, formally opened for business on 7 December 2017. In line with our aim to be a leader in sustainable financing, we continued to increase our involvement in supporting the issuance of green bonds, participating in green bond issues for several major issuers including ICBC, DBS, CLP, Asian Development Bank, and Korea Development Bank. We were the first foreign bank to raise funds through the China-Hong Kong Bond Connect following its launch in July 2017, and were the first foreign bank to be approved as a joint-lead underwriter for Panda bond issuance by offshore non-financial corporates in mainland China's interbank bond market. We ranked first among foreign banks for Panda bond underwriting, and first among all banks in the Renminbi Qualified Foreign Institutional Investor custodian business.

We were very pleased to win a number of awards including 'Asia's Best Bank' and 'Hong Kong's Best Bank', alongside 'World's Best Bank' for the HSBC Group in the *Euromoney Awards for Excellence*. We received 'Best Overall International Bank for Belt and Road' from *Asiamoney*, and 'Best Belt and Road Bank' from *FinanceAsia*. We also ranked first overall and first in all 11 categories of *Asiamoney's* Offshore RMB Poll, for the sixth consecutive year. In January this year, we were also named by *Euromoney* as 'Top Global Trade Finance Bank'.

As I step down as Chairman, I would like to thank all our customers and staff for their support over the last seven years. I am proud of our achievements and confident that under my successor John Flint, we are strongly positioned to continue to deliver value to all our stakeholders. Asia has entered 2018 with favourable growth prospects, and we will continue to play our part in connecting customers to opportunities in the region's growth, China's Belt and Road initiative and internationalisation of the renminbi.

Consolidated income statement and balance sheet data by global business (audited)

	Retail Banking and Wealth Management	Commercial Banking	Global Banking and Markets	Global Private Banking	Corporate Centre ¹	Total
	HK\$m	HK\$m	HK\$m	HK\$m	HK\$m	HK\$m
Year ended 31 Dec 2017						
Net interest income	50,789	31,237	19,147	1,868	7,196	110,237
Net fee income	20,695	10,443	9,936	1,916	160	43,150
Net trading income	2,056	2,976	16,161	963	1,054	23,210
Net income/(expense) from financial instruments designated at fair value	15,903	(416)	19	—	(126)	15,380
Gains less losses from financial investments	149	64	1	—	1,894	2,108
Dividend income	36	1	—	—	195	232
Net insurance premium income/(expense)	53,275	2,933	—	—	(32)	56,176
Other operating income	1,488	336	189	51	2,676	4,740
Total operating income	144,391	47,574	45,453	4,798	13,017	255,233
Net insurance claims and benefits paid and movement in liabilities to policyholders	(65,941)	(2,849)	—	—	—	(68,790)
Net operating income before loan impairment charges and other credit risk provisions	78,450	44,725	45,453	4,798	13,017	186,443
Loan impairment (charges)/releases and other credit risk provisions	(1,907)	(2,157)	(451)	(2)	80	(4,437)
Net operating income	76,543	42,568	45,002	4,796	13,097	182,006
Operating expenses	(34,807)	(16,115)	(20,653)	(2,679)	(6,813)	(81,067)
Operating profit	41,736	26,453	24,349	2,117	6,284	100,939
Share of profit in associates and joint ventures	86	—	—	—	14,594	14,680
Profit before tax	41,822	26,453	24,349	2,117	20,878	115,619
Balance at 31 Dec 2017						
Net loans and advances to customers	1,049,006	1,143,241	1,004,350	115,064	17,319	3,328,980
Customer accounts	2,701,399	1,311,873	905,991	187,825	31,184	5,138,272
Year ended 31 Dec 2016						
Net interest income	43,632	26,945	17,367	1,444	7,520	96,908
Net fee income	17,949	10,355	9,502	1,278	218	39,302
Net trading income	1,377	2,450	17,168	1,007	2,062	24,064
Net income/(expense) from financial instruments designated at fair value	3,591	(276)	91	—	164	3,570
Gains less losses from financial investments	335	249	33	—	615	1,232
Dividend income	67	1	—	—	166	234
Net insurance premium income/(expense)	52,954	3,004	—	—	(46)	55,912
Other operating income	7,792	473	1,143	15	2,093	11,516
Total operating income	127,697	43,201	45,304	3,744	12,792	232,738
Net insurance claims and benefits paid and movement in liabilities to policyholders	(61,280)	(3,306)	—	—	—	(64,586)
Net operating income before loan impairment charges and other credit risk provisions	66,417	39,895	45,304	3,744	12,792	168,152
Loan impairment (charges)/releases and other credit risk provisions	(2,133)	(2,469)	(874)	4	(82)	(5,554)
Net operating income	64,284	37,426	44,430	3,748	12,710	162,598
Operating expenses	(32,520)	(14,971)	(19,413)	(2,332)	(5,567)	(74,803)
Operating profit	31,764	22,455	25,017	1,416	7,143	87,795
Share of profit in associates and joint ventures	148	—	—	—	14,764	14,912
Profit before tax	31,912	22,455	25,017	1,416	21,907	102,707
Balance at 31 Dec 2016						
Net loans and advances to customers	936,310	996,772	791,522	91,574	17,936	2,834,114
Customer accounts	2,537,128	1,286,368	857,583	192,163	26,762	4,900,004

¹ Includes inter-segment elimination.

Results Commentary

The group reported profit before tax of HK\$115,619m, an increase of 13% compared with 2016, driven by higher net interest income, higher net fee income and higher income (net of claims) from insurance business.

Net interest income increased by HK\$13,329m, or 14%, compared with 2016, driven by Hong Kong mainly from wider customer deposit spreads and higher yields on financial investments, which benefited from interest rate rises since late 2016, coupled with balance sheet growth, mainly in loans and advances to customers.

Net fee income increased by HK\$3,848m, or 10%, compared with 2016, mainly in Hong Kong from higher securities brokerage, unit trust and funds under management fees due to higher turnover from favourable equity market sentiment in 2017, and to a lesser extent from higher mandatory provident fund and underwriting fees.

Net trading income decreased by HK\$854m, or 4%, driven by mainland China from foreign exchange translation losses on foreign currency denominated financial assets, higher interest expense and revaluation losses on structured deposits, coupled with higher revaluation losses on foreign currency funding swaps. The decrease in net trading income was also due to unfavourable valuation adjustments on derivative contracts from the narrowing of own credit spreads, mainly in Hong Kong and Australia. These were partly offset by higher net trading income in insurance business in Hong Kong, mainly from the favourable revaluation of foreign currency swaps. Net trading income in Taiwan also increased, mainly from higher revaluation gains on foreign currency funding swaps.

Net income from financial instruments designated at fair value increased by HK\$11,810m, driven by revaluation gains on the equity portfolio held by the insurance business in Hong Kong from strong equity market performance in 2017. To the extent that investment returns are attributable to policyholders, there is an offsetting movement reported under 'Net insurance claims and benefits paid and movement in liabilities to policyholders'.

Gains less losses from financial investments increased by HK\$876m, mainly reflecting the gain on disposal of our available-for-sale investment in Vietnam Technological and Commercial Joint Stock Bank ('Techcom Bank').

Other operating income decreased by HK\$6,776m, driven by lower favourable movements in the present value of in-force insurance business, mainly in Hong Kong and Singapore due to unfavourable actuarial assumption updates. This was partly offset by higher gains from the revaluation of investment properties.

Net insurance claims and benefits paid and movement in liabilities to policyholders increased by HK\$4,204m, reflecting higher investment returns to policyholders due to strong equity market performance in 2017, partly offset by the impact from lower favourable movements in the present value of in-force business.

Loan impairment charges and other credit risk provisions decreased by HK\$1,117m, or 20%, with decreases across various countries, notably in Singapore from impairment releases in CMB, in India mainly from the non-recurrence of impairment charges in GB&M, coupled with releases in CMB, in mainland China from lower impairment charges mainly in CMB, and in Australia mainly due to the non-recurrence of a charge in GB&M. These were partly offset by higher impairment charges in Hong Kong, mainly in CMB.

Total operating expenses increased by HK\$6,264m, or 8%, mainly in IT-related costs and professional and consultancy expenses to support business growth, and continued investment in regulatory and compliance programmes, coupled with higher staff costs mainly due to higher performance-related pay.

Share of profit in associates and joint ventures decreased by HK\$232m, or 2%, mainly from the impact of foreign exchange translation.

Consolidated income statement

for the year ended 31 December

	2017	2016
	HK\$m	HK\$m
Net interest income	110,237	96,908
– interest income	138,081	122,564
– interest expense	(27,844)	(25,656)
Net fee income	43,150	39,302
– fee income	52,312	47,139
– fee expense	(9,162)	(7,837)
Net trading income	23,210	24,064
Net income from financial instruments designated at fair value	15,380	3,570
Gains less losses from financial investments	2,108	1,232
Dividend income	232	234
Net insurance premium income	56,176	55,912
Other operating income	4,740	11,516
Total operating income	255,233	232,738
Net insurance claims and benefits paid and movement in liabilities to policyholders	(68,790)	(64,586)
Net operating income before loan impairment charges and other credit risk provisions	186,443	168,152
Loan impairment charges and other credit risk provisions	(4,437)	(5,554)
Net operating income	182,006	162,598
Employee compensation and benefits	(40,095)	(38,896)
General and administrative expenses	(34,786)	(29,917)
Depreciation of property, plant and equipment	(4,650)	(4,493)
Amortisation and impairment of intangible assets	(1,536)	(1,497)
Total operating expenses	(81,067)	(74,803)
Operating profit	100,939	87,795
Share of profit in associates and joint ventures	14,680	14,912
Profit before tax	115,619	102,707
Tax expense	(19,601)	(17,912)
Profit for the year	96,018	84,795
Profit attributable to shareholders of the parent company	88,530	78,646
Profit attributable to non-controlling interests	7,488	6,149

Consolidated statement of comprehensive income

for the year ended 31 December

	2017 HK\$m	2016 HK\$m
Profit for the year	96,018	84,795
Other comprehensive income/(expense)		
Items that will be reclassified subsequently to the income statement when specific conditions are met:		
Available-for-sale investments:	1,609	499
– fair value gains/(losses)	3,346	(430)
– fair value gains reclassified to the income statement on disposal	(2,118)	(1,226)
– amounts reclassified to the income statement in respect of impairment losses	5	2
– fair value losses transferred to the income statement on hedged items	451	2,296
– income taxes	(75)	(143)
Cash flow hedges:	607	(802)
– fair value gains/(losses)	(6,780)	1,354
– fair value (gains)/losses reclassified to the income statement	7,506	(2,295)
– income taxes	(119)	139
Share of other comprehensive income/(expense) of associates and joint venture	(852)	1,266
Exchange differences	25,387	(15,241)
Items that will not be reclassified subsequently to the income statement:		
Changes in fair value of financial liabilities designated at fair value arising from changes in own credit risk ¹	(209)	–
– before income taxes	(250)	–
– income taxes	41	–
Property revaluation:	8,864	3,147
– fair value gains taken to equity	10,442	3,825
– income taxes	(1,578)	(678)
Remeasurement of defined benefit asset/liability:	1,371	833
– before income taxes	1,640	1,016
– income taxes	(269)	(183)
Other comprehensive income for the year, net of tax	36,777	(10,298)
Total comprehensive income for the year	132,795	74,497
Attributable to:		
– shareholders of the parent company	123,739	68,577
– non-controlling interests	9,056	5,920
Total comprehensive income for the year	132,795	74,497

¹ On 1 January 2017, the group adopted the requirements of Hong Kong Financial Reporting Standard ('HKFRS') 9 relating to the presentation of gains and losses on financial liabilities designated at fair value. As a result, the effect of changes in fair value of those liabilities arising from changes in own credit risk is presented in other comprehensive income. As permitted by the transitional requirements of HKFRS 9, comparatives have not been restated.

Consolidated balance sheet

at 31 December

	2017 HK\$m	2016 HK\$m
Assets		
Cash and sight balances at central banks	208,073	213,783
Items in the course of collection from other banks	25,714	21,401
Hong Kong Government certificates of indebtedness	267,174	242,194
Trading assets	496,434	371,634
Derivatives	300,243	479,807
Financial assets designated at fair value	122,646	106,016
Reverse repurchase agreements – non-trading	330,890	271,567
Placings with and advances to banks	433,005	463,211
Loans and advances to customers	3,328,980	2,834,114
Financial investments	1,720,873	1,835,351
Amounts due from Group companies	227,729	242,773
Interests in associates and joint ventures	144,717	125,792
Goodwill and intangible assets	59,865	56,936
Property, plant and equipment	116,336	111,640
Deferred tax assets	2,156	1,503
Prepayments, accrued income and other assets	158,511	171,230
Total assets	7,943,346	7,548,952
Liabilities		
Hong Kong currency notes in circulation	267,174	242,194
Items in the course of transmission to other banks	38,283	37,753
Repurchase agreements – non-trading	47,170	27,810
Deposits by banks	201,697	192,479
Customer accounts	5,138,272	4,900,004
Trading liabilities	231,365	188,470
Derivatives	309,353	462,458
Financial liabilities designated at fair value	49,278	51,116
Debt securities in issue	38,394	25,235
Retirement benefit liabilities	2,222	3,867
Amounts due to Group companies	265,688	198,038
Accruals and deferred income, other liabilities and provisions	110,687	99,487
Liabilities under insurance contracts	438,017	386,170
Current tax liabilities	3,242	1,619
Deferred tax liabilities	24,391	21,401
Subordinated liabilities	4,090	4,836
Preference shares	21,037	26,879
Total liabilities	7,190,360	6,869,816
Equity		
Share capital	151,360	114,359
Other equity instruments	14,737	14,737
Other reserves	123,417	85,886
Retained earnings	406,966	413,024
Total shareholders' equity	696,480	628,006
Non-controlling interests	56,506	51,130
Total equity	752,986	679,136
Total equity and liabilities	7,943,346	7,548,952

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

	Other reserves										
	Share capital	Other equity instruments	Retained earnings	Property revaluation reserve	Available-for-sale investment reserve	Cash flow hedge reserve	Foreign exchange reserve	Other ¹	Total shareholders' equity	Non-controlling interests	Total equity
	HK\$m	HK\$m	HK\$m	HK\$m	HK\$m	HK\$m	HK\$m	HK\$m	HK\$m	HK\$m	HK\$m
At 1 Jan 2017	114,359	14,737	413,024	53,763	6,189	(793)	(31,861)	58,588	628,006	51,130	679,136
Profit for the year	—	—	88,530	—	—	—	—	—	88,530	7,488	96,018
Other comprehensive income/(expense) (net of tax)	—	—	976	8,144	636	596	24,913	(56)	35,209	1,568	36,777
– available-for-sale investments	—	—	—	—	1,422	—	—	—	1,422	187	1,609
– cash flow hedges	—	—	—	—	—	596	—	—	596	11	607
– changes in fair value of financial liabilities designated at fair value arising from changes in own credit risk ²	—	—	(207)	—	—	—	—	—	(207)	(2)	(209)
– property revaluation	—	—	—	8,144	—	—	—	—	8,144	720	8,864
– actuarial gains on defined benefit asset/liability	—	—	1,193	—	—	—	—	—	1,193	178	1,371
– share of other comprehensive expense of associates and joint ventures	—	—	(10)	—	(786)	—	—	(56)	(852)	—	(852)
– exchange differences	—	—	—	—	—	—	24,913	—	24,913	474	25,387
Total comprehensive income/(expense) for the year	—	—	89,506	8,144	636	596	24,913	(56)	123,739	9,056	132,795
Shares issued	1,744	—	—	—	—	—	—	—	1,744	—	1,744
Dividends paid ³	—	—	(56,260)	—	—	—	—	—	(56,260)	(4,632)	(60,892)
Movement in respect of share-based payment arrangements	—	—	(73)	—	—	—	—	(324)	(397)	(9)	(406)
Transfers and other movements ^{4,5,6}	35,257	—	(39,231)	(3,526)	—	—	—	7,148	(352)	961	609
At 31 Dec 2017	151,360	14,737	406,966	58,381	6,825	(197)	(6,948)	65,356	696,480	56,506	752,986
At 1 Jan 2016	96,052	14,737	380,381	52,099	4,880	(35)	(16,991)	53,078	584,201	51,685	635,886
Profit for the year	—	—	78,646	—	—	—	—	—	78,646	6,149	84,795
Other comprehensive income/(expense) (net of tax)	—	—	542	3,123	1,309	(758)	(14,870)	585	(10,069)	(229)	(10,298)
– available-for-sale investments	—	—	—	—	622	—	—	—	622	(123)	499
– cash flow hedges	—	—	—	—	—	(758)	—	—	(758)	(44)	(802)
– property revaluation	—	—	(245)	3,123	—	—	—	—	2,878	269	3,147
– actuarial gains on defined benefit asset/liability	—	—	793	—	—	—	—	—	793	40	833
– share of other comprehensive income/(expense) of associates and joint ventures	—	—	(6)	—	687	—	—	585	1,266	—	1,266
– exchange differences	—	—	—	—	—	—	(14,870)	—	(14,870)	(371)	(15,241)
Total comprehensive income/(expense) for the year	—	—	79,188	3,123	1,309	(758)	(14,870)	585	68,577	5,920	74,497
Shares issued	18,307	—	—	—	—	—	—	—	18,307	—	18,307
Dividends paid ³	—	—	(43,296)	—	—	—	—	—	(43,296)	(6,297)	(49,593)
Movement in respect of share-based payment arrangements	—	—	235	—	—	—	—	(258)	(23)	(3)	(26)
Transfers and other movements ⁵	—	—	(3,484)	(1,459)	—	—	—	5,183	240	(175)	65
At 31 Dec 2016	114,359	14,737	413,024	53,763	6,189	(793)	(31,861)	58,588	628,006	51,130	679,136

¹ The other reserves mainly comprise share of associates' other reserves, purchase premium arising from transfer of business within the HSBC Group and the share-based payment reserve. The share-based payment reserve is used to record the amount relating to share awards and options granted to employees of the group directly by HSBC Holdings plc.

² On 1 January 2017, the group adopted the requirements of Hong Kong Financial Reporting Standard ('HKFRS') 9 relating to the presentation of gains and losses on financial liabilities designated at fair value. As a result, the effect of changes in fair value of those liabilities arising from changes in own credit risk is presented in retained earnings. As permitted by the transitional requirements of HKFRS 9, comparatives have not been restated.

³ Including distributions paid on perpetual subordinated loans classified as equity under HKFRS.

⁴ In 2017, the Bank redeemed US\$775m (HK\$6,022m) of preference shares which were classified as a financial liability in the consolidated balance sheet. The redemption was made by a payment out of distributable profits. The amount of preference shares has been credited to share capital with a corresponding adjustment to retained earnings in accordance with the capital maintenance requirements of the Companies Ordinance. In 2013, the Bank redeemed US\$3,745m (HK\$29,235m) of preference shares in the same manner. This amount was also credited to share capital with a corresponding adjustment to retained earnings in accordance with the capital maintenance requirements of the Companies Ordinance. The total amount credited to share capital with a corresponding adjustment to retained earnings in 2017 in respect of these transactions was HK\$35,257m. This amount is non-distributable.

⁵ The movement from retained earnings to other reserves includes the relevant transfers in associates according to local regulatory requirements.

⁶ The movement from property revaluation reserve to other reserves includes HK\$2,100m relating to transfer of properties to a fellow subsidiary as part of the Recovery & Resolution Plan as set out in the Report of Directors in the Annual Report and Accounts 2017.

1 Net interest income

	2017	2016
	HK\$m	HK\$m
Net interest income	110,237	96,908
Average interest-earning assets	5,850,010	5,527,461
	%	%
Spread	1.80	1.67
Contribution from net free funds	0.08	0.08
Net interest margin	1.88	1.75

Net interest income ('NII') increased by HK\$13,329m, or 14% compared with 2016, driven by Hong Kong mainly from wider customer deposit spreads and higher yields on financial investments, which benefited from interest rate rises since late 2016, coupled with balance sheet growth, mainly in loans and advances to customers. NII also increased in mainland China from balance sheet growth, higher re-investment yields on financial investments, coupled with lower cost of funds, in Australia from balance sheet growth and lower cost of funds, and in Singapore mainly from balance sheet growth.

Average interest-earning assets increased by HK\$323bn, or 6%, compared with 2016, driven by Hong Kong mainly due to an increase in loans and advances to customers, notably in corporate term lending and mortgages.

Net interest margin increased by 13 basis points compared with 2016, driven by Hong Kong, although increases were also noted in mainland China and Australia.

In **Hong Kong**, the net interest margin for the Bank increased by 14 basis points, mainly due to wider customer deposit spreads and higher re-investment yields on financial investments following interest rate increases, coupled with a change in asset portfolio mix due to growth in customer lending. These increases were partly offset by an increase in financial liabilities to meet the 'Total Loss Absorbing Capacity' requirement, coupled with compressed lending spreads.

At **Hang Seng Bank**, the net interest margin increased by 12 basis points, mainly from improved customer deposit spreads and higher re-investment yields on financial investments following interest rate increases and a change in asset portfolio mix due to growth in customer lending, partly offset by compressed lending spreads.

In mainland China, the net interest margin increased, driven by higher yield from portfolio mix changes due to growth in customer lending, higher re-investment yields from financial investments, coupled with lower cost of funds which benefited from increases in savings and current account deposits, partly offset by reduced lending spreads. In Australia, the net interest margin increased mainly from lower cost of funds following successive interest rate cuts by the Reserve Bank of Australia in 2016, while yield decreased to a lesser extent due to a change in asset portfolio mix as customer lending grew.

2 Net fee income

	2017	2016
	HK\$m	HK\$m
Account services	2,863	3,063
Funds under management	7,000	5,771
Cards	7,622	7,063
Credit facilities	2,886	2,825
Broking income	4,386	3,131
Imports/exports	3,627	3,771
Unit trusts	6,987	5,855
Underwriting	1,477	1,188
Remittances	3,316	3,324
Global custody	3,626	3,450
Insurance agency commission	1,982	1,746
Other	6,540	5,952
Fee income	52,312	47,139
Fee expense	(9,162)	(7,837)
Year ended 31 Dec	43,150	39,302

3 Net trading income

	2017 HK\$m	2016 HK\$m
Dealing profits	15,847	18,195
Net interest income on trading activities	4,194	3,718
Dividend income from trading securities	3,146	2,074
Net gain from hedging activities	23	77
Year ended 31 Dec	23,210	24,064

4 Net income from financial instruments designated at fair value

	2017 HK\$m	2016 HK\$m
Income on assets designated at fair value which back insurance and investment contracts	18,162	4,104
Increase in fair value of liabilities to customers under investment contracts	(2,555)	(651)
	15,607	3,453
Net change in fair value of other financial assets/liabilities designated at fair value	(242)	102
Interest income on financial assets and liabilities designated at fair value	15	15
Year ended 31 Dec	15,380	3,570

5 Gains less losses from financial investments

	2017 HK\$m	2016 HK\$m
Gains on disposal of available-for-sale securities	2,113	1,234
Impairment of available-for-sale equity investments	(5)	(2)
Year ended 31 Dec	2,108	1,232

The increase in gains on disposal of available-for-sale securities was mainly from the disposal of our investment in Techcom Bank in 2017.

6 Other operating income

	2017 HK\$m	2016 HK\$m
Movement in present value of in-force insurance business	305	7,306
Gains on investment properties	416	36
Gains/(losses) on disposal of property, plant and equipment and assets held for sale	77	(57)
Gains/(losses) on disposal of subsidiaries, associates and business portfolios	(186)	1
Rental income from investment properties	426	400
Other	3,702	3,830
Year ended 31 Dec	4,740	11,516

7 Insurance income

Included in net operating income are the following revenues earned by the insurance business:

	2017 HK\$m	2016 HK\$m
Net interest income	12,580	11,543
Net fee income	2,800	2,044
Net trading loss	(11)	(1,126)
Net income from financial instruments designated at fair value	15,486	3,315
Net insurance premium income	56,176	55,912
Movement in PVIF	305	7,306
Other operating income	475	771
Total operating income	87,811	79,765
Net insurance claims and benefits paid and movement in liabilities to policyholders	(68,790)	(64,586)
Net operating income	19,021	15,179

Net operating income from the insurance business increased by HK\$3,842m, or 25%, driven by favourable market conditions in 2017.

Net interest income increased by 9% from growth in insurance fund size, reflecting net inflows from new and renewal of life insurance premiums.

Net trading loss decreased mainly due to favourable revaluation of foreign currency swaps in Hong Kong against revaluation losses reported last year.

Net income from financial instruments designated at fair value increased significantly, driven by revaluation gains on the equity portfolio supporting insurance contracts, reflecting strong equity market performance in Hong Kong. To the extent that these gains are attributable to policyholders, there is an offsetting movement reported under 'Net insurance claims and benefits paid and movement in liabilities to policyholders'.

Net insurance premium income increased slightly, as the increase in Hong Kong from new business sales and higher renewals was partly offset by a new reinsurance agreement, coupled with lower insurance premium income in Singapore due to lower new business sales.

The lower favourable movements in the present value of in-force business ('PVIF') was driven by Hong Kong and Singapore. The PVIF movement in Hong Kong was due to the less favourable interest rate assumption update, and also reflected future sharing of higher investment returns with policyholders. The PVIF movement in Singapore was due to changes in actuarial assumptions reflecting regulatory driven changes, and the impact from lapse rate experience and market interest rate movements. These were partly offset by a corresponding movement in 'Net insurance claims and benefits paid and movement in liabilities to policyholders'.

8 Loan impairment charges and other credit risk provisions

	2017	2016
	HK\$m	HK\$m
Individually assessed impairment charges	2,194	3,380
– new charges	4,239	5,224
– releases	(1,865)	(1,567)
– recoveries	(180)	(277)
Collectively assessed impairment charges	2,136	2,065
Other credit risk provisions	107	109
Year ended 31 Dec	4,437	5,554

Loan impairment charges as a percentage of average gross customer advances remained low at 0.14% for 2017 (2016: 0.20%).

9 Employee compensation and benefits

	2017	2016
	HK\$m	HK\$m
Wages and salaries	36,485	35,376
Social security costs	1,110	1,022
Retirement benefit costs	2,500	2,498
Year ended 31 Dec	40,095	38,896

Employee compensation and benefits increased by HK\$1,199m mainly due to higher performance-related pay and wage inflation. Total average headcount remained stable, as the increase in mainland China to support business growth was largely offset by decreases across various countries, mainly in Indonesia, India and Brunei.

10 General and administrative expenses

	2017	2016
	HK\$m	HK\$m
Premises and equipment	7,814	7,772
– rental expenses	3,717	3,665
– other premises and equipment expenses	4,097	4,107
Marketing and advertising expenses	2,785	2,909
Other administrative expenses	24,187	19,236
Year ended 31 Dec	34,786	29,917

Other administrative expenses increased by HK\$4,951m compared with 2016, mainly due to higher recharges from global functions, mainly IT-related costs, and from global businesses, coupled with higher professional and consultancy expenses largely relating to regulatory and compliance programmes, transformation initiatives and to support business growth.

11 Associates and joint ventures

At 31 December 2017, an impairment review on the group's investment in Bank of Communications Co., Ltd ('BoCom') was carried out and it was concluded that the investment was not impaired at the end of the year based on our value in use calculation (see note on 'Associates and Joint Ventures' in the *Annual Report and Accounts 2017* for further details). In future periods, the value in use may increase or decrease depending on the impact of changes to model inputs. It is expected that the carrying amount will increase in 2018 due to retained earnings earned by BoCom. At the point where the carrying amount exceeds the value in use, the group will determine whether an impairment exists. If so, the group would continue to recognise its share of BoCom's profit or loss, but the carrying amount would be reduced to equal the value in use, with a corresponding reduction in income, unless the market value has increased to a level above the carrying amount.

12 Tax expense

	2017	2016
	HK\$m	HK\$m
Current tax		
– Hong Kong taxation	10,486	8,493
– overseas taxation	8,315	7,261
Deferred tax	800	2,158
Year ended 31 Dec	19,601	17,912
Effective tax rate	16.9%	17.4%

13 Dividends

Dividends to ordinary shareholders of the parent company

	2017		2016	
	HK\$ per share	HK\$m	HK\$ per share	HK\$m
Ordinary dividends paid				
– fourth interim dividend in respect of the previous financial year approved and paid during the year	0.56	25,438	0.44	17,065
– first interim dividend paid	0.22	10,000	0.20	8,500
– second interim dividend paid	0.22	10,000	0.19	8,500
– third interim dividend paid	0.22	10,000	0.19	8,500
Total	1.22	55,438	1.02	42,565

The Directors have declared a fourth interim dividend in respect of the financial year ended 31 December 2017 of HK\$0.36 per ordinary share (HK\$16,559m) (2016: HK\$0.56 per ordinary share (HK\$25,438m)).

Distributions on other equity instruments

	2017	2016
	HK\$m	HK\$m
Floating rate perpetual subordinated loans (interest rate at one year US dollar LIBOR plus 3.84%)	822	731

14 Analysis of loans and advances to customers

The following analysis of loans and advances to customers is based on categories used by the HSBC Group.

	Hong Kong HK\$m	Rest of Asia-Pacific HK\$m	Total HK\$m
At 31 Dec 2017			
Residential mortgages	549,247	306,541	855,788
Credit card advances	61,672	27,696	89,368
Other personal	156,121	73,998	230,119
Total personal	767,040	408,235	1,175,275
Commercial, industrial and international trade	488,705	422,672	911,377
Commercial real estate	245,279	69,247	314,526
Other property-related lending	275,744	85,036	360,780
Government	39,558	5,509	45,067
Other commercial	171,438	157,939	329,377
Total corporate and commercial	1,220,724	740,403	1,961,127
Non-bank financial institutions	116,915	84,917	201,832
Settlement accounts	3,021	770	3,791
Total financial	119,936	85,687	205,623
Gross loans and advances to customers	2,107,700	1,234,325	3,342,025
Individually assessed impairment allowances	(3,429)	(4,800)	(8,229)
Collectively assessed impairment allowances	(2,240)	(2,576)	(4,816)
Net loans and advances to customers	2,102,031	1,226,949	3,328,980
At 31 Dec 2016			
Residential mortgages	492,989	267,619	760,608
Credit card advances	58,289	22,665	80,954
Other personal	132,171	70,947	203,118
Total personal	683,449	361,231	1,044,680
Commercial, industrial and international trade	428,035	384,227	812,262
Commercial real estate	198,579	55,786	254,365
Other property-related lending	221,919	69,911	291,830
Government	20,230	2,405	22,635
Other commercial	136,729	132,944	269,673
Total corporate and commercial	1,005,492	645,273	1,650,765
Non-bank financial institutions	103,311	45,611	148,922
Settlement accounts	1,337	1,102	2,439
Total financial	104,648	46,713	151,361
Gross loans and advances to customers	1,793,589	1,053,217	2,846,806
Individually assessed impairment allowances	(2,960)	(5,099)	(8,059)
Collectively assessed impairment allowances	(1,959)	(2,674)	(4,633)
Net loans and advances to customers	1,788,670	1,045,444	2,834,114

Allowances as a percentage of gross loans and advances to customers

	2017	2016
– individually assessed	0.25%	0.28%
– collectively assessed	0.14%	0.16%
Total allowances	0.39%	0.44%

Gross loans and advances to customers in Hong Kong increased by HK\$314bn, or 18%, largely from increases in corporate and commercial lending of HK\$215bn, mainly in the property sector, coupled with growth in residential mortgages of HK\$56bn and other personal lending of HK\$24bn.

In the Rest of Asia-Pacific, gross loans and advances to customers increased by HK\$181bn, or 17%, including favourable foreign exchange translation effects of HK\$81bn. Excluding this impact, the underlying increase of HK\$100bn was driven by increases in corporate and commercial lending of HK\$49bn, lending to non-bank financial institutions of HK\$35bn and residential mortgages of HK\$16bn, mainly in mainland China and Australia.

15 Movement in impairment allowances against loans and advances to customers

	Individually assessed	Collectively assessed	Total
	HK\$m	HK\$m	HK\$m
At 1 Jan 2017	8,059	4,633	12,692
Amounts written off	(2,189)	(2,806)	(4,995)
Recoveries of loans and advances written off in previous years	180	713	893
Net charge to income statement	2,194	2,136	4,330
Unwinding of discount of loan impairment	(235)	(17)	(252)
Exchange and other adjustments	220	157	377
At 31 Dec 2017	8,229	4,816	13,045
At 1 Jan 2016	7,040	4,489	11,529
Amounts written off	(2,334)	(2,694)	(5,028)
Recoveries of loans and advances written off in previous years	277	881	1,158
Net charge to income statement	3,380	2,065	5,445
Unwinding of discount of loan impairment	(310)	(58)	(368)
Exchange and other adjustments	6	(50)	(44)
At 31 Dec 2016	8,059	4,633	12,692

16 Financial investments

	2017 HK\$m	2016 HK\$m
Available-for-sale	1,419,930	1,574,584
– treasury and other eligible bills	539,014	688,369
– debt securities	871,641	877,504
– equity shares	9,275	8,711
Held-to-maturity	300,943	260,767
– treasury and other eligible bills	699	–
– debt securities	300,244	260,767
At 31 Dec	1,720,873	1,835,351

17 Prepayments, accrued income and other assets

	2017 HK\$m	2016 HK\$m
Prepayments and accrued income	24,541	21,505
Bullion	44,555	69,894
Acceptances and endorsements	36,720	32,290
Reinsurers' share of liabilities under insurance contracts	15,734	11,368
Current tax assets	2,485	3,537
Other accounts	34,476	32,636
At 31 Dec	158,511	171,230

18 Customer accounts

	2017 HK\$m	2016 HK\$m
Current accounts	1,078,661	991,562
Saving accounts	3,057,145	2,946,379
Other deposit accounts	1,002,466	962,063
At 31 Dec	5,138,272	4,900,004

19 Accruals and deferred income, other liabilities and provisions

	2017	2016
	HK\$m	HK\$m
Accruals and deferred income	25,880	24,409
Acceptances and endorsements	36,720	32,290
Share based payment liability to HSBC Holdings plc	2,268	1,945
Other liabilities	45,193	39,676
Provisions for liabilities and charges	626	1,167
At 31 Dec	110,687	99,487

20 Contingent liabilities, contractual commitments and guarantees

	2017	2016
	HK\$m	HK\$m
Guarantees and contingent liabilities	289,892	259,559
Commitments	2,481,711	2,287,617
At 31 Dec	2,771,603	2,547,176

21 Capital overview

The following tables show the capital ratios, risk-weighted assets ('RWAs') and capital base on a consolidated basis, in accordance with the Banking (Capital) Rules.

Capital ratios

	2017	2016
	%	%
Common equity tier 1 ('CET1') capital ratio	15.9	16.0
Tier 1 capital ratio	17.0	17.2
Total capital ratio	18.9	19.0

Total regulatory capital and RWAs

	2017	2016
	HK\$m	HK\$m
Common equity tier 1 capital	438,693	414,308
Additional tier 1 capital	29,328	30,564
Tier 2 capital	54,223	46,430
Total regulatory capital	522,244	491,302
RWAs	2,758,609	2,588,589

22 Accounting policies

The accounting policies and methods of computation adopted by the group for this document are consistent with those described in the *Annual Report and Accounts 2017*.

Standards adopted during the year ended 31 December 2017

The group has adopted the requirements of HKFRS 9 'Financial Instruments' relating to the presentation of gains and losses on financial liabilities designated at fair value from 1 January 2017. As a result, the effect of changes in the fair value of those liabilities arising from changes in own credit risk is presented in other comprehensive income with the remaining effect presented in profit or loss. As permitted by the transitional requirements of HKFRS 9, comparatives have not been restated.

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

Transitional impact of HKFRS 9

With the exception of the provisions relating to the presentation of gains and losses on financial liabilities designated at fair value, which were adopted from 1 January 2017, the requirements of HKFRS 9 'Financial Instruments' will be adopted from 1 January 2018. HKFRS 9 includes an accounting policy choice to continue with HKAS 39 hedge accounting, which the group has exercised, although it will implement the revised hedge accounting disclosures required by the related amendments to HKFRS 7 'Financial Instruments: Disclosures'. The classification and measurement and impairment requirements are applied retrospectively by adjusting the opening balance sheet at the date of initial application, with no requirement to restate comparative periods. The group does not intend to restate comparatives.

The adoption of HKFRS 9 is expected to reduce net assets at 1 January 2018 by HK\$7,290m, with classification and measurement changes reducing net assets by HK\$4,674m, impairment reducing net assets by HK\$4,187m, and the resulting changes to deferred tax increasing net assets by HK\$1,571m. There is no material impact on the group's capital resources.

23 Statutory accounts

The information in this document is not audited and does not constitute the Bank's statutory accounts.

Certain financial information in this document is extracted from the financial statements for the year ended 31 December 2017, which were approved by the Board of Directors on 20 February 2018 and will be delivered to the Registrar of Companies and the Hong Kong Monetary Authority. The Auditor's Report was unqualified; did not include a reference to any matters to which the auditor drew any attention by way of emphasis without qualifying their report; and did not contain a statement under sections 406(2), 407(2) or (3) of the Hong Kong Companies Ordinance (Cap.622). The *Annual Report and Accounts 2017*, which include the financial statements, will be published on the Bank's website: www.hsbc.com.hk. A press release will be issued to announce the availability of this information.

24 Ultimate holding company

The Hongkong and Shanghai Banking Corporation Limited is an indirectly-held, wholly-owned subsidiary of HSBC Holdings plc, which is incorporated in England.

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